

## **MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING**

These consolidated financial statements have been prepared by the management of Ladysmith & District Credit Union (the "Credit Union") who are responsible for their reliability, completeness and integrity. The financial statements were prepared in accordance with requirements of the Financial Institutions Act of British Columbia and conform in all material respects with International Financial Reporting Standards. The financial information presented in the annual report is consistent with the consolidated financial statements.

Systems of internal control and reporting procedures are designed to provide reasonable assurance that financial records are complete and accurate so as to safeguard the assets of the Credit Union. These systems provide assurance that all transactions are authorized and proper records are maintained. Internal audit procedures provide management with the ability to assess the adequacy of these controls. In addition, they are reviewed by the Credit Union's external auditors.

The Board of Directors has approved the consolidated financial statements. The Audit Committee of the Board has reviewed the statements with the external auditors, in detail, and received regular reports on internal control findings. KPMG LLP, Chartered Accountants, the independent external auditors appointed by the membership, examined the consolidated financial statements of the Credit Union in accordance with Canadian generally accepted auditing standards. They have had full and free access to the management and staff of the Credit Union and the Audit Committee of the Board.

A handwritten signature in black ink, reading "John de Leeuw". The signature is written in a cursive style with a long horizontal flourish extending to the right.

John de Leeuw  
Chief Executive Officer



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## **INDEPENDENT AUDITORS' REPORT**

To the Members of Ladysmith & District Credit Union

We have audited the accompanying consolidated financial statements of Ladysmith & District Credit Union, which comprise the consolidated statements of financial position as at December 31, 2012, the consolidated statements of profit or loss and other comprehensive income, changes in members' equity and cash flows for the year ended then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these 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.

### *Auditors' 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 our 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, we consider 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 in our audit is sufficient and appropriate to provide a basis for our audit opinion.



Page 2

*Opinion*

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

*KPMG LLP*

A handwritten signature in black ink that reads 'KPMG LLP'. The signature is written in a cursive, slanted style. Below the signature is a long, horizontal, slightly curved line that tapers at both ends, resembling a signature flourish or a checkmark.

Chartered Accountants

March 18, 2013  
Victoria, Canada

# LADYSMITH & DISTRICT CREDIT UNION

## Consolidated Statements of Financial Position

Years ended December 31, 2012 and 2011

	Notes	2012	2011
<b>Assets</b>			
Cash and cash equivalents	5	\$ 7,396,163	\$ 5,040,463
Loans to members	9	113,987,990	107,889,650
Financial investments	6	8,085,218	8,602,502
Derivative financial instruments	7	495,991	697,518
Trade and other receivables	8	606,386	569,392
Income taxes receivable	15	-	34,612
Deferred income taxes	15	4,900	4,900
Property classified as held for resale	11	865,242	850,000
Premises and equipment	12	3,311,271	3,448,491
Intangible assets	12	187,634	206,137
		\$ 134,940,795	\$ 127,343,665
<b>Liabilities</b>			
Member deposits	13	\$ 127,124,013	\$ 119,545,813
Other liabilities	14	483,896	430,591
Income taxes payable	15	25,919	-
Deferred income taxes	15	80,611	177,572
		127,714,439	120,153,976
<b>Members' Equity</b>			
Accumulated other comprehensive income		462,994	778,924
Retained earnings		6,763,362	6,410,765
		7,226,356	7,189,689
		\$ 134,940,795	\$ 127,343,665

### SUBSEQUENT EVENT (NOTE 25)

The notes are an integral part of these consolidated financial statements

Signed on behalf of the Board of Directors by:



Board Chair



Audit Chair

# LADYSMITH & DISTRICT CREDIT UNION

## Consolidated Statements of Profit or Loss

Years ended December 31, 2012 and 2011

	Notes	2012	2011
<b>Financial Income</b>			
Interest on member loans		\$ 4,954,026	\$ 5,125,114
Cash resources and investments		651,901	731,043
		5,605,927	5,856,157
<b>Financial expense</b>			
Interest on member deposits		2,816,604	3,006,940
Interest on borrowed funds		172	30,808
		2,816,776	3,037,748
<b>Financial Margin</b>			
		2,789,151	2,818,409
Provision for impairment on loans to members		174,058	172,737
		2,615,093	2,645,672
<b>Other income</b>			
	17	1,520,597	1,583,106
Gain on disposal of assets		9,910	-
		1,530,507	1,583,106
<b>Operating expenses</b>			
	18	3,669,595	3,828,984
<b>Income from operations</b>			
		476,005	399,794
Distribution to members		62,807	68,705
<b>Income before income taxes</b>			
		413,198	331,089
<b>Provision for income taxes</b>			
Current	15	41,353	48,300
Future		19,248	2,676
		60,601	50,976
<b>Profit for the year</b>			
		\$ 352,597	\$ 280,113

The notes are an integral part of these consolidated financial statements

# LADYSMITH & DISTRICT CREDIT UNION

## Consolidated Statements of Profit or Loss and Other Comprehensive Income

Years ended December 31, 2012 and 2011

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<b>Profit for the year</b>	<b>\$ 352,597</b>	<b>\$ 280,113</b>
<b>Other comprehensive income:</b>		
<b>Items that will not be reclassified to profit or loss:</b>		
Net gains (losses) on revaluation of land and buildings	(50,067)	115,543
Income tax relating to items that will not be reclassified	6,674	(15,401)
	<b>(43,393)</b>	<b>100,142</b>
<b>Items that may be reclassified subsequently to profit or loss:</b>		
Net gains (losses) on derivatives designated as cash flow hedges	(315,072)	526,755
Income tax relating to items that may be reclassified	42,535	(71,111)
	<b>(272,537)</b>	<b>455,644</b>
<b>Other comprehensive (loss) income for the year, net of tax</b>	<b>(315,930)</b>	<b>555,786</b>
<b>Total comprehensive income for the year</b>	<b>\$ 36,667</b>	<b>\$ 835,899</b>

The notes are an integral part of these consolidated financial statements

# LADYSMITH & DISTRICT CREDIT UNION

## Consolidated Statements of Changes in Members' Equity

Years ended December 31, 2012 and 2011

	Accumulated Other Comprehensive Income			Retained Earnings	Total
	Cash Flow Hedges	Revaluation Reserve			
<b>Balance, January 1, 2011</b>	\$ 223,138	\$ -	\$ 6,130,652	\$ 6,353,790	
Profit for the year			280,113	280,113	
Net gains on derivatives designated as cash flow hedges, net of tax \$ 71,111	455,644	-	-	455,644	
Net gains on revaluation of land and building, net of tax \$ 15,401	-	100,142	-	100,142	
<b>Balance, December 31, 2011</b>	<b>678,782</b>	<b>100,142</b>	<b>6,410,765</b>	<b>7,189,689</b>	
Profit for the year	-	-	352,597	352,597	
Net losses on derivatives designated as cash flow hedges, net of tax \$ 42,535	(272,537)	-	-	(272,537)	
Net losses on revaluation of land and building, net of tax \$ 6,674	-	(43,393)	-	(43,393)	
<b>Balance, December 31, 2012</b>	<b>\$ 406,245</b>	<b>\$ 56,749</b>	<b>\$ 6,763,362</b>	<b>\$ 7,226,356</b>	

