Prospera Credit Union

Consolidated Financial Statements
December 31, 2013
(expressed in thousands of dollars)

February 27, 2014

Independent Auditor's Report

To the Members of
Prospera Credit Union

We have audited the accompanying consolidated financial statements of Prospera Credit Union, which comprise the consolidated statement of financial position as at December 31, 2013 and the consolidated statements of income and comprehensive income, changes in members' equity and cash flows for the year then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

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Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Prospera Credit Union as at December 31, 2013 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Accountants

Prospera Credit Union

Consolidated Statement of Financial Position

As at December 31, 2013

(expressed in thousands of dollars)

	2013 $	2012 $
Assets		
Cash and cash equivalents	5,373	19,250
Interest bearing deposits with financial institutions	230,704	154,484
Loans to members (note 5)	2,196,277	2,106,749
Other assets (note 9)	3,523	3,480
Derivative financial instruments (note 23)	944	3,134
Investments (note 7)	25,952	16,182
Property, premises and equipment (note 8)	6,015	7,312
Intangibles (note 10)	3,242	3,268
Income taxes receivable	194	654
Deferred income tax assets (note 19)	1,512	1,438
TOTAL ASSETS	2,473,736	2,315,951
Liabilities		
Borrowings (note 11)	173,241	170,770
Member deposits (note 12)	2,178,512	2,029,488
Retirement benefit obligation (note 14)	6,538	8,437
Other liabilities	3,970	4,493
	2,362,261	2,213,188
Members' Equity		
Capital and reserves attributable to members		
Members' equity shares (note 13(c))	4,388	4,764
Retained earnings	109,555	101,535
Other reserves	(2,468)	(3,536)
	111,475	102,763
TOTAL LIABILITIES AND MEMBERS' EQUITY	2,473,736	2,315,951

Commitments and contingent liabilities (note 20)

Approved by the Board of Directors

_________________________ Director   _________________________ Director

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

Prospera Credit Union

Consolidated Statement of Income and Comprehensive Income

For the year ended December 31, 2013

(expressed in thousands of dollars)

	2013 $	2012 $
Interest income		
Loans	84,065	82,353
Interest bearing deposits with financial institutions and investments	5,896	5,729
	89,961	88,082
Interest expense		
Deposits	36,106	35,451
Borrowings	2,206	1,731
	38,312	37,182
Net interest income (note 15)	51,649	50,900
Loan impairment expense (note 5)	1,700	1,500
Net interest income after loan impairment expense	49,949	49,400
Other income (note 16)	12,257	11,590
Net interest income and other income	62,206	60,990
Non-interest expenses		
Salaries and employee benefits (note 17)	30,427	28,932
Occupancy	6,966	7,149
Administration	3,951	4,059
Other (note 18)	3,331	3,056
Depreciation and amortization	2,562	2,755
Data processing	2,167	2,046
Clearing charges	1,685	1,888
Communication and marketing	1,666	1,758
	52,755	51,643
Income before dividends on member deposit shares	9,451	9,347
Dividends on member deposit shares	425	817
Income before income taxes	9,026	8,530
Provision for (recovery of) income taxes (note 19)		
Current	995	562
Deferred	(119)	155
	876	717
Net income for the year	8,150	7,813
Other comprehensive (loss) income for the year		
Change in fair value of retained interests - net of taxes of $5 (2012 - $nil)	(30)	-
Changes related to defined benefit plans, net of taxes of ($213) (2012 - $301) (note 14(d))	1,761	(1,931)
Net unrealized loss on cash flow hedges - net of taxes of $142 (2012 - $146) (note 23)	(663)	(1,197)
	1,068	(3,128)
Comprehensive income attributable to members	9,218	4,685

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

Prospera Credit Union

Consolidated Statement of Changes in Members' Equity

For the year ended December 31, 2013

(expressed in thousands of dollars)

			Other reserves			
	Members' equity shares $	Retained earnings[3] $	Defined benefit plans[1,3] $	Cash flow hedges[2] $	Retained interest[2] $	Members' equity $
Balance - December 31, 2011	4,983	93,860	(2,654)	2,216	30	98,435
Net income and other comprehensive income	-	7,813	(1,931)	(1,197)	-	4,685
Dividends on members' equity shares	-	(138)	-	-	-	(138)
Share redemptions	(219)	-	-	-	-	(219)
Balance - December 31, 2012	4,764	101,535	(4,585)	1,019	30	102,763
Net income and other comprehensive income	-	8,150	1,761	(663)	(30)	9,218
Dividends on members' equity shares	-	(130)	-	-	-	(130)
Share redemptions	(376)	-	-	-	-	(376)
Balance - December 31, 2013	4,388	109,555	(2,824)	356	-	111,475

[1] Changes in other reserves related to defined benefit plans are not recyclable to net income.
[2] Changes in other reserves related to cash flow hedges and retained interest are recyclable to net income.
[3] Upon adoption of IAS 19 (revised 2011), the Credit Union immediately recognized in other reserves all pension adjustments recognized in other comprehensive income, which were recognized previously through retained earnings. As a result of this accounting policy change, the Credit Union transferred accumulated re-measurements of ($2,654) at January 1, 2012 and a further ($1,931) at December 31, 2012 from retained earnings to other reserves.

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

Prospera Credit Union

Consolidated Statement of Cash Flows

For the year ended December 31, 2013

(expressed in thousands of dollars)

	2013 $	2012 $
Cash flows from operating activities		
Net income for the year	8,150	7,813
Items not affecting cash		
Net interest income	(51,649)	(50,900)
Depreciation and amortization	2,562	2,755
Loan impairment expense	1,700	1,500
Provision for income taxes	972	540
Deferred income taxes	(119)	155
Net change in fair value of derivative financial instruments (note 23)	914	197
Amortization of service liability (note 6))	(29)	(69)
Loss on sale of property, premises and equipment (note 18)	5	14
	(37,494)	(37,995)
Net change in loans to members	(110,410)	(177,117)
Net change in member deposits	160,372	68,220
Interest received	88,933	88,520
Interest paid	(37,207)	(37,987)
Issuance of member deposit shares	225	237
Redemption of member deposit shares	(9,745)	(684)
Dividends paid	(2,402)	(977)
Change in other assets and retirement benefit asset	(43)	611
Net change in derivative financial instruments	471	360
Change in other liabilities and retirement benefit obligation	(335)	(1,773)
Income taxes paid	(293)	(1,997)
Income tax reduction related to dividends	23	22
Other items	(795)	(113)
	51,300	(100,673)
Cash flows from investing activities		
Investment in Central 1 term deposits	(121,203)	(50,000)
Proceeds from maturity of Central 1 term deposits	44,983	42,745
Increase in investments	(9,771)	(1,480)
Additions to property, premises, equipment and intangibles	(1,244)	(1,191)
	(87,235)	(9,926)
Cash flows from financing activities		
Proceeds from borrowed funds	44,985	89,959
Proceeds from securitization transactions	74,918	61,219
Repayments of borrowed funds	(89,998)	(48,000)
Repayments of secured borrowings	(7,471)	(2,188)
Redemption of members' equity shares	(376)	(219)
	22,058	100,771
Decrease in cash and cash equivalents	(13,877)	(9,828)
Cash and cash equivalents - Beginning of year	19,250	29,078
Cash and cash equivalents - End of year	5,373	19,250
Cash and cash equivalents consist of:		
Demand deposits and clearings with Central 1	3,459	(3,656)
Term deposits with Central 1 with less than 90 days to maturity	1,914	22,906
	5,373	19,250

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

(expressed in thousands of dollars)

1 General information

Prospera 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 "FIA"). The Credit Union's primary business activities include providing financial services to its members and the general public across British Columbia. It provides retail and business financial services through 16 branches, on-line banking and a contact centre.

The Credit Union is domiciled in Canada and its registered office is at #500 - 32071 S. Fraser Way, Abbotsford, British Columbia.

The consolidated financial statements have been approved for issue by the Board of Directors (the "Board") on February 20, 2014. The Board has the authority to amend the financial statements after issue.

2 Basis of presentation

a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") using applicable IFRS as well as the regulations of the FIA. The accounting policies applied in these consolidated financial statements are based upon IFRS effective for the year ended December 31, 2013, as issued and effective.

b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis, except for available-for-sale financial assets, financial assets and financial liabilities accounted for at fair value through profit or loss and all derivative financial instruments, which are measured at fair value.

c) Functional and presentation currency

These consolidated financial statements are presented in Canadian dollars, which is also the Credit Union's functional currency. The figures shown in the consolidated financial statements are expressed in thousands of dollars, unless otherwise stated.

d) Use of estimates and judgments

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

(expressed in thousands of dollars)

Information on significant areas of uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements are described in note 4.

3 Summary of significant accounting policies

a) Consolidation

The Credit Union consolidates investees when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

The Credit Union consolidates the following investees in which it has control as wholly owned subsidiaries. Its wholly owned subsidiaries are Prospera Insurance Agencies Ltd., Prospera Technologies Inc., 413297 B.C. Ltd., and Prospera Holdings Ltd.

Intercompany balances, and income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements. Intercompany losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. The integration of the subsidiaries into the consolidated financial statements is based on consistent accounting and valuation methods for similar transactions and other occurrences under similar circumstances.

b) Foreign currency translation

Transactions in foreign currencies are translated to the functional currency of the Credit Union at the exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between the amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in the foreign currency translated at the exchange rate at the end of the reporting period. Foreign currency differences arising on translation are recognized in the consolidated statement of income. Non-monetary items that are measured at historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary items in a foreign currency that are measured at fair value are translated using the exchange rates at the date when the fair value was determined.

c) Cash resources

Cash and cash equivalents include highly liquid balances with less than 90 days maturity from the original date of issuance. Interest bearing deposits with financial institutions include deposits with Central 1 Credit Union (“Central 1”) and restricted cash deposits held in custodian accounts for repayment on secured borrowings.

(expressed in thousands of dollars)

d) Financial assets and liabilities: categorization, measurement and recognition

i) Financial assets

Management determines the categorization of its financial assets at initial recognition. The Credit Union initially recognizes loans and receivables and deposits on the date that they are originated. All other financial assets, including assets designated at fair value through profit or loss ("FVTPL"), are recognized initially on the trade date at which the Credit Union becomes a party to the contractual provisions of the instrument. The Credit Union's financial assets are categorized as one of the following: financial assets at FVTPL, loans and receivables, financial assets available-for-sale ("AFS") and financial assets held-to-maturity ("HTM").

Financial assets at FVTPL

This category comprises financial assets classified as FVTPL and financial assets designated by the Credit Union as FVTPL upon initial recognition.

A financial asset is required to be classified as FVTPL if it is acquired principally for the purpose of selling it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivative financial instruments are also categorized as FVTPL unless they are designated and are effective as hedging instruments in a hedge accounting relationship. Gains and losses on assets classified as FVTPL are recorded in net income.

The Credit Union has not designated any assets as FVTPL. The Credit Union's financial assets classified as FVTPL consist of derivative financial instruments such as equity options and interest rate swaps related to securitized loans, index-linked deposit contracts, and economic hedging.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

1) those that the Credit Union intends to sell immediately or in the short term, which are classified as FVTPL, and those that the Credit Union upon initial recognition designates as FVTPL;

2) those that the Credit Union upon initial recognition designates as AFS; or

3) those for which the holder may not recover substantially all of its initial investment, for reasons other than credit deterioration.

Loans and receivables are recorded at fair value on initial recognition and subsequently at amortized cost using the effective interest method.

(expressed in thousands of dollars)

The Credit Union's loans and receivables principally consist of cash and cash equivalents, loans to members, interest bearing deposits with financial institutions, and other receivables.

Financial assets available-for-sale

AFS assets are those non-derivative financial assets that are designated as AFS or are not classified as FVTPL, not designated as FVTPL or do not qualify as loans and receivables. AFS assets are recorded at fair value. Subsequently, they are carried at fair value, unless they do not have a quoted market price in an active market and fair value is not reliably determinable, in which case they are carried at cost.

