servus credit union

Management's Discussion and Analysis
Consolidated Financial Statements

For the year ended October 31, 2011

Servus Corporate Centre, 151 Karl Clark Road, Edmonton, Alberta, T6N 1H5
Toll Free 187SERVUSCU / 1.877.378.8728 servus.ca

SERVUS CREDIT UNION LTD.
Management's Discussion and Analysis
For the year ended October 31, 2011

Table of Contents

Management's Discussion and Analysis

Consolidated Financial Statements

SERVUS CREDIT UNION LTD.
Management's Discussion and Analysis
For the year ended October 31, 2011

Servus Credit Union Ltd.'s (Servus or the credit union) 2011 annual report consists of two documents:

1. A Management's Discussion & Analysis and Consolidated Financial Statements for the year ended October 31, 2011, which detail our credit union's financial and operating results.
2. A Corporate Profile, which provides a general overview of Servus Credit Union.

Both documents are available in print at any of our branches or online at servus.ca.

Note Regarding Forward-Looking Statements

This annual report contains forward-looking statements about the operations, objectives, and expected financial performance of Servus Credit Union. These statements are subject to risks and uncertainties. Actual results may differ depending on a number of factors, including but not limited to legislative or regulatory changes, interest rates and general economic conditions in Alberta and Canada. These issues should be given careful consideration and readers should not place undue reliance on Servus' forward-looking statements.

Overview

About Servus Credit Union
With roots dating back to 1938, Servus Credit Union is proud of our long history of providing exceptional service to our members. Our nearly 2,300 employees serve approximately 390,000 members from 100 locations in 62 communities across Alberta. With business support offices in Red Deer, Lloydminster and Edmonton, we are Alberta's largest credit union and the first province-wide credit union in Canada.

Servus is a co-operative financial institution that is firmly committed to a core set of principles that make us different than other financial institutions—Member Ownership, Exceptional Service, Local Decision-Making, Profit Share and Community Support. Our members share directly in the credit union's success through our Profit Share program, new products and services, and community support.

Servus is Alberta Venture Magazine's 2011 Best Overall Workplace for Over 750 Employees and a member of the Platinum Club of Canada's 50 Best Managed Companies, an honour we first received in 2009 and re-qualified for in 2010 and 2011.

Vision, Mission and Values
Servus employees and our Board of Directors worked together in 2009 to define a vision and mission for the credit union that captures what Servus should be and represent. Our vision, mission and values come together to provide a clear direction for our credit union; they focus our efforts and guide our operations.

SERVUS CREDIT UNION LTD.
Management's Discussion and Analysis
For the year ended October 31, 2011

Our Vision
Servus Credit Union builds a better world – one member at a time.

Our Mission
Servus Credit Union provides sound, advice-based financial products and services. We are here for our members through all stages of their lives. We help them achieve personal satisfaction, enjoy financial stability and a good quality of life, and we are committed to making a difference in the communities where they live and work.

Our Values
Community, Fairness, Integrity, Investing in Our People, Life/Work Balance, Member Service, Teamwork

Integration

In the two years that followed the 2008 amalgamation of Alberta's three largest credit unions to form Servus Credit Union, we focused on the integration of our legacy organizations and the creation of a single, unified credit union. As we moved into our third year as one credit union, we recognized the need to balance honouring our past with focusing on our direction for the future. In 2011, key priority areas that we focused on as fundamental to achieving our long-term vision included:

- Refining our member service philosophy, called Members First
- Defining our core brand and market differentiators
- Developing our employees' leadership skills and capacity, and supporting ongoing skill development
- Continued development of a new banking system platform
- Positioning Servus as a key partner in the provincial, national and international credit union system

As a reflection of our success and testament to the difference we make for our members, our communities and our world, Servus Credit Union and our employees were honoured to receive a number of awards this year, including:

- Alberta Venture's Best Overall Workplace for Over 750 Employees and Best Workplace for Benefits; Honourable Mention for Best Employer Perks and Incentives
- Four Best of Red Deer awards: Top Financial Institution, Friendliest Staff, Best Business to Work For, and Best Customer Service
- Slave Lake Chamber of Commerce named Servus Credit Union the community's 2011 Employer of the Year
- Big Brothers Big Sisters of Lloydminster's Champion of Magic 2011 award for outstanding contribution to their agency through fundraising and other support