The notes are an integral part of these consolidated financial statements

# LADYSMITH & DISTRICT CREDIT UNION

## Consolidated Statements of Cash Flows

Years ended December 31, 2012 and 2011

	2012	2011
<b>Operating activities</b>		
<b>Profit for the year</b>	\$ 352,597	\$ 280,113
Adjustments to determine cash flows:		
Amortization of premises and equipment	105,567	111,666
Amortization of intangible assets	36,291	32,566
Provision for income taxes	41,353	48,300
Deferred income tax expense	19,248	2,676
Gain on disposal of assets	(9,910)	-
Provision for impairment losses on loans	174,058	172,737
Provision for impairment of property held for resale	-	144,666
Loss on revaluation of land and buildings	22,954	2,424
Changes in investment interest accruals	(293)	-
Changes in member deposit interest accruals	234,177	18,020
Changes in loans to members interest accruals	(29,825)	16,862
Hedge ineffectiveness on derivative financial instruments	22,418	(30,778)
Amortization of settlement gain on derivative financial instruments	(135,962)	(56,651)
	832,673	742,601
Proceeds on settlement of derivative financial instruments	-	215,907
Income taxes recovered (paid)	(47,822)	(165,129)
Change in trade and other receivables	(36,994)	11,401
Change in payables and accruals	53,305	(30,797)
<b>Total cash inflows from operating activities</b>	<b>801,162</b>	<b>773,983</b>
<b>Investing activities</b>		
Loans, net of repayments	(6,242,573)	(75,169)
Purchase of investments	(29,608)	(309,780)
Proceeds from sale/redemption of investments	557,095	-
Purchase of premises and equipment	(41,371)	(36,612)
Purchase of intangible asset	(17,788)	(27,494)
Improvements to property held for resale	(15,242)	(2,458)
<b>Total cash (outflows) from investing activities</b>	<b>(5,789,487)</b>	<b>(451,513)</b>
<b>Financing activities</b>		
Repayments of short-term borrowings	-	(3,000,000)
Deposits, net of withdrawals	7,344,025	4,846,647
<b>Total cash inflows from financing activities</b>	<b>7,344,025</b>	<b>1,846,647</b>
<b>Net increase in cash resources</b>	<b>2,355,700</b>	<b>2,169,117</b>
<b>Cash resources, beginning of year</b>	<b>5,040,463</b>	<b>2,871,346</b>
<b>Cash resources, end of year</b>	<b>\$ 7,396,163</b>	<b>\$ 5,040,463</b>

The notes are an integral part of these consolidated financial statements



# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### 1. REPORTING ENTITY

Ladysmith & District Credit Union 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 consolidated financial statements of the Credit Union as at and for the year ended December 31, 2012 comprise the Credit Union and its subsidiaries L.C.U. Insurance Agencies Ltd. and LDCU Financial Management Ltd. (together referred to as the “Credit Union”).

L.C.U. Insurance Agencies Ltd. (“the Insurance Company”) is incorporated under the Companies Act and its operations are subject to the Insurance Council of British Columbia.

LDCU Financial Management Ltd. (“the Financial Management Company”) is incorporated under the Companies Act and its operations are subject to the Financial Institutions Act of British Columbia.

The Credit Union provides a broad range of products and services to members including mortgages, personal and commercial loans, chequing and savings accounts, term deposits, registered saving and retirement products, automated banking machines, debit and credit cards, and telephone and internet banking.

The Insurance Company offers ICBC Autoplan and driver licensing services, as well as a comprehensive variety of insurance products for home, business, vehicle, marine, and travel purposes.

The Financial Management Company is recently incorporated with the intent of offering a variety of wealth management services at a future date.

The Credit Union and its subsidiaries are domiciled in Canada and serve members in Ladysmith, British Columbia and the surrounding area. The address of the Company’s registered office is 330 First Avenue, Ladysmith, British Columbia.

These financial statements have been authorized for issue by the Board of Directors on March 18, 2013.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### 2. BASIS OF PREPARATION

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

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

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Credit Union's accounting policies. Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 4.

### 3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, unless otherwise indicated. The accounting policies have been applied consistently by the Credit Union's subsidiaries.

#### a) Principles of consolidation

The financial statements of the wholly-owned subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Intercompany balances and any unrealized income and expenses arising from intercompany transactions are eliminated in preparing the consolidated financial statements.

#### b) Cash and cash equivalents

Cash and cash equivalents include cash on hand and demand deposits held at Central 1 Credit Union ("Central 1"). Cash and cash equivalents are classified as loans and receivables and are carried at amortized cost, which approximates fair value due to their short-term nature.

#### c) Liquidity terms

Deposits held for liquidity purposes with Central 1 are classified as loans and receivables and are initially measured at fair value plus transaction costs that are directly attributable to their acquisition. Subsequently they are carried at amortized cost using the effective interest method which approximates fair value.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### **Financial investments**

These instruments are classified as available-for-sale and are initially recognized at fair value plus transaction costs that are directly attributable to their acquisition. 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.

Changes in fair value, except for those arising from interest calculated using the effective interest rate, are recognized as a separate component of other comprehensive income. Dividend income is recognized in profit or loss when the Credit Union becomes entitled to the dividend.

Where there is a significant or prolonged decline in the fair value of an equity instrument which constitutes objective evidence of impairment, the full amount of the impairment, including any amount previously recognized in other comprehensive income, is recognized in net income.

On sale, the amount held in accumulated other comprehensive income associated with that instrument is removed from equity and recognized in profit or loss.

### **d) Derivative financial instruments**

The Credit Union uses interest rate swaps to hedge its exposure to interest rate risks arising from operational and financing activities. The Credit Union does not hold or issue derivative financial instruments for trading purposes.

Derivative financial instruments are recognized initially at fair value. Subsequent to initial recognition, derivative financial instruments are measured at fair value. Recognition of the gain or loss on remeasurement to fair value follows the policy outlined in Note 3 e).

### **e) Hedges**

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

The Credit Union manages interest rate risk through interest rate swaps. These derivatives are carried at fair value and are reported as assets where they have a positive fair value and as liabilities where they have a negative fair value, in both cases shown on the Statement of Financial Position.

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

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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

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

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

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

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

### **f) Loans to members**

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

Member loans are initially measured at fair value, and inclusive of transaction costs incurred. Member loans are subsequently measured at amortized cost, being the cost of the loan on initial recognition less principal repayments, accumulated amortization using the effective interest rate method, and impairment losses.

Loans to members are reported at their recoverable amount representing the aggregate amount of principal, less any allowance or provision for impaired loans plus accrued interest.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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Loan application and origination fees, including commitment, renewal, and renegotiation fees, are considered to be adjustments to loan yield, and are deferred and amortized to loan interest income over the term of the loans using the effective interest method.

### **Impaired loans**

All loan assets are subject to recurring review and assessed for possible impairments. Impairment of loans is recognized when objective evidence is available that a loss event has occurred.