Unrealized gains and losses arising from changes in the fair value of AFS financial assets are recognized directly in equity, until the financial asset is derecognized or impaired. As a result of the derecognition or impairment of an AFS asset, the cumulative gain or loss previously recognized in equity is recognized in the consolidated statement of income.

Interest income on AFS assets is calculated using the effective interest method and is recognized in the consolidated statement of income. Dividends on AFS equity instruments are recognized in the consolidated statement of income when the Credit Union's right to receive payment is established.

The Credit Union's AFS assets consist of investments.

Financial assets held-to-maturity

HTM assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Credit Union's management has the positive intention and ability to hold to maturity, other than:

1) those that Credit Union upon initial recognition designates as FVTPL;

2) those that the Credit Union designates as AFS; and

3) those that meet the definition of loans and receivables.

These are initially recognized at fair value including direct and incremental transaction costs and measured subsequently at amortized cost, using the effective interest method. Interest on HTM assets is recognized in the consolidated statement of income.

The Credit Union's HTM assets consist of government backed securities.

(expressed in thousands of dollars)

ii) Financial liabilities

Management determines the categorization of its financial liabilities at initial recognition. The Credit Union initially recognizes financial liabilities (including liabilities designated at FVTPL) on the trade date at which the Credit Union becomes a party to the contractual provisions of the instrument. Financial liabilities are categorized as FVTPL or financial liabilities at amortized cost. Financial liabilities are derecognized when extinguished.

Financial liabilities at FVTPL

Upon initial recognition, financial liabilities are classified as FVTPL or are designated by the Credit Union as FVTPL.

A financial liability is required to be classified as FVTPL if it is incurred principally for the purpose of repurchasing it in the near term or if it is part of a portfolio of identified financial liabilities that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivative liabilities are also categorized as FVTPL unless they are designated and are effective hedging instruments in a hedge accounting relationship. Gains and losses on FVTPL financial liabilities are recorded in net income.

At December 31, 2013, the Credit Union has financial liabilities designated as FVTPL. The Credit Union's financial liabilities classified as FVTPL consist of equity linked derivatives, secured borrowings and other derivative liabilities.

Financial liabilities at amortized cost

Financial liabilities that are not classified as FVTPL fall into this category. Financial liabilities at amortized cost consist of amounts drawn on lines of credit, accounts payable, member deposits, secured borrowings, and member deposit shares. These are measured at fair value on initial recognition and subsequently at amortized cost using the effective interest method.

iii) Fair value of financial instruments

The best evidence of fair value at initial recognition is prices quoted in an active market. Fair values of financial instruments quoted in active markets are determined by reference to closing bid prices at the reporting date. If there is no active market for a financial instrument, the Credit Union establishes fair value using an appropriate valuation technique. These techniques principally include the use of recent arm's length transactions for investments in unquoted securities, discounted cash flow analysis for derivatives and third-party option pricing models for index-linked option contracts and other valuation techniques commonly used by market participants.

(expressed in thousands of dollars)

Fair values reflect the credit risk of the instruments and include adjustments to take account of the credit risk of the Credit Union and the counterparty as relevant. Fair value estimates obtained from models are adjusted for other factors, such as liquidity risk or model uncertainties, to the extent that the Credit Union believes a third-party market participant would take them into account in pricing a transaction. Fair values determined by applying valuation techniques utilize independent observable market inputs to the maximum extent possible.

iv) Impairment of financial assets

The Credit Union assesses, at each consolidated statement of financial position date, whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are recorded only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a “loss event”) and the loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Credit Union on non-market terms that the Credit Union would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, or other observable data relating to a group of assets such as conditions that correlate with defaults in the group.

Financial assets classified as loans and receivables

The Credit Union maintains an allowance for credit losses that, in management’s estimation, is considered adequate to provide for credit-related losses. The allowance for credit losses consists of individual and collective allowances. The individual allowance is determined on the basis of specific loans that, in management’s opinion, may not be fully collectible. The individual allowance is the amount required to reduce the carrying value of an impaired loan to its present value of estimated future cash flows discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment is the current effective interest rate determined under the contract at the time the loan becomes impaired.

For the purposes of a collective evaluation of impairment, the portfolio is grouped on the basis of similar credit risk characteristics. These characteristics are relevant to the estimation of future cash flows and historical loss experience which is adjusted on the basis of current observable data to reflect the effects of current conditions. Assets that are individually assessed for impairment and for which no individual allowances are recorded are included in a collective assessment of impairment.

(expressed in thousands of dollars)

The Credit Union adjusts its input to its collective allowance methodology on an ongoing basis, taking into account factors such as historical loss experience and adjusting for current observable data that did not impact the period which the historical loss experience was based on. Estimates of changes in future cash flows for groups of assets reflect and are directionally consistent with changes in related observable data from period to period (for example, bankruptcy, residential mortgage delinquency, or other factors indicative of changes in the probability of losses by the Credit Union and in their magnitude).

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 by adjusting the allowance account. The amount of the reversal is recognized in the consolidated statement of income in loan impairment expense.

Loans that were past due and either subject to collective impairment assessment or are individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans. In subsequent years, if the loan becomes past due again, this will be disclosed only if the loan is renegotiated.

The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Credit Union to reduce any differences between loss estimates and actual loss experience. When a loan is uncollectible, it is written off after all the necessary procedures have been completed and the amount of the final loss has been determined.

Assets classified as available-for-sale

A significant or prolonged decline in the fair value of an AFS equity security below its cost is considered objective evidence in determining whether the asset is impaired. An AFS debt instrument may be identified as impaired due to circumstances which can include actual delinquency in contractual payment of principal or interest and/or significant events which indicate there is doubt as to the collectibility of the principal or contractual interest. For designated AFS assets, if any such evidence exists, the cumulative loss, measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in the consolidated statement of income, is reclassified from equity and recognized in the consolidated statement of income.

If, in a subsequent period, the fair value of a debt instrument classified as AFS increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the consolidated statement of income, the impairment loss is reversed through the consolidated statement of income. Impairment losses recognized in the consolidated statement of income on equity instruments are not reversed.

(expressed in thousands of dollars)

Assets classified as held-to-maturity

A HTM debt instrument may be identified as impaired due to circumstances which can include actual delinquency in contractual payment of principal or interest and/or significant events which indicate there is doubt as to the collectibility of the principal or contractual interest. In the case of an impairment, the impairment loss is reported as a deduction from the carrying value of the investment and recognized in the consolidated statement of income.

e) Property held for resale

In certain circumstances, the Credit Union may take possession of property held as collateral as a result of foreclosure on loans that are in default. Foreclosed properties are classified as assets held for sale and are measured at the lower of the carrying amount and the fair value less costs to sell.

The Credit Union does not, as a rule, occupy repossessed properties for its business use. These assets are normally sold in a manner that maximizes the benefit to the Credit Union, the member and the member's other creditors, and may involve the use of realtors.

The Credit Union does not hold any properties that were acquired as a result of loan default or that are held for resale.

f) Derivatives and hedge accounting

Derivative financial instruments are financial contracts whose value changes in response to a change in a specified interest rate, exchange rate or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract. Derivative contracts usually have no initial net investment or a net investment which would be smaller than a non-derivative contract and are settled at a future date.

Derivatives are initially recognized at fair value on the date a derivative contract is entered into. They are subsequently re-measured at their fair value and reported as assets where they have a positive fair value or as liabilities where they have a negative fair value.

Derivatives may also be embedded in other financial instruments and are treated as separate derivatives when:

i) their economic characteristics and risks are not closely related to those of the host contract;

ii) a separate instrument with the same terms would meet the definition of a derivative instrument; and

iii) the host contract is not designated as FVTPL or classified as FVTPL. Changes in fair value on derivative financial instruments not qualifying for hedge accounting are recognized in interest income or expense as appropriate in the consolidated statement of income.

(expressed in thousands of dollars)

The Credit Union designates derivatives as either hedges of highly probable future cash flows attributable to a recognized asset or liability, or a forecasted transaction (cash flow hedge), or FVTPL derivatives in instances where the derivative does not qualify or has not been designated as a hedge in a hedge accounting relationship. The Credit Union periodically uses derivatives for economic hedging purposes to mitigate an identified financial instrument risk.

g) Cash flow hedges

The Credit Union uses hedge accounting for derivatives designated as cash flow hedges provided certain criteria are met. The Credit Union documents the relationship, at its inception, between hedged items and hedging instruments, as well as identifying the risk being hedged and its risk management objective and strategy for undertaking various hedge transactions. The Credit Union also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in the cash flows attributable to the hedged risk.

The effective portion of changes in the fair value of a derivative that is designated and qualifies as a cash flow hedge is recognized in the consolidated statement of changes in members' equity. The gain or loss relating to the ineffective portion is recognized immediately in the consolidated statement of income. Amounts accumulated in equity are reclassified to the consolidated statement of income in the periods when the hedged item affects profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, hedge accounting ceases and any cumulative gain or loss existing in equity at that time remains in equity and is recognized when the hedged forecast transaction is ultimately recognized in the consolidated statement of income. However, when a forecast transaction is no longer expected to occur, or when the hedged item expires or is sold, the cumulative gain or loss that was deferred in equity is immediately transferred to the consolidated statement of income.

h) Derecognition of financial instruments

Financial assets are derecognized when the contractual rights to receive the cash flows from these assets have ceased to exist or the assets have been transferred and substantially all the risks and rewards of ownership of the assets are also transferred. If the Credit Union has neither transferred nor retained substantially all the risks and rewards of the transferred financial asset, it assesses whether it has retained control over the transferred asset. If control has been retained, the Credit Union continues to recognize the transferred asset to the extent of its continuing involvement. If control has not been retained, the Credit Union derecognizes the transferred asset.

Financial liabilities are derecognized when they have been redeemed or otherwise extinguished.

(expressed in thousands of dollars)

The Credit Union, through securitizations, periodically transfers loans to independent third parties. Where the Credit Union's securitizations and other transfers of receivables do not result in a transfer of contractual cash flows of the receivables or an assumption of an obligation to pay the cash flows of the receivable to a transferee, the Credit Union has not derecognized the transferred receivables and has instead recorded a secured borrowing with respect to any consideration received.

For whole loan sales that result in a transfer of contractual cash flow the Credit Union derecognizes the assets sold. The Credit Union accounts for gains or losses in the consolidated statement of income. The amount of the gain or loss is based on the carrying value of the loans sold.

i) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to offset the recognized amounts with the same counterparty and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

j) Interest income and expenses

Interest income or expense for all interest-bearing financial instruments is recognized within interest income or interest expense in the consolidated statement of income using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Credit Union estimates future cash flows considering all contractual terms of the financial instrument but does not consider future credit losses.

The calculation of the effective interest method includes all fees and costs paid or received between parties to the contract that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Interest income and expenses presented in the consolidated statement of income include:

i) interest on financial assets and financial liabilities measured at amortized cost, calculated on an effective interest basis;

ii) interest on AFS investment securities calculated on an effective interest basis;

iii) the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period that the hedged cash flows affect interest income/expense;

(expressed in thousands of dollars)

iv) fair value changes in qualifying derivatives, including hedge ineffectiveness; and

v) gains or losses on economic hedges.

k) Fee and commission income

The accounting treatment for loan fees varies depending on the transaction. Fees that are considered to be adjustments to loan yield are recognized using the effective interest method. The effective interest method capitalizes fees and transaction costs on the consolidated statement of financial position and amortizes them to interest income over the expected life of the related loan. Mortgage prepayment fees are recognized in interest income when received, unless they relate to a minor modification to the terms of the mortgage, in which case the fees are recognized over the expected remaining term of the original mortgage using the effective interest method. Loan origination, restructuring and renegotiation fees for commercial loans are recorded as interest income over the expected term of the loan using the effective interest method. Commitment fees are recorded in interest income over the expected term of the loan, unless the loan commitment is not expected to be used in which case it is recorded to other income. Loan discharge and administration fees are recorded directly to other income when the loan transaction is complete.