- Sylvan Lake Chamber of Commerce Employee of the Year for awarded to Bev Gunderson, Financial Advisor

- Gold medal for credit union innovation from the Filene Research Institute awarded to Robert Christiansen, Branch Manager, Medicine Hat - Southview

- Three 2011 Business Awards from the Town of Blackfalds: Community Involvement, Customer Service, and Long Term Business

- Next Top Credit Union Executive title awarded by the Credit Union Executive Society to Devin Selte, Corporate Trainer, Leadership Development and Change Leadership

- Re-qualified as a member of the Platinum Club of Canada's 50 Best Managed Companies for the third year in a row

As we continue with our integration activities we are seeing increased efficiencies resulting in improved service for members and more opportunities for employees. We will continue to balance harmonization activities with our focus on the future, and will be well positioned to be a strong, stable, and competitive credit union that provides exceptional member service now and into the future.

Market and Economic Environment
During 2011 Alberta continued the economic recovery that began to build momentum in 2010. Employment conditions improved as did prospects for most commercial and retail members of the credit union. Evidence of this can be seen in an almost 40% decline in the amount of loans written off in 2011 compared to 2010.

A stronger economy supported loan and deposit growth for the credit union but, as was anticipated in last year's report, increased competition tempered the growth rate.

The European government debt situation dominated the headlines and cast doubts on the global economy's ability to stage a sustainable recovery. This in turn caused the Bank of Canada to forestall any increases in the Bank Rate until there is greater certainty around these issues. While beneficial for members borrowing funds from the credit union, the extended period of very low interest rates has become a material challenge for members dependent on investment income. Interest rates that are barely above the rate of inflation also induce higher levels of borrowing and reduce the incentive to pay down debt, which in turn contributes to a worrying level of consumer debt overall.

The historically low interest rate environment created challenges for the credit union's interest income, but through 2011 these challenges were managed well and sufficient income was earned to support investment in the credit union, in our communities and in our members through profit sharing.

Overall, the credit union was fortunate to do business in a province that weathered the economic crisis well through 2011. This can be seen in the growth, financial performance and strong capital position of the credit union.

Key Performance Drivers

2011 Balanced Scorecard

The balanced scorecard is an at-a-glance summary of Servus Credit Union's performance on a mix of financial and non-financial measures against specified targets.

Objective	Measure	2011 Target	2011 Result
Financial Performance			
Financial growth	Operating income (millions) [1]	$100.7	$102.6
Reduced dependency on interest-based income	Other income growth as a percentage of average assets [1]	0.647%	0.651%
Leveraging assets profitably	Return on assets [1]	0.827%	0.938%
Employee Experience			
High-level employee satisfaction	Employee engagement score as reported by employee survey	80%	80%
Dedicated to life-long learning	Percent of employees attending development programs	60%	85%
Future-focused strategic staffing	Percent of executive leadership and senior leadership with a succession plan	100%	100%
Member Experience			
Servus members are advocates	Member satisfaction score as reported by member survey	75%	79.1%
Business Processes			
Business process improvements for effectiveness and efficiency	Operating efficiency ratio [1,2]	72.364%	70.445%
	Operating expenses as a percentage of average assets [1]	2.413%	2.398%

1. Results are before patronage, taxes, employee incentives and extraordinary items. The extraordinary items include the impairment of costs directly related to the core banking system software, a single commercial loan provision and income from our investment in Alberta Central.
2. The operating efficiency ratio is a ratio of expenses to revenues. In essence, it measures how much the credit union spent to earn a dollar of revenue.

Growth and Balance: 2011 Results

For Servus, 2011 was a year of modest and balanced growth. Alberta's economy began recovering from the recent financial crisis and we started seeing more potential for growth. The second half of the year showed marked improvement in growth compared to the first six months, despite global turmoil during that period.

Our credit union's total assets grew by 4.2% in 2011. Loan growth of 6.3% was slightly stronger than the 5.3% growth we saw in 2010 but was moderately below our planned results for 2011. Deposit growth of 3.8% was lower than growth of 6.2% experienced during 2010. This was because of a challenging interest rate environment and work done by the credit union to balance our loan and deposit book to maximize returns to our members, have funds available to lend, and manage exposure to larger institutional depositors. Deposit growth was more than enough to satisfy operating needs and to fund the loans advanced during the year, and overall liquidity was managed well within policy and operating objectives.