If there is objective evidence that an impairment loss has occurred, the amount of the loss is measured as the difference between the loan's carrying amount and the present value of expected cash flows. The present value of the estimated future cash flows is discounted at the loan's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralized loan reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

Impairment losses are recognized in profit and loss. The carrying amount of loans is reduced through use of an allowance for impairment account.

The Credit Union considers evidence of impairment at both a specific and a non-specific collective level.

#### **i) Specific provision**

The Credit Union assesses whether objective evidence of impairment exists for loans that are individually significant. If objective evidence exists indicating impairment, a specific provision for impairment is recorded. All bad debts are written off against the specific provision in the period in which they are classified as not recoverable. If no provision had been recognized, the write offs are recognized as expenses in profit or loss.

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

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### ii) Collective provision

Loans for which no specific individual impairment provision exists, are included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. The expected future cash outflows for a group of financial assets with similar credit risk characteristics are estimated based on a variety of factors including historical loss experience, known risks in the portfolio, current economic conditions and relative changes in member credit scores and bankruptcy navigator indices. All bad debts are written off against the collective provision in the period in which they are classified as not recoverable. If no provision had been recognized, the write offs are recognized as expenses in profit or loss.

### g) Derecognition of financial assets and liabilities

Financial assets are derecognized only when the contractual rights to receive cash flows from the assets have expired or transferred and either all of the risks and rewards of ownership have been substantially transferred; or the risks and rewards of ownership have not been retained nor substantially transferred and control has not been retained. Financial liabilities are derecognized when they are extinguished, that is, when the obligation is discharged, is cancelled or expires.

### h) Premises and equipment

#### i) Equipment

Equipment is initially recorded at cost and subsequently measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset.

Depreciation is calculated over the depreciable amount, which is the cost of an asset, or other amount substituted for cost, less its residual value. Depreciation is recognized in profit or loss and is provided on a straight-line basis sufficient to write off the net cost of each asset over its estimated useful life as follows:

Furniture, fixtures and equipment	2 to 10 years
Vehicles	3 years

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

#### ii) Premises

Premises are measured initially at cost including transaction costs. Transaction costs include transfer taxes, professional fees for legal services, initial leasing commissions to bring the premises to the condition necessary for it to be capable of operating and similar costs. The carrying amount also includes the cost of replacing part of an existing property at the time

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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the cost is incurred if the recognition criteria are met. Depreciation is recognized in profit or loss and is provided on a straight-line basis sufficient to write off the net cost of each asset over its estimated useful life of 15 to 30 years. Land is not depreciated.

Subsequent to initial recognition, premises are stated at the revalued amount at each reporting date. Any surplus arising on revaluation is recognized in other comprehensive income except to the extent that surpluses reverse a previous revaluation deficit on the same asset recognized in profit or loss, in which case the credit to that extent is recognized in profit or loss. Any deficit on revaluation is recognized in profit or loss except to the extent that it reverses a previous revaluation surplus on the same asset, in which case the debit to that extent is recognized in other comprehensive income.

Fair value is determined based on available market evidence at the reporting date. The fair value of properties is based on valuations by a combination of independent appraisers and management estimates.

Management regularly undertakes a review of its premises revaluation between appraisal dates to assess the continuing validity of the underlying assumptions such as cash flow and capitalization rates. These assumptions are tested against market information obtained from independent industry experts. Expenditures with a future economic benefit to the Credit Union, are added to the carrying amount of properties. Repairs and maintenance expenditures are expensed when incurred.

When parts of an item of premises and equipment have different useful lives, they are accounted for as separate items (major components) of premises and equipment. Gains and losses on disposal of an item of premises and equipment are determined by comparing the proceeds from disposal with the carrying amount of premises and equipment, and are recognized net within other income in profit or loss.

The cost of replacing a part of an item of premises and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Credit Union, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of premises and equipment are recognized in profit or loss as incurred.

### **i) Intangible assets**

Intangible assets are initially recorded at cost and are subsequently measured at cost less accumulated amortization and accumulated impairment losses.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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Amortization is recognized in profit or loss and is provided on a straight-line basis over the estimated useful life of the intangible assets as follows:

Core banking system	10 years
Website	5 years
Other computer software	1 to 5 years

### j) Impairment

#### i) Financial assets

Impairment losses on loans and receivables are discussed in Note 3 f). Impairment losses on available-for-sale investment securities are recognized by transferring the cumulative loss that has been recognized in other comprehensive income, and presented in unrealized gains/losses on available-for-sale financial assets in equity, to profit or loss. The cumulative loss that is removed from other comprehensive income and recognized in profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

#### ii) Non-financial assets

The Credit Union's non-financial assets are subject to impairment tests whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. If any such indication exists, then the asset's recoverable amount is estimated. The recoverable amount of an asset or cash-generating unit is the higher of its value in use and fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit", or "CGU").

The Credit Union's corporate assets do not generate separate cash inflows. If there is an indication that a corporate asset may be impaired, then the recoverable amount is determined for the CGU to which the corporate asset belongs.

If the non-financial assets are considered to be impaired, the impairment to be recognized equals the amount by which the carrying value of the asset exceeds its recoverable amount, and the asset is written down accordingly.

Impairment charges are included in profit or loss, except to the extent they reverse gains previously recognized in other comprehensive income.



# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### **k) Property classified as held for resale**

Assets that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. Immediately before classification as held for sale, the assets, or components of a disposal group, are remeasured in accordance with the Credit Union's accounting policies. Thereafter, generally the assets, or disposal group, are measured at the lower of their carrying amount and fair value less cost to sell. Impairment losses on initial classification as held for sale and subsequent gains or losses on remeasurement are recognized in profit or loss. Gains are not recognized in excess of any cumulative impairment loss.

### **l) Income taxes**

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

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

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for the financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantially enacted at the reporting date.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be utilized.

### **m) Member deposits**

All member deposits are classified as other financial liabilities and are initially measured at fair value, net of any transaction costs directly attributable to the issuance of the instrument.

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

### **n) Other financial liabilities**

Liabilities for trade creditors, accruals for wages and benefits payable, deferred revenue in respect of loan application fees and other sundry payables and accruals are classified as other financial liabilities. Other financial liabilities are initially measured at fair value net of any transaction costs directly attributable to the issuance of the instrument and subsequently carried at amortized cost using the effective interest rate method.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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**o) Employee benefits**

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Credit Union has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee, and the obligation can be estimated reliably.

The Credit Union participates in a Group Registered Savings Plan, recognizing contributions as an expense in the year during which services are rendered by employees. The Credit Union has no legal or constructive obligation to pay further amounts beyond these contributions.

**p) 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 the risks specific to the liability. The unwinding of the discount is recognized as finance cost.

**q) Members' shares**

Members' shares issued by the Credit Union are classified as other liabilities and are carried at amortized cost.

**r) Distributions to members**

Dividends on member shares classified as other liabilities are recognized in profit or loss.