Loan fees that are recognized using the effective interest method are included with loan balances in the consolidated statement of financial position.

Service charges and foreign exchange transaction fees are recognized on an accrual basis when the service is performed.

Commission income is earned on the sale of insurance policies and is recognized as at the related insurance policy's effective date. The Credit Union may receive additional commissions from insurance companies, which are recorded at the earlier of the period in which amounts can be reliably measured or the period in which the amounts are received.

Investment management fees, mutual fund fees and financial planning fees are recorded at the date of sale on an accrual basis or upon performance of services.

(expressed in thousands of dollars)

l) Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

m) Property, premises and equipment

i) Recognition and measurement

All premises and equipment used by the Credit Union are measured at historical cost less accumulated depreciation and accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

ii) Subsequent costs

Subsequent expenditures are included in the asset's carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Credit Union and the cost of the item can be reliably measured.

All other repair and maintenance costs are charged to the consolidated statement of income during the financial period in which they are incurred.

iii) Depreciation

Land is carried at cost and is not depreciated. Asset classes are further categorized for depreciation where significant differences in the estimated useful life of the various components of individually significant assets are identified. Depreciation is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

Leasehold improvements	3 to 10 years
Computer equipment	3 to 10 years
Office furniture	3 to 7 years
Equipment	3 to 7 years

The residual values and useful lives of premises and equipment are reviewed, and adjusted if appropriate, at each consolidated statement of financial position date. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

(expressed in thousands of dollars)

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the consolidated statement of income.

n) Intangibles

i) Computer software

Computer software is capitalized when the future economic benefit is expected to exceed a period of one year. Otherwise, software costs are expensed when incurred. Capitalized software costs are initially recognized at cost and amortized using the straight-line method over the expected useful life. The expected useful life ranges from 3 to 10 years.

o) Leased assets

In accordance with International Accounting Standards ("IAS") 17, *Leases*, the economic ownership of a leased asset is transferred to the lessee if the lessee bears substantially all the risks and rewards related to the ownership of the leased asset. In some cases, the lease transaction is not always conclusive, and management uses judgment in determining whether the lease is a finance lease arrangement that transfers substantially all the risks and rewards incidental to ownership. If this determination is positive, the related asset is then recognized by the lessee at the inception of the lease at an amount equal to the lower of its fair value and the present value of the minimum lease payments. A corresponding amount is recognized as a finance lease liability.

All of the Credit Union's lease agreements are classified as operating leases. Payments on operating lease agreements are recognized as an expense on a straight-line basis over the lease term. Associated costs such as maintenance and insurance are expensed as incurred.

p) Income tax

Income tax expense comprises current and deferred taxes. Current and deferred taxes are recognized in the consolidated statement of income except to the extent that they relate to items recognized directly in members' equity or in other comprehensive income.

i) Current income tax

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

(expressed in thousands of dollars)

ii) Deferred income tax

Deferred tax is recognized with respect to temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable income will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

q) Employee benefits

The Credit Union operates various pension plans. The plans are generally funded through contributions to trustee-administered funds determined by periodic actuarial calculations. The Credit Union has both defined benefit and defined contribution plans.

i) Defined benefit pension plans

A defined benefit pension plan typically defines an amount of a pension benefit that an employee will receive on retirement, usually dependent upon one or more factors, such as age, years of service and compensation. The actuarial and investment risk of a defined benefit plan are typically primarily the responsibility of the sponsor of the plan.

The Credit Union uses the projected unit credit method to determine the present value of its defined benefit pension obligations and the related current service cost and, where applicable, past service cost. The defined benefit obligation is calculated on an annual basis by the appointed independent actuary to the respective defined benefit plans. This requires the Credit Union to determine the benefit attributable to the current and prior periods and to make estimates about demographic and financial variables that will affect the ultimate cost of the benefit. The present value of the defined benefit obligation of the respective plan is determined by discounting the estimated future cash flow outflows using interest rates of high quality corporate bonds that are denominated in Canadian dollars, and that have terms to maturity approximating the terms of the respective related defined benefit plan liability.

For funded plans, the Credit Union recognizes the fair value of the plan assets in accordance with the requirements of IFRS 13 for fair value measurements. Financial instruments such as quoted equities are valued using closing prices.

(expressed in thousands of dollars)

The fair value of any plan assets is deducted from the present value of the defined benefit obligation in determining the deficit or surplus on an individual plan basis. If a plan surplus exists, the fair value of the plan assets recognized on the Credit Union's consolidated statement of financial position is limited to the amount from which the Credit Union can derive a future economic benefit.

The Credit Union recognizes the service cost of the respective plans in the consolidated statement of income. The service cost principally comprises the current service cost representing the increase in the present value of the defined benefit obligation from employee service in the current period and the past service cost representing the changes in the present value of the defined benefit obligation from a plan amendment or curtailment.

The Credit Union recognizes the net interest on the defined benefit liability (asset) directly in the consolidated statement of income.

Re-measurements of the defined benefit asset (obligation) are recognized immediately in other comprehensive income and are transferred into other reserves within the consolidated statement of changes in members' equity. Re-measurements principally consist of actuarial gains and losses, the return on plan assets excluding amounts incorporated into the net interest on the net defined benefit asset (obligation) and any change in the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit asset (obligation).

ii) Post-employment health care benefits

The Credit Union operates a post-employment health care benefit plan. The method of accounting, assumptions and the frequency of valuations are similar to those used for defined benefit pension plans.

iii) Defined contribution pension plans

For defined contribution plans, the Credit Union pays a specified flat rate for employer contributions. The Credit Union has no further payment obligations once the contributions have been paid. The contributions are recognized as an employee benefit expense on an accrual basis in the periods during which services are rendered by employees.

(expressed in thousands of dollars)

iv) Participation in multi-employer pension plan

The Credit Union provides defined retirement benefits to certain employees through a multi-employer plan administered by Central 1. Each member credit union is exposed to the actuarial risks of the other employers with the result that, in the Credit Union's opinion, there is no reasonable way to allocate any defined benefit obligations. The Plan has informed the Credit Union that it is not able to provide defined benefit information on a discrete employer basis as the investment records are not tracked by individual employer and each employer is exposed to the actuarial risks of the Plan as a whole. Accordingly, the Credit Union's participation in the Plan is accounted for as a defined contribution plan with contributions recorded on an accrual basis. The Credit Union has provided additional disclosure on the overall funding status of the multi-employer plan and future contribution levels in note 14(g).

r) Related parties

A related party is a person or an entity that is related to the Credit Union.

i) A person or a close member of that person's family is related to the Credit Union if that person:

1) has control or joint control over the Credit Union, with the power to govern the Credit Union's financial and operating policies;

2) has significant influence over the Credit Union, participating in financial or operating policy decisions, but not control over these policies; or

3) is a member of the key management personnel of the Credit Union. Key management personnel, consistent with the definition under IAS 24, *Related Party Disclosures*, are persons having authority and responsibility for planning, directing and controlling the activities of the Credit Union, directly or indirectly, including any director (whether executive or otherwise) of the Credit Union.

ii) An entity is related to the Credit Union if any of the following conditions apply:

1) The entity and the Credit Union are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

2) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

3) Both entities are joint ventures of the same third party.

4) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(expressed in thousands of dollars)

5) The entity is a post-employment benefit plan for the benefit of employees of either the Credit Union or an entity related to the Credit Union.

6) The entity is controlled or jointly controlled by a person identified in (i) above.

7) A person identified in (i)(1) above has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

s) Provisions

A provision is recognized if, as a result of a past event, the Credit Union has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

A provision for onerous contracts is recognized when the expected benefits to be derived by the Credit Union from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Credit Union recognizes any impairment loss on the assets associated with the contract.

t) Equity and non-equity shares

Upon opening an account at the Credit Union, new members are required to purchase a minimum of 25 Class A Membership equity shares (junior members - five shares). Class A Membership equity shares are redeemable on demand by the member. Periodically, members may purchase Class F, G, H or I Preferred shares, as authorized by the Board, which are redeemable at the end of the time periods stated for that particular class of share. Accordingly, these classes of shares are recorded as member deposits.

Class A Membership, Class C Investment, Class D Insured, Class E Equity, and Preferred shares of the Credit Union are not subject to guarantee by the Credit Union Deposit Insurance Corporation of British Columbia (“CUDIC”). No Class H or I Preferred shares are issued. Dividends may be declared annually on Class A Membership, Class C Investment, Class E Equity and Preferred shares at the discretion of the Board.

Members, periodically, as authorized by the Board, are permitted to purchase Class C Investment and Class E Equity shares. Redemption of Class C Investment and Class E Equity shares is subject to certain conditions and approval of the Board. Accordingly, they are recorded as members’ equity.

(expressed in thousands of dollars)

u) Current year changes in accounting policies

i) International Accounting Standards ("IAS") 1 Amendment, *Presentation of Items in Other Comprehensive Income*

IAS 1, *Presentation of Financial Statements*, was revised to require the format of the statement of comprehensive income to segregate comprehensive income items recycled to net income and the comprehensive income items not recycled to net income. The Credit Union has adopted the amendments to IAS1 effective January 1, 2013; however, there was no major change required to the presentation of other comprehensive income and the change did not result in any adjustments to other comprehensive income or comprehensive income. All items within other comprehensive income recycle to net income with the exception of changes related to defined benefit plans.

ii) IAS 19, *Employee Benefits*

IAS 19, (amended in 2011), amends certain accounting requirements for defined benefit plans and termination benefits. IAS 19 (revised 2011), effective January 1, 2013, requires the net defined benefit liability (asset) to be recognized on the consolidated statement of financial position without any deferral of actuarial gains and losses and past service costs as previously allowed. Past service costs are recognized in net income when incurred. Expected returns on plan assets are no longer included in post-employment benefits expense. Instead, post-employment benefits expense includes the net interest on the net defined benefit liability (asset) calculated using a discount rate based on market yields on high quality bonds. The consolidated statement of income and comprehensive income has been adjusted for the year ended December 31, 2012 to reflect the accounting changes for defined benefit plans, resulting in an increase of $262 to post-employment benefits expense and a provision for income taxes reduction of $35. Re-measurements consisting of actuarial gains and losses, the actual return on plan assets (excluding the net interest component) and any change in the asset ceiling are recognized in other comprehensive income. Upon adoption of IAS 19 (revised 2011), the Credit Union immediately recognized in other reserves all pension adjustments recognized in other comprehensive income, which were recognized previously through retained earnings. As a result of this accounting policy change, the Credit Union transferred accumulated re-measurements of ($2,654) at January 1, 2012 and a further ($1,931) at December 31, 2012 from retained earnings to other reserves. The Credit Union continues to recognize interest expense (income) on net post-employment benefits liabilities (assets) in employee benefits expense in the consolidated income statement.

IAS 19 (amended in 2011) clarified that benefits are classified as long-term employee benefits if payments are not expected to be made within the next 12 months. The Credit Union has reviewed the classification of its benefits and determined that no reclassifications between current and long-term benefits are required.