**s) Revenue recognition**

**Loan interest**

Interest on loans is recognized on an amortized cost basis, being the cost of the loan on initial recognition less principal repayments, accumulated amortization using the effective interest rate method and impairment losses. The effective interest rate is the rate that exactly discounts the estimated future cash payments through the expected life of the loan to the net carrying amount of the loan. Interest is recognized on an accrual basis.

**Revenue from services rendered**

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

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### **Dividends**

Dividends from investments are recognized in profit or loss when the right to receive the dividend has been established.

### **Commissions**

Revenue is recognized in profit or loss on an accrual basis upon the provision of services from acting in the capacity of an agent rather than as the principal in a transaction.

### **t) Foreign currency translation**

On initial recognition, all foreign currency transactions are recorded at the exchange rate prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are subsequently measured and translated into Canadian dollars at the rates prevailing on the reporting date. Exchange differences resulting from differences in exchange rates at the reporting date and initial recognition are recorded in profit and loss.

### **u) Standards, amendments and interpretations not yet effective**

Certain standards, amendments to standards, and interpretations, have been published that are mandatory for the Credit Union accounting periods beginning on or after January 1, 2013. Early adoption is permitted.

The Credit Union has chosen not to implement early adoption of the following relevant standards, amendments to standards and interpretations;

- i)** IFRS 9 *Financial Instruments* is part of the IASB's wider project to replace IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets, amortized cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The standard is effective for annual periods beginning on or after January 1, 2015. The Credit Union is in the process of evaluating the impact of the new standard.
- ii)** IFRS 13 *Fair Value Measurement* defines fair value, provides guidance on the measurement of fair value, and requires disclosures about fair value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The standard is effective for annual periods beginning on or after January 1, 2013. The Credit Union is in the process of evaluating the impact of the new standard.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### v) **Comparatives**

Where appropriate, amounts shown for prior periods have been reclassified to facilitate comparison.

### **4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS**

The Credit Union makes estimates and assumptions about the future that affect the reported amounts of assets and liabilities. Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions.

The effect of a change in an accounting estimate is recognized prospectively in profit or loss in the period of the change, if the change affects that period only; or in the period of the change and future periods, if the change affects both.

Estimates and assumptions that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

#### **Fair value of financial instruments**

The Credit Union determines the fair value of financial instruments that are not quoted in an active market, using valuation techniques. Those techniques are significantly affected by the assumptions used, including discount rates and estimates of future cash flows. In that regard, the derived fair value estimates cannot always be substantiated by comparison with independent markets and, in many cases, may not be capable of being realized immediately.

The methods and assumptions applied, and the valuation techniques used, for financial instruments that are not quoted in an active market are disclosed in Note 20.

#### **Member loan loss provision**

In determining whether an impairment loss should be recorded in profit or loss, the Credit Union makes judgment on whether objective evidence of impairment exists individually for financial assets that are individually significant. Where this does not exist the Credit Union uses its judgment to group member loans with similar credit risk characteristics to allow a collective assessment of the group to determine any impairment loss.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

In determining the collective loan loss provision, management uses estimates based on historical loss experience for assets with similar credit risk characteristics and objective evidence of impairment. Further details on the estimates used to determine the allowance for impaired loans collective provision are provided in Note 10.

### 5. CASH AND CASH EQUIVALENTS

	2012	2011
Cash on hand and at bank	\$ 6,596,163	\$ 4,740,463
Liquidity reserve deposits callable or maturing in three months or less	800,000	300,000
<b>Total cash and cash equivalents</b>	<b>\$ 7,396,163</b>	<b>\$ 5,040,463</b>

The Credit Union cash resources exceed the minimum liquidity requirement by approximately \$3,999,992 (December 31, 2011 - \$3,100,000).

### 6. FINANCIAL INVESTMENTS

	2012	2011
Liquidity reserve deposits:		
Deposits callable or maturing between three months and five years	\$ 7,500,000	\$ 8,000,000
Accrued interest	78,636	78,343
Other financial investments:		
Central 1 Credit Union, membership	455,594	469,330
CUPP Services Ltd.	50,988	44,829
CUISA MGA	-	10,000
<b>Total</b>	<b>\$ 8,085,218</b>	<b>\$ 8,602,502</b>

Under governing legislation, for liquidity purposes, the Credit Union must maintain liquidity reserve deposits with Central 1 of at least 8% (2011 – 8%) of total members' deposits and non-equity shares.

The liquidity reserve deposits can be withdrawn only if there is a sufficient reduction in the Credit Union's total assets or upon withdrawal of membership from Central 1.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### **Central 1 Credit Union, membership**

The membership share requirement in Central 1 is determined based on the percentage of the Credit Union's assets to the total member credit unions' assets. Central 1 has a policy designed to ensure its capital is sufficient to support its operations and to comply with regulatory requirements.

Central 1 rebalances the membership shareholdings on an annual basis based on the proportion of each credit union's assets to the total assets of all Central's member credit unions.

In addition, member credit unions are subject to additional capital calls at the discretion of the Board of Directors of Central 1.

Central 1 shares are a condition of membership and are issued at par value. The shares are redeemable at par value upon withdrawal of membership or at the discretion of the Board of Directors of Central 1.

Dividends on the shares are at the discretion of the Board of Directors of Central 1. The Credit Union received dividends amounting to 2% of the membership shares in 2012 (2011 – 2%).

There is no separately quoted market value for the shares however, fair value is determined to be equivalent to the par value due to the fact transactions occur at par value on a regular and recurring basis.

The Credit Union is not intending to dispose of any Central 1 shares as the services supplied by Central 1 are relevant to the day to day activities of the Credit Union.

### **CUPP Services Ltd.**

The fair value of the shares in CUPP Services Ltd. is not readily determinable because of the lack of an active resale market for them. Fair value cannot be measured reliably as the timing of redemption of these shares cannot be determined, the range of reasonable fair value estimates is significant, and the probabilities of the various estimates cannot be reasonably assessed. Accordingly, they are carried at cost.

### **CUISA MGA**

During the year, the Credit Union sold its shares in CUISA MGA.

## **7. DERIVATIVE FINANCIAL INSTRUMENTS**

As part of its interest rate risk management process, the Credit Union has entered into interest rate swap contracts with Central 1 to hedge the Credit Union's exposure to interest rate risks.

As at December 31, 2012, the Credit Union had entered into 3 receive fixed interest rate swaps contracts, 1 of which is a forward swap agreement, with a total notional amount of \$15,000,000 (December 31, 2011 - \$15,000,000).

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

Under the terms of the contracts, Central 1 is obligated to pay the Credit Union a fixed rate ranging from 2.725% to 3.550% (December 31, 2011 - 2.725% to 3.550%). The Credit Union is obligated to pay Central a variable rate based upon the 3 month Banker's Acceptance rates. At December 31, 2012, the Credit Union is paying a variable rate of 1.29% (December 31, 2011 - 1.28%). All payments are based on the notional amount of the underlying swaps. The swap contracts will mature from March 15, 2014 to January 25, 2016 (December 31, 2011 - March 15, 2014 to January 25, 2016).

### 8. TRADE AND OTHER RECEIVABLES

	2012	2011
Commissions and premiums receivable	\$ 367,891	\$ 335,155
Prepaid expenses	145,538	148,328
Other accounts receivable	92,957	85,909
	\$ 606,386	\$ 569,392

### 9. LOAN TO MEMBERS

	2012	2011
Residential mortgages	\$ 63,491,688	\$ 57,643,946
Personal loans	19,344,452	20,726,596
Commercial mortgages	27,286,587	26,235,107
Commercial loans	3,977,394	3,376,020
	114,100,121	107,981,669
Accrued interest receivable	253,376	223,551
	114,353,497	108,205,220
Allowance for impaired loans		
Individual specific provision	(159,037)	(107,014)
Collective provision	(206,470)	(208,556)
	(365,507)	(315,570)
Net loans to members	\$ 113,987,990	\$ 107,889,650

At December 31, 2012, \$ 72,502,897 (December 31, 2011 - \$65,173,170) of loans are expected to be settled more than 12 months after the reporting date.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### Terms and conditions

Member loans can have either a variable or fixed rate of interest and they mature within five years.

Variable rate loans are based on a "prime rate" formula, ranging from prime minus 0.5% to prime plus 8.0%. The rate is determined by the type of security offered and the members' credit worthiness. The Credit Union's prime rate at December 31, 2012 was 3.0% (December 31, 2011 – 3.0%).

The interest rate offered on fixed rate loans being advanced at December 31, 2012 ranges from 1% to 14.5%. The rate offered to a member varies with the type of security offered and the member's credit worthiness.

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

Personal loans consist of term loans and lines of credit that are non real estate secured and, as such, have various repayment terms. Some of the personal loans are secured by funds on deposit and personal property or investments, and some are unsecured.

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

### Average yields to maturity

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

	Principal	2012 Yield	Principal	2011 Yield
Variable rate	\$ 37,675,346	4.53%	\$ 35,423,106	4.46%
Fixed rate	76,424,775	4.54%	72,558,563	4.89%
	\$ 114,100,121	4.54%	\$ 107,981,669	4.75%



# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### Credit quality of loans

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

	2012	2011
Unsecured loans	\$ 2,283,127	\$ 2,484,560
Loans secured by member deposits or other assets	8,477,434	8,509,419
Loans secured by real estate	103,339,560	96,987,690
	\$ 114,100,121	\$ 107,981,669

**Fair value** The fair value of member loans at December 31, 2012 was \$ 115,455,000 (December 31, 2011 - \$ 109,583,000).

### 10. PROVISION FOR IMPAIRMENT ON LOANS TO MEMBERS

	2012	2011
Individual specific provision	\$ 159,037	\$ 107,014
Collective provision	206,470	208,556
	\$ 365,507	\$ 315,570

#### Movement in the individual specific provision and collective provision for impairment

2012	Residential mortgages	Personal loans	Commercial mortgages	Commercial loans	Total
Balance, beginning of year	\$ -	\$ 229,753	\$ 80,984	\$ 4,833	\$ 315,570
Recoveries of loans previously written off	-	4,358	-	3,498	7,856
Allowance charged to profit or loss	40,000	104,860	26,254	2,944	174,058
	40,000	338,971	107,238	11,275	497,484
Write-offs	-	(131,977)	-		(131,977)
Balance, end of year	\$ 40,000	\$ 206,994	\$ 107,238	\$ 11,275	\$ 365,507
Gross principal balance of individually impaired loans	\$ 357,715	\$ 179,123	\$ 176,675	\$ -	\$ 713,513

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

2011	Residential mortgages	Personal loans	Commercial mortgages	Commercial loans	Total
Balance, beginning of year	\$ -	\$ 152,454	\$ 72,905	\$ 4,178	\$ 229,537
Recoveries of loans previously written off	-	605	-	1,712	2,317
Allowance charged to profit or loss	-	111,506	8,079	53,152	172,737
	-	264,565	80,984	59,042	404,591
Write-offs	-	(34,812)	-	(54,209)	(89,021)
Balance, end of year	\$ -	\$ 229,753	\$ 80,984	\$ 4,833	\$ 315,570
Gross principal balance of individually impaired loans	\$ -	\$ 144,390	\$ -	\$ -	\$ 144,390

### Individual loans that are impaired or potentially impaired based on age of repayments outstanding

Period of delinquency	2012		2011	
	Carrying value	Individual specific provision	Carrying value	Individual specific provision
30 to 90 days	\$ 889,175	\$ -	\$ 1,328,755	\$ -
Over 90 days	2,075,948	159,036	778,765	107,014
Total loans in arrears	2,965,123	159,036	2,107,520	107,014
Total loans not in arrears	111,388,374	-	106,097,700	-
Total loans	\$ 114,353,497	\$ 159,036	\$ 108,205,220	\$ 107,014

### Key assumptions in determining the allowance for impaired loans collective provision

The Credit Union has determined the likely impairment loss on loans which have not maintained the loan repayments in accordance with the loan contract, or where there is other evidence of potential impairment. In identifying the likely impairment, the Credit Union estimates the potential impairment using the loan type, type of loan security, the length of time the loans are past due and member beacon scores and bankruptcy navigator indices reflecting the financial services historical loss experience.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

The circumstances may vary for each loan over time, resulting in higher or lower impairment losses. The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Credit Union in order to reduce any differences between loss estimates and actual loss experience.

For purposes of the collective provision, loans are classified into separate groups with similar risk characteristics, based on the type of product and type of security.

Delinquent loans without a specific provision are summarized below:

<b>2012</b>	<b>Residential mortgage</b>	<b>Personal loans</b>	<b>Commercial mortgage</b>	<b>Commercial loans</b>	<b>Total</b>
30 to 90 days	\$ 889,175	\$ -	\$ -	\$ -	\$ 889,175
Over 90 days	1,324,909	104,359	467,612	20,031	1,916,911
	\$ 2,214,084	\$ 104,359	\$ 467,612	\$ 20,031	\$ 2,806,086

<b>2011</b>	<b>Residential mortgage</b>	<b>Personal loans</b>	<b>Commercial mortgage</b>	<b>Commercial loans</b>	<b>Total</b>
30 to 90 days	\$ 1,013,731	\$ -	\$ 314,817	\$ -	\$ 1,328,548
Over 90 days	647,092	24,866	-	-	671,958
	\$ 1,660,823	\$ 24,866	\$ 314,817	\$ -	\$ 2,000,506

### 11. PROPERTY CLASSIFIED AS HELD FOR RESALE

The Credit Union holds title to certain property in Ladysmith as a result of a loan foreclosure. The property is being actively marketed by the Credit Union, therefore its assets are classified as "property held for sale" on the consolidated statement of financial position. During the year, an impairment loss of \$ nil (2011 - \$144,666) was recognized on the property to reduce its carrying value to the estimated fair value less costs to sell.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### 12. PREMISES AND EQUIPMENT AND INTANGIBLE ASSETS