(expressed in thousands of dollars)

The standard requires termination benefits to be recognized at the earlier of when the entity can no longer withdraw the offer of the termination benefit or recognizes any related restructuring costs. Termination benefits that require future services are required to be recognized over the periods the future services are provided. This amendment required the Credit Union to change its accounting policy for termination benefits when future services are required.

iii) IFRS 13, *Fair Value Measurement*

IFRS 13, provides a single framework for measuring fair value. The measurement of the fair value of an asset or liability is based on assumptions that market participants would use when pricing the asset or liability under current market conditions, including assumptions about risk. The Credit Union adopted IFRS 13 on January 1, 2013 on a prospective basis. The adoption of IFRS 13 on a prospective basis as of January 1, 2013 did not require any adjustments to the valuation techniques used by the Credit Union to measure fair value and did not result in any measurement adjustments as at January 1, 2013. IFRS 13 does expand the disclosures of financial instruments and these additional disclosures have been presented in these financial statements.

iv) IFRS 10, *Consolidated Financial Statements*

IFRS 10, replaces the guidance on control and consolidation in IAS 27, *Consolidated and Separate Financial Statements*, and SIC-12, *Consolidation - Special Purpose Entities*. IFRS 10 requires consolidation of an investee only if the investor possesses power over the investee, has exposure to variable returns from its involvement with the investee and has the ability to use its power over the investee to affect its returns. Detailed guidance is provided on applying the definition of control. The accounting requirements for consolidation have remained largely consistent with IAS 27. The adoption of IFRS 10 on January 1, 2013 did not have any consequential impact on the Credit Union.

v) IFRS 12, *Disclosure of Interests in Other Entities*

IFRS 12, sets out the disclosure requirements for entities reporting under IFRS 10 and IFRS 11 and replaces the disclosure requirements currently found in IAS 28, *Investments in Associates and Joint Ventures*. The adoption of IFRS 12 on January 1, 2013 did not have any consequential impact on the Credit Union.

(expressed in thousands of dollars)

vi) IFRS 7, *Financial Instruments: Disclosures*

IFRS 7, has been amended to enhance disclosure requirements related to offsetting of financial assets and financial liabilities. The amendment does not change the current offsetting model in IAS 32 which only allows for the right of offset when the entity has a legally enforceable right of set-off and intends to either settle the asset and liability on a net basis or to realize the asset and settle the liability simultaneously. These new disclosures are intended to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US generally accepted accounting principles ("GAAP"). The adoption of IFRS 7 on January 1, 2013 resulted in additional disclosures to the Credit Union's consolidated financial statements.

a) Standards and interpretations issued but not yet effective

At December 31, 2013, a number of standards and interpretations, and amendments thereto, had been issued by the IASB, which are not effective for these consolidated financial statements. Those which are expected to have an effect on the Credit Union's consolidated financial statements are discussed below:

i) IFRS 9, *Financial Instruments*

IFRS 9 was issued in 2009 and addresses classification and measurement of financial assets. It replaces the multiple category and measurement models in International Accounting Standard ("IAS") 39, *Financial Instruments: Recognition and Measurement*, for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments. Such instruments are either recognized at fair value through profit or loss or, where recognition through profit or loss creates an accounting mismatch, at fair value through other comprehensive income.

Requirements for financial liabilities were added to IFRS 9 in 2010 and they mainly carried forward existing requirements in IAS 39, except that fair value changes due to credit risk for liabilities designated at fair value through profit or loss are generally recorded in other comprehensive income.

The Credit Union does not anticipate any changes to the measurement basis of its financial assets or financial liabilities as a result of these changes in accounting policy. In 2013 IFRS 9 was updated to remove the mandatory effective date and leave the date open pending finalization of other components of IFRS 9. Revisions to the impairment standards, and limited amendments to the classification and measurement of financial instruments are expected to be issued during 2014.

(expressed in thousands of dollars)

In November 2013 the IASB issued further amendments to IFRS 9 which introduced a new hedge accounting model. They are in the process of being reviewed for suitability for incorporation into the CICA Handbook. The amendments introduce significant changes that enable companies to better reflect their risk management activities through hedge accounting. The new standard results in a simplified hedge accounting model and it is not anticipated that any of Prospera's current hedging relationships will be impacted. The Credit Union will assess the impact of the new requirements as it relates to future derivative strategies prior to the effective date of implementation.

ii) IAS 32, *Financial Instruments: Presentation*

IAS 32, has been amended to clarify requirements for offsetting of financial assets and financial liabilities on the consolidated statement of financial position. The amendment does not change the current offsetting model in IAS 32 which only allows for the right of offset when the entity has a legally enforceable right of set-off and intends to either settle the asset and liability on a net basis or to realize the asset and settle the liability simultaneously. These new disclosures are intended to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US GAAP. The standard is effective for annual periods beginning on or after January 1, 2014 and must be applied retrospectively. The adoption of this standard is not expected to result in a change to the Credit Union's consolidated financial statements.

4 Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Credit Union's accounting policies. Changes in assumptions may have a significant impact on the financial statements in the period the assumptions changed. The principal areas involving a higher degree of judgment or complexity and/or areas which require significant estimates are described below:

a) Allowance for credit losses on loans to members

The Credit Union regularly reviews its loan portfolio for impairment. In determining whether an impairment loss should be recorded in the consolidated statement of income, the Credit Union makes judgments as to whether there is any observable data indicating an impairment trigger followed by a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of members in a group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed annually to reduce any difference between loss estimates and actual loss experience. Were the net present value of estimated cash flows to differ by +/-1%, the impairment loss is estimated to be $186 (2012 - $94) higher or lower.

(expressed in thousands of dollars)

b) Fair value of financial instruments

The fair values of financial instruments where no active market exists or where quoted prices are not otherwise available are determined using specific valuation techniques. In these cases, the fair values are estimated from observable data in respect of similar financial instruments or by using models. Where market observable inputs are not available, they are estimated based on appropriate assumptions. Where valuation techniques are used to determine fair values, they are validated and periodically reviewed by management. To the extent practical, models use only market observable data; however, areas such as credit risk (both the Credit Union's credit risk and counterparty risk) and correlations require management to make estimates.

c) Securitizations and derecognition of transferred financial instruments

The Credit Union transfers residential mortgages to an independent third party either directly or through an initial transfer to intermediary financial institutions that are eligible, authorized transferors approved by the third party.

Depending on the contractual arrangements, the Credit Union may not derecognize the securitized residential mortgages and may instead recognize a secured borrowing; recognize only a portion of the assets up to the Credit Union's remaining involvement in those assets; or may derecognize the assets and recognize, as separate assets or liabilities, any rights and obligations constituted or retained in the transfer. In assessing the derecognition criteria, management is often required to make judgments as to the extent to which cash flows are transferred and any continuing exposure to risks and rewards of the transferred receivables. The Credit Union has disclosed the accounting treatment for securitization transactions during the year in note 6.

d) Retirement benefits

The present value of retirement benefit obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. Any changes in these assumptions will impact the carrying amount of pension obligations.

One of the assumptions used in determining the net cost for retirement benefit plans is the discount rate. The Credit Union determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the pension obligations. In determining the appropriate discount rate, the Credit Union considers the interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating the terms of the related pension liability. Other key assumptions for pension obligations are based in part on current market conditions.

(expressed in thousands of dollars)

e) Income taxes

The Credit Union computes an effective tax rate which includes an evaluation of the current and future availability of the credit union deduction under the Canadian Income Tax Act and the small business income tax rate under the British Columbia Income Tax Act. The credit union deduction and the BC small business income tax rate apply to credit unions on taxable income of the credit union until such time as 4/3 of 5% of the amounts owing to members (including deposits, members shares and other borrowings) ("the maximum cumulative reserve") exceeds the cumulative taxable income that was previously subject to the credit union deduction (the "preferred rate amount") of the credit union. An estimate of future deposit, member borrowing, share and income growth is based on the modeling of the Credit Union's business plan, inclusive of economic indicators, and provides the basis in determining the availability of the credit union deduction and the credit union small business income tax rate.

In 2013, the Canadian Income Tax Act was amended to phase out the credit union deduction available to credit unions over five years. The phase out of the credit union deduction is effective for taxation years that end after March 20, 2013. The British Columbia government has yet to announce whether it will continue to allow credit unions to claim the BC small business income tax rate on qualifying credit union taxable income and as a result, the Credit Union has determined its effective income tax rate assuming the BC small business income tax rate will be available for 2013 and in the future on the basis that any change to the BC income tax rate affecting credit unions is not "substantively enacted" as at December 31, 2013.

The credit union deduction and the BC small business income tax rate is taken into account to determine the effective tax rate used in computing the income tax provision. However, the actual amounts of income tax expense do not become known until the filing with and assessment of the income tax return by the relevant tax authorities, which occurs subsequent to the issuance of the consolidated financial statements. To the extent that estimates differ from the final tax returns, net income would be affected in the subsequent year.

The Credit Union periodically assesses its liabilities and contingencies related to income taxes for all years open to audit based on the latest information available. For matters where it is probable that an adjustment will be made, the Credit Union records its best estimate of the tax liability including the related interest and penalties in the current tax provision.

(expressed in thousands of dollars)

5 Loans to members

	2013 $	2012 $
Retail		
Residential mortgages (note 6)	1,294,407	1,245,643
Personal loans	302,553	294,343
Commercial mortgages and loans	597,615	565,640
Net deferred transaction fees and related costs	3,493	2,864
Accrued interest	4,290	3,823
	2,202,358	2,112,313
Less: Allowance for credit losses	(6,081)	(5,564)
	2,196,277	2,106,749
Current	883,848	837,528
Non-current	1,312,429	1,269,221

Reconciliation of allowance for credit losses

	2013			2012
	Residential mortgages and personal loans $	Commercial mortgages and loans $	Total $	Total $
Balance - Beginning of year	3,377	2,187	5,564	5,717
Loan write-offs	(824)	(359)	(1,183)	(1,653)
(Decrease) increase in impairment allowance	(160)	1,860	1,700	1,500
Balance - End of year	2,393	3,688	6,081	5,564
Individual allowance	793	2,345	3,138	2,139
Collective allowance	1,600	1,343	2,943	3,425
Total allowance for credit losses	2,393	3,688	6,081	5,564

(expressed in thousands of dollars)

Loans to members individually impaired

A loan is considered impaired when a counterparty has not made a payment by the contractual due date and an individual allowance for credit has been established. The following table presents the carrying value of loans that are individually impaired:

	2013 $	2012 $
Retail		
Residential mortgages	1,227	1,520
Personal loan	799	341
Commercial mortgages and loans	2,868	2,351
	4,894	4,212

Loans past due but not impaired

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 because they are either:

(i) less than 90 days past due and there is no information that an impairment event has occurred; or

(ii) fully secured and collection efforts are reasonably expected to result in repayment.

Loans that are past due but not impaired are as follows:

	2013				2012
	1-29 days $	30-89 days $	90 days and greater $	Total $	Total $
Retail					
Residential mortgages	19,234	4,335	2,796	26,365	25,411
Personal loans	582	372	546	1,500	1,684
Commercial mortgages and loans	3,667	925	6,937	11,529	3,821
	23,483	5,632	10,279	39,394	30,916

The fair value of the collateral held by the Credit Union as security for impaired and past due loans was $75,426 (2012 - $77,452). The Credit Union has estimated the fair value of collateral based on an updated assessment of the security appraisals undertaken at the original funding assessment or management's knowledge of the fair value of security.

(expressed in thousands of dollars)

The principal collateral and other credit enhancements 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.

6 Loan securitizations and other transfers

Transferred financial assets that are not derecognized in their entirety

The Credit Union securitizes insured residential mortgages by participating in the National Housing Authority ("NHA") CMB and MBS programs. Through the programs, the Credit Union issues securities backed by residential mortgages that are insured against borrower's default. Once the mortgages are securitized, the Credit Union assigns underlying mortgages and/or related securities to Canada Mortgage and Housing Corporation ("CMHC").

(expressed in thousands of dollars)

During the year, the Credit Union entered into transfer agreements which were reviewed in order to determine whether the transfers of financial assets should result in all or a portion of the transferred mortgages being derecognized from its consolidated statement of financial position. The derecognition requirements include an assessment of whether the Credit Union's rights to contractual cash flows have expired or have been transferred or whether an obligation has been undertaken by the Credit Union to pay the cash flows collected on the underlying transferred assets over to a third party. The derecognition standards also include an assessment of whether substantially all the risks and rewards of ownership have been transferred.

The Credit Union has determined that an amount of $56,165 (2012 - $60,908) raised from securitization transactions during the year should be accounted for as a secured borrowing as the Credit Union did not transfer substantially all of the risks and rewards of ownership, principally because it did not transfer prepayment, interest and credit risk of the mortgages in the securitization. At December 31, 2013, the Credit Union had $115,090 (2012 - $73,365) of residential mortgages which had been securitized and included on the consolidated statement of financial position as the securitization transaction did not meet the requirements for derecognition. The total carrying amount of the original loans securitized as at December 31, 2013 was $137,898 (2012 - $81,732). These loans are held as security for the secured borrowing (note 11). As a result of the transactions, the Credit Union receives the net differential between the monthly interest receipts of the mortgages and the interest expense on the borrowings. The exposure to variability of future interest income and expense has been incorporated into the Credit Union's interest rate sensitivity calculations in note 21.

	Loans and receivables	
	2013 **$**	**2012** **$**
Carrying amount of assets	128,239	79,544
Carrying amount of associated liabilities	(128,239)	(79,544)
For those liabilities that have recourse only to the transferred assets:		
Fair value of assets	129,174	80,000
Fair value of associated liabilities	(128,257)	(80,811)
Fair value of associated derivatives	(201)	608
Net position	716	(203)

Transferred financial assets that are derecognized

For securitization transactions initiated prior to transition to IFRS, the Credit Union entered into an agreement with Central 1 to sell CMHC insured mortgages for participation in the Canada Mortgage Bond Program, which are used by Central 1 to create mortgage-backed securities sold to Canada Mortgage Housing Trust, an independent special purpose entity.

(expressed in thousands of dollars)

The Credit Union's retained interests in securitized loans consist of a right to receive future cash flows arising after the investors in the special purpose entity have received the return for which they contracted and from credit enhancement provided to the special purpose entity in the form of cash collateral accounts. The investors and special purpose entities, as holders of the securitized mortgages, have recourse only to a cash collateral account, the mortgages securitized and cash flows from the securitized mortgages. The investors and the third parties have no recourse to the Credit Union's other assets for failure of debtors to pay when due. The Credit Union's retained interests are subject to credit, prepayment and interest rate risks on the securitized mortgages.

During the year, the Credit Union entered into a whole loan sale agreement with Central 1 to sell CMHC insured mortgages. The Credit Union transferred all rights and obligations to the interest and principal from these mortgages and retains no prepayment, credit and interest rate risk. The Credit Union continues to service these mortgages and collect any associated cash flow.

The Credit Union received proceeds of $19,182 (2012 - $nil) from this whole loan sale and recognized a gain of $215 (2012 - $nil) in the consolidated statement of income.

Undiscounted cash flows to repurchase transferred assets that are derecognized

2013

	Maturity of continuing involvement						
	Total	**Within 3 months**	**3-6 months**	**6 months - 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Type of continuing involvement							
Securitized loans	18,145	-	-	-	-	18,145	-

2012

	Maturity of continuing involvement						
	Total	**Within 3 months**	**3-6 months**	**6 months - 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Type of continuing involvement							
Securitized loans	11,936	176	4,795	6,965	-	-	-

(expressed in thousands of dollars)

7 Investments

(expressed in thousands of dollars except for number of shares and value per share)

	2013 $	2012 $
Central 1 equity shares and accrued dividends	8,379	7,660
Government backed securities	6,265	3,296
Government backed securities - reinvestment account (note 11)	10,741	4,438
Other investments	567	788
	25,952	16,182
Current portion	932	82
Non-current portion	25,020	16,100

Included in Central 1 equity shares and accrued dividends are 88,587 Class E Central 1 shares issued with a par value of $0.01 each, redeemable at $100 each at the option of Central 1. There is no separately quoted market value for these shares and the fair value cannot be reliably determined. The timing of redemption of these shares cannot be determined, therefore, the range of reasonable fair value estimates is significant and the probabilities of the various estimates cannot be reasonably assessed. Therefore, they are recorded at cost.

8 Property, premises and equipment

	Office equipment $	Office furniture $	Leasehold improvements $	Land and buildings $	Automotive equipment $	Total $
Cost						
As at December 31, 2011	12,069	1,657	10,268	90	32	24,116
Additions	624	10	82	-	-	716
Disposals	(1,321)	-	(167)	-	-	(1,488)
As at December 31, 2012	11,372	1,667	10,183	90	32	23,344
Additions	482	15	162	-	-	659
Disposals	(202)	-	(7)	-	-	(209)
As at December 31, 2013	11,652	1,682	10,338	90	32	23,794
Depreciation and impairment						
As at December 31, 2011	8,449	1,432	5,349	-	32	15,262
Disposals	(1,310)	-	(164)	-	-	(1,474)
Depreciation charge for the year	1,222	59	963	-	-	2,244
As at December 31, 2012	8,361	1,491	6,148	-	32	16,032
Disposals	(202)	-	(2)	-	-	(204)
Depreciation charge for the year	1,051	39	861	-	-	1,951
As at December 31, 2013	9,210	1,530	7,007	-	32	17,779
Carrying amounts						
As at December 31, 2012	3,011	176	4,035	90	-	7,312
As at December 31, 2013	2,442	152	3,331	90	-	6,015

(expressed in thousands of dollars)

9 Other assets

	2013 $	2012 $
Prepaid expenses	2,286	2,139
Accounts receivable	1,237	1,189
Retained interests in securitized loans (note 6)	-	152
	3,523	3,480
Current portion	2,218	2,172
Non-current portion	1,305	1,308

10 Intangibles

	Software $
Cost	
As at December 31, 2011	8,989
Additions	475
Disposals	(315)
As at December 31, 2012	9,149
Additions	585
Disposals	-
As at December 31, 2013	9,734
Amortization	
As at December 31, 2011	5,685
Disposals	(315)
Amortization charge for the year	511
As at December 31, 2012	5,881
Disposals	-
Amortization charge for the year	611
As at December 31, 2013	6,492
Carrying amounts	
As at December 31, 2012	3,268
As at December 31, 2013	3,242

Remaining amortization of the carrying amounts as at December 31, 2013 is as follows:

	$
Within 1 year	642
1 - 5 years	2,032
After 5 years	568
	3,242

(expressed in thousands of dollars)

11 Borrowings

	2013 $	2012 $
Lines of credit	44,984	89,959
Secured borrowings (note 6)		
At amortized cost	15,079	21,758
At fair value	113,178	59,053
	173,241	170,770

Maturity date	Weighted average interest rate %	2013 $	2012 $
Due in 2013	1.53	-	89,959
Due in 2014	1.57	60,063	21,758
Due in 2016	2.38	38,820	30,434
Due in 2017	1.91	45,968	28,619
Due in 2018	1.75	28,390	-
		173,241	170,770
Current		60,063	89,959
Non-current		113,178	80,811

As of December 31, 2013, the Credit Union has two approved lines of credit totalling $154,924 (2012 - $190,924).

Security provided as collateral for the line of credit facilities is a general assignment of loans to members, accounts receivable and a demand debenture in favour of Central 1.

The secured borrowings arise from securitization transactions and are secured by specific pools of loans to members of $115,090 (2012 - $73,365) and $10,741 (2012 - $4,438) of government backed securities (notes 6 and 7).

(expressed in thousands of dollars)

12 Member deposits

	2013 $	2012 $
Term deposits	1,176,813	1,074,297
Demand deposits	603,242	565,672
Registered savings plans	374,458	355,386
Member deposit shares (note 13(b))	7,943	19,231
Deferred transaction costs	(211)	(259)
Accrued interest	16,267	15,161
	2,178,512	2,029,488
Current	1,624,650	1,396,501
Non-current	553,862	632,987

The Credit Union holds funds in segregated accounts for members investing in self-directed registered savings plans and mutual funds. The value of publicly traded investments is determined using the quoted market amounts at the year-end date. These funds are not included in the consolidated statement of financial position at December 31, 2013 and amount to $578,933 (2012 - $460,781).

13 Member deposit and members' equity shares

a) Authorized shares
(expressed in thousands of dollars except for value per share)

Unlimited number of shares with a par value and redemption value of $1 each:

Class A Membership voting equity shares
Class B Patronage voting equity shares
Class C Investment non-voting equity shares
Class D Non-equity shares

Unlimited Class E Equity voting, non-redeemable, non-cumulative shares with a par value of $1 each.

Unlimited Class F, G, H and I Preferred shares. Each class of Preferred share is issuable in Series (Series 1, 2 or 3). Each Series of each class can be offered in three, five, seven or 10-year terms. Each class of Preferred share is redeemable at the end of its term, is non-voting and is entitled to cumulative dividends at a rate set when issued.

(expressed in thousands of dollars)

b) Issued shares classified as member deposits (note 12) consist of the following:
(expressed in thousands of dollars except for number of shares)

	2013 $	2012 $
4,364,044 (2012 - 4,496,733) Class A Membership Equity shares	4,364	4,497
40,202 (2012 - 46,935) Class D Non-equity shares	40	47
2,626,564 (2012 - 11,951,858) Class F, Series 1-3 and Class G, Series 1, 3-to-10 year Preferred shares; the shares have cumulative dividends of 5.07% to 7.00%	2,627	11,952
Accrued dividends on Preferred shares	927	2,761
	7,958	19,257
Deferred transaction costs	(15)	(26)
	7,943	19,231

	2013 $	2012 $
Class A Membership equity shares issued in the year	225	237
Class A Membership equity shares redeemed in the year	(358)	(420)
Net redemptions in the year	(133)	(183)

The changes in Class D Non-equity shares and Class F and G Preferred shares relate to redemptions only as no shares were issued during the year (2012 - nil).

The Class F, Series 1 - 3 and Class G, Series 1, 3-to- 10-year Preferred shares are subject to redemption as follows:

	2013 $	2012 $
2013	-	11,260
2015	1,388	1,383
2016	2,166	2,070
Less: Accrued dividends	(927)	(2,761)
	2,627	11,952

(expressed in thousands of dollars)

c) Issued shares classified as members' equity consist of the following:
(expressed in thousands of dollars except for number of shares)

	2013 $	2012 $
4,145,836 (2012 - 4,521,621) Class C Investment equity shares	4,146	4,522
242,000 (2012 - 242,000) Class E Equity shares	242	242
	4,388	4,764

The changes in Class C Investment equity shares and Class E Equity shares relate to redemptions only as no shares were issued during the year (2012 - nil).

14 Pension and other retirement benefits

The Credit Union provides pension benefits to employees through defined contribution, defined benefit, and supplemental retirement and multi-employer defined benefit plans. Other post-retirement benefits including health care, dental benefits or cash alternatives are provided to eligible Credit Union employees upon or after retirement.

The defined benefit plans are registered in the province of British Columbia and governed by provincial regulations and practices. They are administered by a Board of Trustees.

The Credit Union operates four defined benefit plans in Canada. Three of these plans are not material in relation to the total of the defined benefit plans. The risk characteristics and assumptions are similar for all defined benefit plans; therefore, the information provided below relates to the four plans combined. The Credit Union funds the defined benefit plans and multi-employer defined benefit plans based on actuarially prescribed amounts. The unfunded supplemental retirement and non-pension benefits are paid by the Credit Union at the time of entitlement. The weighted average duration of the defined benefit obligation is 18.0 years.

Retirement benefits for the defined contribution plans are paid by the Credit Union on a monthly basis. The unfunded portion of the defined benefit obligation is $3,561 (2012 - $3,708). The accrued benefit obligation for the supplemental retirement plan is secured by an irrevocable letter of credit issued by the Credit Union in the amount of $2,640 (2012 - $2,613).

The accrued benefit obligation and plan assets were actuarially measured for accounting purposes as of December 31, 2013. The effective date of the last actuarial valuation report for funding purposes was December 31, 2012 and the effective date of the next required actuarial valuation report for funding purposes will be December 31, 2015.