	Land	Buildings	Equipment	Vehicle	Total	Intangible assets
Balance at January 1, 2011	\$ 1,412,753	\$ 1,736,042	\$ 759,969	\$ 11,113	\$ 3,919,877	\$ 301,896
Additions	-	6,168	31,452	-	37,620	27,494
Reclassifications	-	-	(8,897)	-	(8,897)	8,897
Reset of amortization on revaluation of buildings	-	(40,000)	-	-	(40,000)	-
Gain on revaluation	28,156	84,960	-	-	113,116	-
Disposals	-	-	(2,162)	-	(2,162)	-
Balance at December 31, 2011	1,440,909	1,787,170	780,362	11,113	4,019,554	338,287
Additions	-	10,381	30,989	-	41,370	17,788
Reset of amortization on revaluation of buildings	-	(81,191)	-	-	(81,191)	-
Loss/Gain on revaluation	(99,726)	26,704	-	-	(73,022)	-
Disposals	-	-	-	-	-	-
<b>Balance at December 31, 2012</b>	<b>\$ 1,341,183</b>	<b>\$ 1,743,064</b>	<b>\$ 811,351</b>	<b>\$ 11,113</b>	<b>\$ 3,906,711</b>	<b>\$ 356,075</b>
<b>Accumulated depreciation</b>						
Balance at January 1, 2011	\$ -	\$ 40,000	\$ 381,980	\$ 3,704	\$ 425,684	\$ 174,450
Depreciation expense	-	40,000	64,957	5,557	110,514	32,566
Impairment losses	-	-	-	-	-	-
Reclassifications	-	-	74,866	-	74,866	(74,866)
Reset of amortization on revaluation of buildings	-	(40,000)	-	-	(40,000)	-
Disposals	-	-	-	-	-	-
Balance at December 31, 2011	-	40,000	521,803	9,261	571,064	132,150
Depreciation expense	-	41,191	62,523	1,852	105,567	36,291
Impairment losses	-	-	-	-	-	-
Reset of amortization on revaluation of buildings	-	(81,191)	-	-	(81,191)	-
Disposals	-	-	-	-	-	-
<b>Balance on December 31, 2012</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 584,326</b>	<b>\$ 11,113</b>	<b>\$ 595,440</b>	<b>\$ 168,441</b>
<b>Net book value</b>						
December 31, 2011	\$ 1,440,909	\$ 1,747,170	\$ 258,560	\$ 1,852	\$ 3,448,491	\$ 206,137
December 31, 2012	\$ 1,341,183	\$ 1,743,064	\$ 227,025	\$ -	\$ 3,311,271	\$ 187,634

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### 13. MEMBER DEPOSITS

	2012	2011
Demand and chequing	\$ 46,913,813	\$ 42,300,303
Term	47,759,961	46,673,183
Registered savings plans	19,368,838	19,227,836
Registered retirement income funds	6,619,287	5,915,516
Tax free savings accounts	3,064,332	2,193,705
Membership equity shares	2,053,359	2,125,026
	125,779,590	118,435,569
Accrued deposit interest	1,344,423	1,110,244
	<u>\$ 127,124,013</u>	<u>\$ 119,545,813</u>

At December 31, 2012, \$ 57,768,184 (December 31, 2011 - \$63,882,902) of deposits are expected to be settled more than 12 months after the reporting date.

The Credit Union Deposit Insurance Corporation (CUDIC), a government corporation, guarantees all deposits and non-equity shares of BC credit unions as set out in the Financial Institutions Act. Membership equity shares are not covered by the deposit insurance.

#### Terms and conditions

Chequing deposits are due on demand and are generally non-interest bearing. Certain chequing deposits bear interest at a variable rate up to 1.5% at December 31, 2012.

Demand deposits bear interest at variable rates ranging from 0.125% to 1.250% as at December 31, 2012. Interest is calculated daily and paid on the accounts monthly.

Term deposits bear fixed rates of interest for terms up to five years. Interest can be paid monthly, annually or at maturity. Interest rates offered on regular term deposits issued on December 31, 2012 range from 0.25% to 3.00% (December 31, 2011 – 0.25% to 4.00%)

Registered retirement savings plan (RRSP) accounts bear fixed or variable rates of interest for terms of up to five years. Fixed rate RRSPs have terms and rates similar to the term deposit accounts described above.

Registered retirement income funds (RRIFs) consist of fixed and variable rate products with terms and conditions similar to those of the RRSPs described above. Members may make withdrawals from a RRIF account on a monthly, semiannual, or annual basis. The regular withdrawal amounts vary according to individual needs and statutory requirements.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

The tax-free savings accounts can be fixed or variable rate with terms and conditions similar to those of the RRSPs described above.

### Average yields to maturity

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

	2012	2012	2011	2011
	Principal	Yield	Principal	Yield
Variable rate	\$ 49,103,899	0.73%	\$ 46,450,775	0.70%
Fixed rate	76,675,691	3.04%	71,984,794	3.44%
	\$ 125,779,590	2.14%	\$ 118,435,569	2.37%

The majority of member deposits are with members located in and around Ladysmith, British Columbia.

### 14. OTHER LIABILITIES

	2012	2011
Payables and accruals	\$ 357,496	\$ 314,616
Deferred income	126,400	115,975
	\$ 483,896	\$ 430,591

### 15. INCOME TAXES

The significant components of tax expense included in profit or loss are composed of:

	2012	2011
Current tax expense	\$ 41,353	\$ 48,300
Deferred tax expense (recovery)		
Origination and reversal of temporary differences	19,248	2,676
	\$ 60,601	\$ 50,976

## LADYSMITH & DISTRICT CREDIT UNION

### Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

Reasons for the difference between tax expense for the year and the expected income taxes based on the statutory tax rate of 25.0% (2011 – 26.5%) are as follows:

	2012	2011
Profit for the year	\$ 413,198	\$ 331,089
Expected taxes based on the statutory rate of 25.0% (2011 -26.5%)	103,300	87,739
Reduction due to small business deduction	(48,177)	(43,042)
Other	5,478	6,279
Income tax expense	\$ 60,601	\$ 50,976

The tax effects of temporary differences that give rise to significant portions of the future tax asset are as follows:

	2012	2011
Allowance for loan losses	\$ (49,344)	\$ (29,600)
Cumulative eligible capital	21,431	23,929
Premises and equipment	100,928	92,069
Interest rate swap	-	90,392
Other	2,696	(4,118)
Future income tax liability, net	\$ 75,711	\$ 172,672

#### 16. MEMBER SHARES

Member shares are recognized as a liability, equity or compound instrument based on their respective terms and in accordance with *IAS 32 Financial Instrument Presentation*, and *IFRIC 2 Members' Shares in Cooperative Entities and Similar Instruments*. All of the Credit Union's member shares are classified as financial liabilities, and are initially recognized at fair value net of any transaction costs directly attributable to the issuance of the instrument and subsequently carried at amortized cost using the effective interest rate method. An unlimited number of shares are authorized for issuance. During the year, there was a net redemption of 134,475 shares (2011 – net redemption of 141,013 shares).

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### Terms and conditions

#### Membership shares

As a condition of membership, which is required to use the services of the Credit Union, each member is required to hold \$25 in membership shares. These membership shares are redeemable at par only when a membership is withdrawn. Dividends are at the discretion of the Board of Directors. All issued shares are fully paid.