(expressed in thousands of dollars)

a) Retirement benefit obligation

	2013 $	2012 $
Defined benefit obligation	(22,427)	(23,116)
Fair value of plan assets	15,889	14,679
Net retirement benefit obligation	(6,538)	(8,437)
Current portion	(329)	(319)
Non-current portion	(6,209)	(8,118)

The movement in the defined benefit obligation is as follows:

	2013 $	2012 $
Defined benefit obligation at January 1	23,116	19,650
Current service cost (net of employee contributions)	845	700
Interest costs	1,052	1,032
Re-measurements - experience	(210)	(225)
Re-measurements - demographic	512	-
Re-measurements - financial	(1,918)	2,882
Benefit payments	(970)	(923)
Defined benefit obligation at December 31	22,427	23,116

b) Fair value of plan assets

i) Movement in the fair value of plan assets is as follows:

	2013 $	2012 $
Fair value of plan assets at January 1	14,679	13,524
Interest income	658	666
Administration expenses	(48)	-
Re-measurements - financial	756	425
Changes in asset ceiling	(398)	-
Employer contributions	1,212	987
Benefit payments	(970)	(923)
Fair value of plan assets at December 31	15,889	14,679

(expressed in thousands of dollars)

ii) Funded plan assets comprise the following:

	Funded defined benefit plans	
	2013 %	**2012 %**
Asset category		
Equity securities	54	52
Debt instruments	37	37
Other assets	9	11
	100	100

Every three years, an actuarial valuation is performed to assess the financial position of the funded plans and the adequacy of the funding level. The most recent actuarial valuations, which were conducted as at December 31, 2012, indicated a going concern unfunded liability of $1,616 and a solvency deficiency of $5,692. The deficit is targeted to be financed over time through increased contributions. The pension regulator has determined the period during which the solvency deficit must be funded. As approved by the regulator, the plan solvency deficit is expected to be funded by December 2022. The Credit Union paid $1,212 (2012 - $987) for employer contributions to the plan in fiscal year 2013. As a result of the valuation, the employer contribution rates were determined to be 14.0% to 22.4% (2012 - 3.6% to 16.8%) per annum, depending on the planholder's age based on the pensionable earnings of the respective participating employees for the period from January 1, 2013 to December 31, 2015.

The investment policy relative to the majority of the funded plan assets reflects the Trustees' belief that the asset mix strategy should contain a combination of return enhancing and liability/duration matching investments to achieve the plan's investment return objectives and to protect the plan from significant fluctuations in the plan's solvency ratio.

As part of a de-risking strategy and considering the current funded position (based on solvency), the Trustees have adopted a formal transition schedule to shift to a long term asset mix. As each funding milestone is achieved over time, the Plan is increasingly de-risked by shifting its asset allocation gradually from equity to fixed income. The Trustees may, at their discretion, elect to accelerate the transition from fixed income relative to the schedule, by directing the Plan's periodic cash flows to long-term bonds.

Investments are diversified, such that the failure of any single investment would not have a material impact on the overall level of assets. The largest proportion of assets is invested in equities, although the plans also invest in properties, bonds and cash.

(expressed in thousands of dollars)

The expected return on plan assets is determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields as at the date of the consolidated statement of financial position. Expected returns on equity and property investments reflect long-term rates of return experienced in the respective markets. The actual return on plan assets for the year ended December 31, 2013 was $1,414 (2012 - $1,091).

c) The amounts recognized in the consolidated statement of income were as follows:

	2013 $	**2012 $**
Current service cost (net of employee contributions)	845	700
Interest costs	1,052	1,032
Administration costs	48	-
Interest income	(658)	(666)
Amortization of past service cost	-	4
Total included in employee benefits expense (note 17)	1,287	1,070

d) The amounts recognized in other comprehensive income (loss) were as follows:

	2013 $	**2012 $**
Re-measurements in the year	2,372	(2,232)
Changes in asset ceiling	(398)	-
Income tax recovery	(213)	301
Other comprehensive income (loss) related to defined benefit plans for the year	1,761	(1,931)

e) The principal actuarial assumptions used were as follows:

	2013 %	**2012 %**
Discount rate	4.98	4.48
Inflation rate	2.00	2.00
Future salary increases	3.00	3.00
Health care cost		
Extended health	8.00	8.00
MSP	4.00	4.00
Dental	3.00	3.00

For plans or portion of plans where indexing is used, future pension increase assumptions are based on 50% of the inflation rate.

(expressed in thousands of dollars)

Assumptions regarding future mortality are set based on actuarial advice in accordance with published statistics and experience. Mortality assumptions are based on the 1994 Uninsured Pensioner Mortality Table with projection for future mortality improvements for 20 years and a general adjustment factor of 90% to reflect increases in life expectancy since the publication date of the tables. The projection factors are in accordance with the published table Scale AA where annual improvements range from 0.4% to 2% for males and 0.3% to 1.8% for females.

The tables translate the average life expectancy of males to 20 years and females to 22 years for a pensioner retiring at age 65.

The sensitivity to changes in the weighted principal assumptions presented below was performed by changing each assumption individually. If an actual change occurs, it is likely that some of these assumptions are correlated, which could change the combined impact.

	2013 %	**2012** %
Discount rate		
Impact of: 1% increase	(3,217)	(3,645)
1% decrease	4,107	4,704
Inflation rate		
Impact of: 1% increase	985	1,102
1% decrease	(907)	(1,015)
Future salary increases		
Impact of: 1% increase	829	1,178
1% decrease	(739)	(1,037)
Medical/dental trends		
Impact of : 1% increase	133	127
1% decrease	(115)	(110)

f) Through its defined benefit plans, the Credit Union is exposed to a number of risks, the most significant of which are detailed below:

i) Investment risk

The defined benefit obligation is calculated with a discount rate. If the return on assets is lower than the discount rate, it will create a deficit.

ii) Interest rate risk

A variation in bond rates will affect the value of the defined benefit obligation.

(expressed in thousands of dollars)

iii) Longevity risk

A greater increase in life expectancy than the one predicted by the mortality table used will increase the defined benefit obligation

iv) Inflation risk

The defined benefit obligation is calculated taking into account an increase in the level of salary and future cost of living adjustments. If actual inflation is greater than expected, that would result in an increase in the defined benefit obligation.

g) Participation in multi-employer plan

The Credit Union participates in a plan for certain eligible employees which is administered by Central 1.

The Credit Union is one of several employers that participate in the BC Credit Union Employees' Pension Plan (the "Plan"). The Plan is a multi-employer contributory defined benefit pension plan governed by a 12-member Board of Trustees. The Board of Trustees is responsible for overseeing the management of the Plan, including investment of the assets and administration of the benefits. The Plan, as at December 31, 2012, had about 3,100 active employees and approximately 550 retired plan members. Total plan assets at December 31, 2013 are estimated at $407,000. Every three years, an actuarial valuation is performed to assess the financial position of the Plan and the adequacy of the funding level. The most recent actuarial valuation, which was conducted as at December 31, 2012, indicated a going concern unfunded liability of $32,330 and a solvency deficiency of $129,869. The deficit is targeted to be financed over time through increased contributions, collectively, from the participating employers. The pension regulator has determined the period during which the solvency deficit must be funded. As approved by the regulator, the plan solvency deficit is expected to be funded by October 2022. The Credit Union paid $1,474 (2012 - $1,156) for employer contributions to the Plan in fiscal year 2013. As a result of the valuation, the contribution rates were determined to be 14.8% (2012 - 9.5%) per annum for employer contributions based on the pensionable earnings of the respective participating employees and 2.5% to 9% per annum, depending on the planholder's age, for employee contributions for the period from October 1, 2013 to December 31, 2015. The contributions continue to be expensed as invoiced by the Plan.

The next actuarial valuation is scheduled for December 31, 2015 with results available in mid-2016. The Trustees of the Plan may, however, decide to conduct a valuation sooner than December 31, 2015.

h) Future contributions and benefit payments

The expected contributions and benefits payments for the year ending December 31, 2014 are as follows:

	$
Employer contributions	1,587
Employee benefits	(1,011)

(expressed in thousands of dollars)

15 Net interest income

	2013 $	2012 $
Interest income		
Cash and cash equivalents	46	28
Interest bearing deposits with financial institutions	4,517	3,846
Financial assets		
Cash flow hedges	876	1,588
Fair value through profit or loss	238	158
Held to maturity investments	219	109
Loans to members	84,065	82,353
	89,961	88,082
Interest expense		
Deposits	36,106	35,451
Borrowings		
Lines of credit	1,019	885
Secured borrowings	1,187	846
	38,312	37,182
Net interest income	51,649	50,900

16 Other income

	2013 $	2012 $
Service charges	4,986	5,106
Investment management	3,888	3,309
Insurance commissions	1,263	1,409
Foreign exchange	800	823
Loan fees	633	849
Other	472	94
Gain on securitization transactions	215	-
	12,257	11,590

(expressed in thousands of dollars)

17 Salaries and employee benefits

	2013 $	2012 $
Salaries	24,657	23,894
Benefits		
Other	2,852	2,608
Post-employment defined benefit plans	78	98
Pension costs		
Defined contribution plans	1,631	1,360
Defined benefit plans	1,209	972
	30,427	28,932

18 Other expenses

	2013 $	2012 $
Deposit insurance fees	1,359	1,168
Professional services	764	746
Other	513	453
Central 1 dues	369	376
Loan administration fees	321	299
Loss on sale of property, premises and equipment	5	14
	3,331	3,056

19 Income taxes

	2013 $	2012 $
Current tax expense	995	562
Deferred tax expense	(119)	155
	876	717

(expressed in thousands of dollars)

Reconciliation of effective tax rate

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate. The income tax expense differs from the amount that would be computed by applying the combined federal and provincial statutory income tax rates of 25.75% (2012 - 25%) to income before income taxes. The reasons for the differences are as follows:

	2013 $	2012 $
Computed tax expense	2,285	2,133
(Decrease) increase resulting from		
Preferred rate amount deduction for credit unions	(1,026)	(1,089)
Non-taxable items	7	16
Effect of tax rate changes and changes in income tax asset	(102)	193
Other	(288)	(536)
	876	717

The weighted average applicable tax rate was 9.7% (2012 - 8.6%). The rates reflect adjustments to the prior year tax return and provision adjustments due to more accurate information available at the time of filing the return.

Deferred income tax assets and liabilities analysis are as follows:

	2013 $	2012 $
Deferred income tax assets		
To be recovered within 12 months	195	(30)
To be recovered after more than 12 months	2,024	2,213
	2,219	2,183
Deferred income tax liabilities		
To be settled within 12 months	235	284
To be settled after more than 12 months	472	461
	707	745
Net deferred income tax assets	1,512	1,438

(expressed in thousands of dollars)

The movement in deferred tax assets and liabilities are:

	December 31, 2012 $	Recognized in profit or loss $	Recognized in other comprehensive income $	December 31, 2013 $
Deferred income tax assets				
Provision for credit losses	492	-	-	492
Deferred revenue	135	2	-	137
Retirement benefit obligation and severance accruals	1,109	142	(213)	1,038
Property, premises, equipment and software intangibles - differences between carrying amounts and undepreciated capital cost	354	98	-	452
Loss carry-forwards	58	(4)	-	54
Other	-	46	-	46
	2,148	284	(213)	2,219
Deferred income tax liabilities				
Prepaid loan expenses	550	146	-	696
Retained interest in securitizations	(95)	100	(5)	-
Other	255	(102)	(142)	11
	710	144	(147)	707
Net deferred income tax assets	1,438	140	(66)	1,512

(expressed in thousands of dollars)

	December 31, 2011 $	Recognized in profit or loss $	Recognized in other comprehensive income $	December 31, 2012 $
Deferred income tax assets				
Provision for credit losses	485	7	-	492
Deferred revenue	121	14	-	135
Retirement benefit obligation and severance accruals	863	(90)	336	1,109
Property, premises, equipment and software intangibles - differences between carrying amounts and undepreciated capital cost	293	61	-	354
Loss carry-forwards	45	13	-	58
	1,807	5	336	2,148
Deferred income tax liabilities				
Prepaid loan expenses	330	220	-	550
Retained interest in securitizations	(113)	18	-	(95)
Goodwill	-	-	-	-
Other	344	(43)	(46)	255
	561	195	(46)	710
Net deferred income tax assets	1,246	(190)	382	1,438

20 Commitments and contingent liabilities

Commitments

Leases

The Credit Union's premises are leased for varying terms and the majority of the leases are renewable at the end of the lease period at market rate. Lease payments included in occupancy expense amounted to $5,242 (2012 - $5,361). Current minimum annual payments are approximately $5,533 (2012 - $5,629) for each of the next five years and $13,743 (2012 - $18,272) in aggregate thereafter.

Letters of credit and other guarantees

In the normal course of business, the Credit Union has outstanding letters of credit issued on behalf of members totalling $8,892 (2012 - $9,847), which are secured by member term deposits or property mortgages.

Undrawn loan commitment to members

Refer to note 21.

(expressed in thousands of dollars)

Contingent liabilities

In the course of its business, various claims and legal proceedings may arise against the Credit Union. The Credit Union defends itself where appropriate and is currently of the opinion that it is likely to prevail; accordingly, no provision has been made in these consolidated financial statements.

21 Risk management

The Credit Union's risk management policies are designed to identify and analyze 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, products and emerging best practice.

Risk management is carried out by a number of delegated committees reporting to the Board. The Board provides written principles for risk tolerance and overall risk management, and management reports to the Board on compliance with the risk management policies of the Credit Union. In addition, the Credit Union maintains an internal audit function, which is responsible for independent 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 mortgages. The primary types of financial risk that arise from this activity are credit risk, liquidity risk and market risk.

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

Activity	Risk	Method
Fixed rate savings products and funding activities involving fixed rate instruments	Sensitivity to changes in interest rates	Asset-liability matching and periodic use of derivatives
Fixed rate mortgages	Sensitivity to changes in interest rates	Asset-liability matching and periodic use of derivatives
Index-linked deposit products	Sensitivity to changes in Canadian equity indices	Options
Foreign currencies	Sensitivity to changes in foreign currency	Asset-liability matching and investment limits

(expressed in thousands of dollars)

Credit risk

Credit risk is the risk of a financial loss occurring due to a Credit Union member's or counterparty's inability or refusal to fully honour the contractual obligations of a financial instrument. This risk results from being a party to a financial instrument with a counterparty. Allowances for credit losses are made for losses that have been incurred at the statement of financial position date. Significant changes in the economy of British Columbia, specifically the Greater Vancouver, Fraser Valley and Okanagan areas, or deteriorations in lending sectors that represent a concentration within the Credit Union's loan portfolio may result in losses that are different from those provided for at the statement of financial position date.

The classes of financial instruments to which the Credit Union is most exposed are loans to members, cash resources and derivatives. The following table presents the maximum exposure to credit risk of financial instruments including undrawn commitments of $279,891 (2012 - $290,858):

			2013	2012
Credit risk exposure	**Outstanding** $	**Undrawn commitments** $	**Total exposure** $	**Total exposure** $
Cash and cash equivalents	5,373		5,373	19,250
Interest bearing deposits with financial institutions	230,704		230,704	154,484
Residential				
Mortgages	1,294,407	14,415	1,308,822	1,273,466
Loans	109,920	171	110,091	92,398
Line of credit and overdraft	192,633	190,019	382,652	384,514
Commercial				
Mortgages	468,654	28,937	497,591	494,506
Loans	91,022	1,106	92,128	66,560
Line of credit and overdraft	37,939	45,243	83,182	85,040
Accrued interest on loans	4,290	-	4,290	3,823
Derivatives	944	-	944	3,134
Investments	25,952	-	25,952	16,182
Retained interest in securitized loans	-	-	-	152
Accounts receivable	1,237	-	1,237	1,189
Income taxes receivable	194	-	194	654
Total exposure	2,463,269	279,891	2,743,160	2,595,352

Management of credit risk 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 treasury activities that result in investments in cash resources. There is also credit risk in unfunded loan commitments. The overall management of credit risk is centralized in the Investment and Lending Committee, which reports to the Board, and the respective operating units of the Credit Union.

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.

(expressed in thousands of dollars)

The Investment and Lending Committee 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 emphasizes responsible lending in its relationships with members and establishes that loans are within the member's ability to repay, rather than relying exclusively on collateral.

Loans to members consist of $1,294,407 (2012 - $1,245,643) residential loans which are secured by residential property, with a further $183,647 (2012 - $205,584) secured personal loans. Loans to members also include $112,674 (2012 - $88,759) of unsecured loans, which principally consist of personal 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 residential 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.

For the retail loan portfolio (residential and consumer loans), the Credit Union's underwriting methodologies and risk modelling is member based rather than product based. The Credit Union reviews the member's capacity to repay the loan rather than relying exclusively on collateral, although it is an important mitigant of establishing credit risk. Decisions on consumer loans are based on an overall assessment of credit risk utilizing a scoring model that takes into account factors such as Beacon scores and debt levels relative to income.

The credit quality of the commercial loan portfolio for those loans that are neither past due nor impaired can be assessed by reference to the Credit Union's internal rating system. The Credit Union assesses the quality of commercial loans using an internal rating tool taking into consideration a number of factors, such as the security, the borrower's management performance, current and projected financial results and industry statistics related to the borrower's industry and utilizes the experience and judgment of the Credit department. Commercial loans are divided into segments based on the following rating system and are regularly reviewed and updated as appropriate:

Risk rating	Risk rating descriptions
1 - 2	Excellent to very good - account is identified to be low or normal risk, requires minimal staff oversight and has a low risk of default
3	Satisfactory - account has acceptable levels of risk with a potential for a heavier reliance on asset security. Staff maintain a certain level of oversight based on assessment factors and industry business practices
4 - 5	Less than satisfactory to poor - management involvement is required as account is identified to be of higher risk driven by a material adverse change, deterioration of the financial situation of the member or major security deficiency

(expressed in thousands of dollars)

The commercial loan portfolio for those loans that are neither past due nor impaired is as follows:

Risk rating	2013 $	2012 $
1 - 2	11,078	16,371
3	565,387	534,027
4 - 5	6,996	9,236
	583,461	559,634

Credit risk within the Treasury department 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 the Treasury department, which reports to the Investment and Lending Committee. The Treasury department managed assets consist of cash resources and interest bearing deposits with financial institutions held with Central 1.

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. To mitigate this risk, the Credit Union is required by the FIA to maintain a minimum liquidity threshold at all times, based on total members' deposits and non-equity shares. At December 31, 2013, the Credit Union's liquidity exceeded the required level. Included in cash and cash equivalents and interest bearing deposits with financial institutions are minimum liquidity threshold cash resources of $188,009 (2012 - $175,724). 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, securitizations and asset-liability maturity management techniques. Management monitors rolling 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 borrowing facilities of $154,924 as an integral part of its liquidity management strategy, as disclosed in note 11.

(expressed in thousands of dollars)

Cash flows payable under financial liabilities which represents the Credit Union's exposure to liquidity risk by remaining contractual maturities are as follows:

	Less than 1 year $	1 - 3 years $	4 - 5 years $	Total $
December 31, 2013				
Member deposits	1,624,650	522,515	31,347	2,178,512
Borrowings				
Money market loans	44,984	-	-	44,984
Secured borrowings	15,079	38,820	74,358	128,257
December 31, 2012				
Member deposits	1,396,501	537,320	95,667	2,029,488
Borrowings				
Money market loans	89,959	-	-	89,959
Secured borrowings	-	21,758	59,053	80,811

Market 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 consolidated statement of income may increase or decrease in response to changes in market interest rates. Accordingly, the Credit Union sets limits on the level of mis-match of interest rate repricing that may be undertaken, which is monitored by the Credit Union's Treasury department and reported to the Asset and Liability Committee ("ALCO"), which is responsible for managing interest rate risk.

In managing interest rate risk, the Credit Union relies primarily upon the use of asset-liability and interest rate sensitivity simulation models. Periodically, the Credit Union may enter into interest rate swaps to adjust the exposure to interest rate risk by modifying the repricing of the Credit Union's financial instruments. The Credit Union's derivative instruments are disclosed in note 23.

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 12-month period. Interest rate shock analysis is calculated in a similar manner to sensitivity analysis but involves a more significant change of 100 basis points or greater in interest rates. Sensitivity analysis and interest rate shock analysis are calculated on a monthly basis and are reported to the ALCO. Based on current differences between financial assets and financial liabilities as at December 31, 2013, the Credit Union estimates that an immediate and sustained 100 basis point increase in interest rates would increase net interest income by $752 (2012 - $1,787) over the next 12 months while an immediate and sustained 100 basis point decrease in interest rates would decrease net interest income by $1,127 (2012 - $2,363) over the next 12 months.

(expressed in thousands of dollars)

Other types of interest rate risk may involve basis risk. The risk of loss arising from changes in the relationship of interest rates that have similar but not identical characteristics, for example the difference between prime rates and the Canadian Deposit Offering Rate ("CDOR"), and prepayment risk (the risk of loss of interest income arising from the early repayment of fixed rate mortgages and loans) are also monitored on a regular basis and are reported to the ALCO.

The carrying amounts of interest-sensitive assets and liabilities are presented in the periods in which they next reprice to market rates or mature and are summed to show the interest rate and maturity gap.

The gap position presented below represents the position outstanding at the close of the business day and may change significantly in subsequent periods based on member behaviour and the application of the Credit Union's asset and liability management policies.

Assets

Fixed term assets, such as residential mortgage loans and consumer loans, are reported based on scheduled repayments.

Assets that are related to the Credit Union's prime rate or other short-term market rates are reported in the variable rate category.

Liabilities

Fixed rate liabilities, such as term deposits, are reported at scheduled maturity.

Interest bearing deposits on which the member interest rate changes with prime or other short-term market rates are reported within variable rate category.

(expressed in thousands of dollars)

Yields

2013

	Weighted average rate %	Variable rate $	Within 3 months $	3 months to 1 year $	1 to 5 years $	Over 5 years $	Non-interest sensitive $	Total $
Assets								
Cash and cash equivalents	1.16%	8,162	1,914	-	-	-	(4,703)	5,373
Interest bearing deposits with financial institutions	1.99%	-	6,000	23,000	201,704	-	-	230,704
Derivative financial instruments	0.02%	-	719	362	(137)	-	-	944
Loans to members	3.75%	622,547	55,507	204,099	1,271,210	41,219	1,695	2,196,277
Investments	2.01%	8,079	632	-	16,373	-	868	25,952
Other		-	-	-	-	-	14,486	14,486
		638,788	64,772	227,461	1,489,150	41,219	12,346	2,473,736
Liabilities and Members' Equity								
Borrowings	1.88%	-	44,971	15,079	113,178	-	13	173,241
Member deposits	1.64%	669,494	194,871	738,952	553,862	-	21,333	2,178,512
Other		-	-	-	-	-	121,983	121,983
				-				
		669,494	239,842	754,031	667,040	-	143,329	2,473,736
Statement of financial position mismatch		(30,706)	(175,070)	(526,570)	822,110	41,219	(130,983)	-
Notional amount of derivatives		-	(126,000)	-	126,000	-	-	-
Net mismatch		(30,706)	(301,070)	(526,570)	948,110	41,219	(130,983)	-

2012

	Weighted average rate %	Variable rate $	Within 3 months $	3 months to 1 year $	1 to 5 years $	Over 5 years $	Non-interest sensitive $	Total $
Assets								
Cash and cash equivalents	1.29%	-	22,906	-	-	-	(3,656)	19,250
Interest bearing deposits with financial institutions	2.12%	-	9,498	27,486	117,500	-	-	154,484
Derivative financial instruments	0.98%	-	-	-	3,134	-	-	3,134
Loans to members	3.81%	683,528	42,371	110,506	1,246,995	22,226	1,123	2,106,749
Investments	1.81%	7,578	-	-	7,734	-	870	16,182
Other	3.32%	152	-	-	-	-	16,000	16,152
		691,258	74,775	137,992	1,375,363	22,226	14,337	2,315,951
Liabilities and Members' Equity								
Borrowings	1.09%	-	89,998	-	80,811	-	(39)	170,770
Member deposits	1.72%	635,008	203,455	535,903	632,987	-	22,135	2,029,488
Other		-	-	-	-	-	115,693	115,693
				-				
		635,008	293,453	535,903	713,798	-	137,789	2,315,951
Statement of financial position mismatch		56,250	(218,678)	(397,911)	661,565	22,226	(123,452)	-
Notional amount of derivatives		-	(97,000)	-	97,000	-	-	-
Net mismatch		56,250	(315,678)	(397,911)	758,565	22,226	(123,452)	-

(expressed in thousands of dollars)

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 financial instruments for an extended period. Foreign currency denominated deposits are matched with foreign currency denominated liquidity to minimize any exposure. Foreign exchange revenues earned by the Credit Union are primarily generated by crystallized spreads on dollars exchanged with members.