Funds invested by members in member shares are not insured by the Credit Union Deposit Insurance Corporation (CUDIC). The withdrawal of member shares is subject to the Credit Union maintaining adequate regulatory capital (see Note 22), as is the payment of dividends on these shares.

### 17. OTHER INCOME

	2012	2011
General insurance commissions	\$ 754,703	\$ 743,117
Account service charges	364,365	421,972
Loan processing fees	244,221	213,593
Other	157,308	204,424
	\$ 1,520,597	\$ 1,583,106

### 18. OPERATING EXPENSES

	2012	2011
Advertising and member relations	\$ 171,291	\$ 140,646
Depreciation of premises and equipment	105,566	111,666
Amortization of intangible assets	36,291	32,567
Data processing	108,020	105,726
Dues and assessments	122,508	122,090
Insurance	50,446	45,545
Training, meetings and travel	94,023	99,337
Premises and office	317,271	345,788
Professional fees and dues	231,080	305,727
Salaries and benefits	2,202,899	2,210,794
Service charges	207,246	162,008
Impairment of property held for resale	-	144,666
Loss on revaluation of land and buildings	22,954	2,424
	\$ 3,669,595	\$ 3,828,984



# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### 19. RELATED PARTY TRANSACTIONS

The Credit Union entered into the following transactions with key management personnel, which are defined by IAS 24 *Related Party Disclosures*, as those persons having authority and responsibility for planning, directing and controlling the activities of the Credit Union, including directors and management.

<b>Compensation of key management personnel</b>	<b>2012</b>	<b>2011</b>
Salaries and benefits	\$ 685,559	\$ 529,069

During the 2012 year, the Credit Union recategorized 2 positions to key management personnel.

<b>Loans and credit extended to key management personnel</b>	<b>2012</b>	<b>2011</b>
Loan balances outstanding	\$ 2,034,217	\$ 2,217,493
Interest received on loans	62,072	67,483
Aggregate value of unadvanced loans	-	-
Lines of credit outstanding	549,770	744,943
Interest received on lines of credit	17,380	12,998
Unused value of lines of credit	382,297	145,409
Letters of credit	15,000	15,000

Loans to key management personnel including their related parties must meet the same qualification requirements and general conditions which apply to Members and must be approved by the Board of Directors and reviewed by the Conduct Review Committee. Loans to key management personnel including their related parties may bear preferential rates of interest.

<b>Deposits on hand from key management personnel</b>	<b>2012</b>	<b>2011</b>
Aggregated value of term and savings deposits	\$ 2,414,279	\$ 1,746,431
Total interest paid on term and saving deposits	32,965	28,071
	1.37%	1.61%

The Credit Union's policy for receiving deposits from key management personnel is that all transactions are approved and deposits accepted on the same terms and conditions which apply to Members for each type of deposit. There are no benefits or concessional terms and conditions applicable to key management personnel or close family members.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### 20. FINANCIAL INSTRUMENT CLASSIFICATION AND FAIR VALUE

The following table represents the carrying amount by classification:

2012	Available- for-sale	Fair value through profit or loss	Cash flow hedges	Loans and receivables	Other financial liabilities
Cash	\$ -	\$ -	\$ -	\$ 7,396,163	\$ -
Loans to members	-	-	-	113,987,990	-
Investments	506,582	-	-	7,578,636	-
Derivative financial instruments	-	-	495,991	-	-
Trade and other receivables	-	-	-	460,848	-
Member deposits	-	-	-	-	(127,124,013)
Trade payables and accruals	-	-	-	-	(357,496)
	\$ 506,582	\$ -	\$ 495,991	\$ 129,423,637	\$ (127,481,509)

2011	Available- for-sale	Fair value through profit or loss	Cash flow hedges	Loans and receivables	Other financial liabilities
Cash	\$ -	\$ -	\$ -	\$ 5,040,463	\$ -
Loans to members	-	-	-	107,889,650	-
Investments	524,159	-	-	8,078,343	-
Derivative financial instruments	-	-	697,518	-	-
Trade and other receivables	-	-	-	421,064	-
Member deposits	-	-	-	-	(119,545,813)
Trade payables and accruals	-	-	-	-	(314,616)
	\$ 524,159	\$ -	\$ 697,518	\$ 121,429,520	\$ (119,860,429)

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

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

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

inputs).

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

	Level 1	Level 2	Level 3	Total
<b>2012</b>				
Central 1 Credit Union, membership	\$ -	\$ -	\$ 455,594	\$ 455,594
CUPP Services Ltd.	-	-	50,988	50,988
CUISA MGA	-	-	-	-
	\$ -	\$ -	\$ 506,582	\$ 506,582
<b>2011</b>				
Central 1 Credit Union, membership	\$ -	\$ -	\$ 469,330	\$ 469,330
CUPP Services Ltd.	-	-	44,829	44,829
CUISA MGA	-	-	10,000	10,000
	\$ -	\$ -	\$ 524,159	\$ 524,159

There were no transfers among the three levels for the years ended December 31, 2012 and 2011.

## 21. FINANCIAL INSTRUMENT RISK MANAGEMENT

### General objectives, policies and processes

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

### CREDIT RISK

Credit risk is the risk of financial loss to the Credit Union if a counterparty to a financial instrument fails to make payments of interest and principal when due. The Credit Union's exposure to credit risk is concentrated primarily in its loans. Risk management policies are implemented by management and the Board. These policies include evaluating the member's ability to repay the loan when it is originally granted and subsequently renewed and regularly monitoring member information such as delinquent and over limit amounts. Notes 9 and 10

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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provide further discussion over the Credit Union's loan balances and exposure to credit risk.

Concentrations of credit risk arise when members are engaged in similar economic activities or in similar geographic areas.

### **Risk measurement**

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

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

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

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

With respect to credit risk, the Investment Lending Committee meets quarterly to review monthly reports summarizing new loans, delinquent loans and overdraft utilization. The Board of Directors receives an analysis of bad debts and allowance for doubtful loans annually.

A sizeable portfolio of the loan book is secured by residential property in Ladysmith, British Columbia. Therefore, the Credit Union is exposed to the risks in reduction of the loan to valuation ratio (LVR) cover should the property market be subject to a decline. The risk of losses from loans undertaken is primarily reduced by the nature and quality of the security taken.

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

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### LIQUIDITY RISK

Liquidity risk is the risk that the Credit Union will not be able to meet all cash outflow obligations as they come due. The Credit Union mitigates this risk by monitoring cash activities and expected outflows so as to meet all cash outflow obligations as they fall due.

#### Risk measurement

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

#### Objectives, policies and procedures

The Credit Union's liquidity management framework is designed to ensure that adequate sources of reliable and cost effective cash or its equivalents are continually available to satisfy its current and prospective financial commitments under normal and contemplated stress conditions.

Provisions of the Credit Union's Liquidity Plan require the Credit Union to maintain a prudent amount of liquid assets in order to meet member withdrawals. The Credit Union has set a minimum liquidity ratio of 10%.