22 Capital management

The FIA requires the Credit Union to maintain, at all times, a capital base which is adequate in relation to its business. Capital levels for credit unions in British Columbia are regulated pursuant to guidelines issued by the Financial Institutions Commission of British Columbia ("FICOM"). Minimum capital standards are based on a total capital to risk weighted assets ("RWA") ratio of 8%, along with a requirement that at least 35% of the capital base consist of retained earnings. The Credit Union met this requirement throughout 2013 and 2012. Capital is managed in accordance with policies established by the Board. Management regards a strong capital base as an integral part of the Credit Union's strategy. The Credit Union has a capital plan to provide a long-term forecast of capital requirements. All of the elements of capital are monitored throughout the year, and modifications of capital management strategies are made as appropriate.

The capital ratio is calculated by dividing total capital by RWA, which is the assets weighted according to relative risk (0% to 150%) as determined by FICOM's prescribed rules relating to on-statement of financial position and off-statement of financial position exposures.

The total capital is as follows:

	2013 $	2012 $
Equity shares	9,557	10,591
Retained earnings	108,979	96,551
Deferred income tax assets	(1,455)	(1,411)
50% of the Credit Union's proportion of retained earnings in CUDIC, Central 1 and Stabilization Central Credit Union as advised by FICOM	16,670	15,245
Deductions from capital	(855)	(731)
	132,896	120,245

(expressed in thousands of dollars)

23 Derivative financial instruments

The table below provides an analysis of the Credit Union's derivative-related credit exposure:

	2013		2012	
	Notional amount $	Fair value $	Notional amount $	Fair value $
Equity options	8,780	1,250	17,387	1,249
Interest rate swaps	156,000	(306)	97,000	1,885
		944		3,134

Notional amounts are the contract amounts used to calculate the cash flows to be exchanged; they do not represent credit or market risk exposure.

	Amounts offset			Amounts not offset	
	Gross liabilities $	Gross assets offset $	Net amounts presented $	Financial instruments $	Cash collateral pledge/ received $
December 31, 2013 - Financial assets					
Derivative assets	(871)	565	(306)	-	-
December 31, 2012 - Financial assets					
Derivative assets	-	1,885	1,885	-	-

Prospera is subject to an enforceable master netting arrangement in the form of an ISDA agreement with a derivative counterparty.

Fair values based on quoted market prices are not available for a significant portion of the Credit Union's derivative instruments. Consequently, fair values are derived using present value and other valuation techniques and may not be indicative of the net realizable values.

(expressed in thousands of dollars)

The following is a summary of the nature of derivative instruments utilized:

a) Interest rate swaps are transactions in which two parties exchange interest flows on a specified notional amount for a predetermined period, based on agreed upon fixed and floating rates. Notional amounts are not exchanged.

   The Credit Union hedges a portion of the interest rate risk that arises on variable interest cash flows on prime rate mortgages through interest rate derivatives. Interest income and expense include the release from other reserves of gains or losses relating to the effective portion of qualifying hedging derivatives designated as cash flow hedges either:

   i) as the hedged item is recorded in interest income (expense); or

   ii) when the forecasted cash flow of the hedged item is no longer probable.

   Any ineffectiveness in the hedging relationship is recorded directly in the consolidated statement of income.

   During the year ended December 31, 2013, $410 (net of tax of $88) (2012 - $512 (net of tax of $80)) was the effective portion of changes in fair value for cash flow hedges in the year. The amount transferred to the consolidated statement of income was $45 (net of tax of $10) (2012 - $138 (net of tax of $22)).

   Consolidated other comprehensive income contains $nil (2012 - $nil) in unrealized net gains on derivatives.

   From time to time, the Credit Union enters into derivative transactions to economically hedge certain business strategies that do not otherwise qualify for hedge accounting, or where hedge accounting is not considered economically feasible to implement. During the year ended December 31, 2013, ($914) (2012 - ($197)) was recorded in net interest income as unrealized changes in fair value of these derivatives. In addition, net interest income contains $530 (2012 - $862) in realized net gains of which $362 (2012 - $751) was released from other comprehensive income.

b) Index-linked call options are equity contracts to pay or receive cash flows based on the increase or decrease in the underlying index or security. The Credit Union utilizes index-linked option contracts in order to economically hedge interest expense on the equity index-linked deposits.

The fair value of all outstanding derivative contracts in a gain position, which takes into account credit risk without factoring in the impact of master netting agreements, totalled $1,250 as at December 31, 2013 (2012 - $3,134). The Credit Union manages this credit risk by dealing with counterparties with a minimum credit rating of “A”, and setting specific limits for investments with those counterparties, which are reviewed monthly.

(expressed in thousands of dollars)

24 Fair value of financial instruments

The Credit Union has estimated fair values taking into account changes in interest rates and credit risk that have occurred since the assets and liabilities were acquired. These calculations represent management's best estimates based on a range of methods and assumptions; since they involve uncertainties, the fair values may not be realized in an actual sale or immediate settlement of the instruments. Interest rate changes are the main cause of changes in the fair value of the Credit Union's financial instruments. The carrying value is a reasonable approximation of fair value for the Credit Union's cash and cash equivalents, demand deposits, and certain other financial assets and liabilities.

The fair values of financial instruments are as follows:

a) Interest bearing deposits with financial institutions

The fair value of interest bearing deposits with financial institutions is determined by discounting remaining contractual cash flows at current market interest rates offered for deposits with similar terms and risks.

b) Derivative financial instruments

The fair value of derivative instruments is determined by using quoted market benchmark rates from an independent source. The Credit Union uses a valuation method that includes discounted cash flows on the remaining contractual life of a derivative instrument, and valuation models that use observable market data.

c) Loans to members

In determining the fair value of loans to members, the Credit Union incorporates the following assumptions:

i) Fair values are determined by discounting remaining contractual cash flows at current market interest rates offered for loans with similar terms, adjusting for estimated prepayments expected.

ii) The total value of loans determined using the above assumption is reduced by the allowance for credit losses to determine the fair value of the Credit Union's loan portfolio.

d) Borrowings

The fair value of borrowings is determined by discounting remaining contractual cash flows at current market interest rates offered for borrowings with similar terms and risks.

(expressed in thousands of dollars)

e) Member deposits

In determining the fair value of member deposits, the Credit Union incorporates the following assumptions:

i) For fixed rate, fixed maturity deposits, the Credit Union discounts the remaining contractual cash flows, adjusted for expected redemptions, at market interest rates offered for deposits with similar terms and risks.

ii) For floating rate deposits, changes in interest rates have minimal impact on the fair value since deposits reprice to market frequently. On that basis, fair value is assumed to equal carrying value.

The following represents the approximate fair values of financial instruments of the Credit Union as at the statement of financial position date:

			2013			2012
	Carrying value $	Fair value $	Difference $	Carrying value $	Fair value $	Difference $
Financial assets						
Interest bearing deposits with financial institutions	230,704	230,829	125	154,484	155,914	1,430
Derivative financial instruments	944	944	-	3,134	3,134	-
Investments	25,952	25,952	-	16,182	16,182	-
Loans to members	2,192,784	2,208,085	15,301	2,103,885	2,117,242	13,357
Financial liabilities						
Borrowings	173,241	172,404	837	170,770	171,168	(398)
Member deposits	2,178,738	2,185,065	(6,327)	2,029,773	2,036,204	(6,431)

The following tables summarize the fair value of financial instruments which are accounted for at fair value on the Credit Union's consolidated statement of financial position. Fair value measurements are analyzed according to a fair value hierarchy of three levels, as outlined below. Observable inputs represent instances where market data is obtained from independent sources. Unobservable inputs are based on the Credit Union's own internal assumptions.

Level 1: Unadjusted market prices in active markets for identical assets and liabilities.

Level 2: Inputs, other than quoted prices included within Level 1, that are observable for the asset or liability either directly or indirectly. This level includes the majority of over the counter derivatives or certain monetary instruments.

Level 3: Entity level inputs which are not based upon market observable data.

(expressed in thousands of dollars)

	2013		
	Level 1 $	**Level 2 $**	**Level 3 $**
Financial assets			
Interest bearing deposits with financial institutions	-	230,829	-
Derivative financial instruments	-	944	-
Investments	-	17,006	8,946
Loans to members	-	2,208,085	-
Financial liabilities			
Borrowings	-	(172,404)	-
Member deposits	-	(2,185,065)	-
	-	99,395	8,946

	2012		
	Level 1 $	**Level 2 $**	**Level 3 $**
Financial assets			
Interest bearing deposits with financial institutions	-	155,914	-
Derivative financial instruments	-	3,134	-
Investments	-	7,734	8,448
Loans to members	-	2,117,242	-
Retained interests	-	-	152
Financial liabilities			
Borrowings	-	(171,168)	-
Member deposits	-	(2,036,204)	-
	-	76,652	8,600

The Credit Union has financial instruments classified as Level 3 in the fair value hierarchy and has provided an analysis of movements in Level 3:

	2013 $	**2012 $**
At January 1	8,600	9,262
Changes in fair value during the year through the consolidated statement of income	-	-
Changes in fair value during the year through consolidated other comprehensive income	(35)	-
Changes in Central 1 equity shares and other investments	498	(242)
Cash flows received during the year	(117)	(420)
At December 31	8,946	8,600

(expressed in thousands of dollars)

The following table shows the sensitivity of the Level 3 measurements to reasonable possible alternative assumptions which includes a 10% change in the discount and repayment rates:

	Reflected in profit or loss	
	Favourable changes $	Unfavourable changes $
December 31, 2013	-	-
December 31, 2012	20	12

The above favourable and unfavourable changes are calculated independently from each other. Correlations and diversification effects are not taken into account.

25 Related party disclosure

Related parties of the Credit Union include subsidiaries, associates, post-employment benefit plans, directors and other key management personnel ("key management"), close family members of key management and entities which are controlled, jointly controlled or significantly influenced, or in which significant voting power is held, by key management or their close family members.

a) Loans and deposits

The Credit Union provides banking services to key management and persons connected to them.

A number of transactions were entered into with key management in the normal course of business. All loans to directors, executive management and employees of the Credit Union are subject to the credit policies established for all members. Credit Union employees may receive special rates or other considerations with respect to loans at the Credit Union. Directors do not receive special rates or other considerations with respect to loans at the Credit Union.

(expressed in thousands of dollars)

No provisions or loan write-offs have been recognized in respect of loans given to related parties (2012 - $nil).

	2013 $	2012 $
i) Loans to related parties:		
Loans outstanding at January 1	8,805	8,797
Loans issued in the year	5,309	6,929
Loan repayments in the year	(6,735)	(6,921)
Loans outstanding at December 31	7,379	8,805
Interest income earned	258	297
ii) Deposits from related parties:		
Balance on deposit at January 1	2,972	3,038
Deposits received in the year	12,315	11,407
Deposits repaid in the year	(12,404)	(11,473)
Balance on deposit at December 31	2,883	2,972
Interest expense on deposits	51	55

b) Key management compensation

	2013 $	2012 $
Salary and other short-term employee benefits	3,648	3,653
Post-employment benefits	226	239
Other long-term benefits	-	5
	3,874	3,897