The Credit Union manages liquidity risk by:

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

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

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

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Qualifying liquid assets on hand	
Cash	\$ 464,332
Central 1 liquidity terms and deposits	13,541,312
<hr/>	
Total liquid assets	14,005,644
Required liquidity – 8% of deposit and debt liabilities	10,005,652
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<b>Excess liquidity</b>	<b>3,999,992</b>
Total liquid assets	14,005,644
Deposit and debt liabilities	125,070,654
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<b>Liquidity ratio</b>	<b>11.20%</b>

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# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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The maturities of liabilities are shown below under market risk.

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

### **MARKET RISK**

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate as a result of market factors. Market factors include three types of risk: interest rate risk, currency risk, and equity risk. The level of market risk to which the Credit Union is exposed varies depending on market conditions and the composition of the Credit Union's investment, lending, and deposit portfolios. The Credit Union has limited exposure to other market risk because the majority of its investments are deposits held with Central 1.

### **INTEREST RATE RISK**

Interest rate risk is the potential for financial loss caused by fluctuations in fair value or future cash flows of financial instruments because of changes in market interest rates. The Credit Union is exposed to this risk through traditional banking activities, such as deposit taking and lending.

The Credit Union's goal is to manage the interest rate risk of the statement of financial position to a target level. The Credit Union continually monitors the effectiveness of its interest rate mitigation activities. The Credit Union uses interest rate swaps to hedge a portion of its interest rate risk (Note 7).

### **Risk measurement**

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

### **Objectives, policies and procedures**

The Credit Union's major source of income is financial margin, the difference between interest earned on investments and members loans and interest paid on member deposits. The objective of asset / liability management is to match interest sensitive assets with interest sensitive liabilities as to amount and as to term to their interest rate repricing dates, thus minimizing fluctuations of income during periods of changing interest rates.

Schedules of matching and interest rate vulnerability are regularly prepared and monitored by Credit Union management and reported to the Investment Lending Committee in accordance with the Credit Union's policy.

### **Interest rate risk**

The following schedule shows the Credit Union's sensitivity to interest rate changes. Amounts with floating rates or due or payable on demand are classified as maturing within three months, regardless of maturity. A significant amount of loans and deposits can be settled before maturity on payment of a penalty, but no adjustment has been made for repayments

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

that may occur prior to maturity. Amounts that are not interest sensitive have been grouped together, regardless of maturity.

In thousands	Interest sensitive balances			Not interest sensitive	Total	Average rates
	Within 1 year	1 year to 4 years	Over 4 years			
<b>Assets:</b>						
Cash resources	\$ 6,194	\$ -	\$ -	\$ 1,202	\$ 7,396	3.28%
Loans	62,263	36,417	15,418	(79)	114,019	4.38%
Investments & other	2,200	5,000	300	585	8,085	0.11%
Average rate	70,657 4.12%	41,417 4.15%	15,718 3.82%	1,708	129,500 3.83%	
<b>Liabilities:</b>						
Deposits	53,130	39,077	11,156	23,761	127,124	2.56%
Other liabilities	-	-	-	655	655	0.00%
Average rate	53,130 2.89%	39,077 3.68%	11,156 2.15%	24,416	127,779 2.40%	
<b>Interest rate swaps:</b>						
Assets	-	10,000	-	-	10,000	
Liabilities	10,000	-	-	-	10,000	
<b>Net mismatch:</b>						
2012	\$ 7,527	\$ 12,340	\$ 4,562	\$ (22,708)	\$ 1,721	
<b>Net mismatch:</b>						
2011	\$ 20,868	\$ 17,412	\$ (14,669)	\$ (20,789)	\$ 2,822	

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

An analysis of the Credit Union's risk due to changes in interest rates determined that an increase in interest rates of 1% could result in an increase in financial margin by approximately \$62,000 or 2.2% (2011 - \$252,000 or 9.6%) while a decrease in interest rates of 1% could result in a decrease in financial margin by approximately \$84,000 or 3.0% (2011 - \$272,000 or 10.4%) over the following twelve months.

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

### CURRENCY RISK

The Credit Union's business is predominantly conducted in Canadian currency with nominal deposits and funds held in US dollars. The Credit Union is not significantly exposed to currency risk.

# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

### 22. CAPITAL MANAGEMENT

The Credit Union's objectives with respect to capital management are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations.

The Credit Union considers its capital to include membership shares and retained earnings. There have been no changes in what the Credit Union considers to be capital since the previous period.

The Credit Union establishes the risk weighted value of its assets in accordance with the Regulations of the Financial Institutions Act which establishes the applicable percentage for each class of assets.

The fair value of deposits at December 31, 2012 was \$128,179,000 (December 31, 2011 - \$120,599,000).

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

As at December 31, 2012, the Credit Union met the capital requirements of its capital plan with a calculated members' capital ratio of 12.14% (2011 – 12.15%).

Regulatory capital consists of the following:

	2012	2011
<b>Primary capital</b>		
Membership shares	\$ 2,053,359	\$ 2,125,206
Retained earnings – previous year end	6,410,765	6,130,652
Net income – current year	352,597	280,113
Deferred income tax	80,611	177,572
Deductions from capital:		
Goodwill and intangibles	(187,635)	(206,137)
Gains on own-use property	(1,257,109)	(1,257,109)
	7,452,588	7,250,297
<b>Secondary capital</b>		
Proportion of system retained earnings – 50%	891,000	787,776
Total regulatory capital	\$ 8,343,588	\$ 8,038,073



# LADYSMITH & DISTRICT CREDIT UNION

## Notes to Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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### 23. CREDIT FACILITIES

The Credit Union has authorized lines of credit with Central 1 as follows:

Canadian funds	\$ 400,000
US dollar funds	\$ 50,000
Capital markets	\$ 200,000
Term loan credit facility	\$ 2,000,000

At December 31, 2012, the Credit Union had not utilized any of the credit facilities.

### 24. COMMITMENTS

#### a) Credit Commitments

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

	2012	2011
Loans approved not disbursed	\$ 1,747,025	\$ 1,031,646
Members unused lines of credit	12,561,776	11,960,065
Letters of credit	498,500	483,380

#### b) Contingencies

In the normal course of business, the Credit Union may be subject to litigation and provisions for amounts that may become payable are included in liabilities where appropriate. Provisions represent management's best estimate of the Credit Union's liability related to legal disputes for which it is probable that an amount will be paid. No amount is provided for disputes for which it is not probable that an amount will be paid. Uncertainty relates to whether litigation claims will be settled in or out of court, or if the Credit Union will be successful in defending claims arising from litigation.

Based on current knowledge, the Credit Union expects that final determination of claims arising from litigation will not have a material adverse effect on its consolidated statement of financial position or operating results. No provision for a liability in respect of litigation is included in the financial statements.

### 25. SUBSEQUENT EVENT

Subsequent to the year end, the Credit Union purchased 2 commercial properties and 1 residential property located adjacent to the Credit Union's existing premises for a total purchase price of \$685,000. The properties were purchased with a view to future potential expansion of the Credit Union's operations.