Net income results were weaker than last year, decreasing $9.2 million or 18.6% because of one large commercial loan provision and the probable decision from management not to use the work completed on the proposed new banking system. Without these two non-recurring events, net income would have risen $10.1 million or 20.4%.

The following is a detailed analysis of our credit union's results in a number of areas.

Net Interest Income

Net interest income increased $18.6 million (6.6%) in 2011. This improvement is due in part to increases in interest rates seen toward the end of 2010 and in part due to growth in our loans and deposits. Net interest income will continue to be a challenge in 2012 because of the low rate environment and the potential for increased competition in Alberta, but our planning process indicates this can be well managed while still meeting strategic and capital objectives.

Provision for Credit Losses

Servus had expected the provision for credit losses to remain at its historical high levels through 2011 because of the continuing difficulties created through the economic slowdown of 2009 and 2010. The actual provision for credit losses increased by $5.0 million or 43.9% in 2011 compared to 2010 due to a large allowance associated with a single loan. Management of the credit union believes there is good potential to recover some or all of the provision on this loan in future periods and expects to see the provision moving down in 2012 as long as the Alberta economy continues to perform at current levels.

Other Income

Other income increased by $1.6 million or 2.1% over last year. Factors contributing to this increase include:

- An increase in insurance and wealth management commissions of $3.4 million, which resulted from a significant investment by the credit union in increasing access to these services for members
- Foreign exchange income that was $0.7 million higher than in 2010 due to members taking advantage of the strong Canadian dollar and rising awareness among credit union members of the excellent exchange rates we offered compared to many competitors

- Higher income from our investment in Alberta Credit Union Central, which rose by $1.5 million in 2011

These gains were partially offset by a modest decrease in service fee income of $1.0 million and a decrease in loan and prepayment fees of $2.5 million. The decreased loan and prepayment fee amounts are associated with lower interest rates on loans to members and are not expected to return to the levels seen in 2010 and 2009.

Diversifying the credit union's income streams to reduce its dependency on margin income continues to be a strategic focus and members will see further investment in our offering of wealth services in 2012.

Operating Expenses

Overall, operating expenses increased $24.1 million or 9.2% during 2011. The increase included personnel costs ($10.9 million or 7.4%), which is a result of increased staffing levels and annual changes in compensation. While a number of financial institutions in Canada and around the world have taken steps to reduce the number of employees, Servus continues to invest in the credit union and increase employment opportunities in the communities we serve.

An increase in general operating expenses of $12.5 million was primarily due to an impairment of costs directly related to the core banking system software. In 2010, Servus selected a new core banking platform and continued its detailed analysis of design and evaluation of requirements. In the process of developing the single banking system platform, management concluded that the development effort required and risks associated with the conversion of three separate banking systems to the platform originally selected cannot be resolved in a cost-effective and timely basis. Management will likely recommend an alternative software solution for the banking system in 2012. As a result, the credit union has determined that it is appropriate to record an impairment loss for the cost directly associated with the original software, resulting in a write-down of $10.3 million ($8.1 million after taxes).

In addition to the impairment, general expenses rose only $2.2 million or 3.8% due to:

- An increase in computer processing costs of $2.8 million or 24.9% to support one of the three legacy banking systems. Servus became the only user of this system during the year and must support all the service provider's operating costs.
- An increase of $1.7 million or 80.1% in professional and legal fees for a number of projects for human resources, marketing and information services.

These increases were offset by:

- A decrease of $1.6 million or 13.5% in marketing costs as the credit union worked to align spending with the rate of revenue growth. The credit union does intend to increase the investment in this area in coming years as work is completed on a number of projects.
- A decrease of $0.8 million or 2.6% in administrative and other expenses to align spending with the rate of revenue growth.
- A decrease of $0.8 million or 4.3% in member security costs primarily due to a reduction in the assessment rate associated with the guarantee on deposits with Servus through the Credit Union Deposit Guarantee Corporation.

Patronage and Dividends
Continuing our commitment to demonstrating the credit union difference and sharing our profits with our members, Servus paid $25.1 million in cash patronage to our members in December 2011. This was an increase of $1.5 million or 6.3% over amounts paid in 2010. This increase is consistent with the growth in the credit union's assets, loans and net interest income. Patronage is shared with members based on the amount and type of business they hold with the credit union.

We also paid $18.6 million in common and investment share dividends to our members based on rates of 4.25% and 5.25% respectively. Servus pays these dividends each year, at the discretion of the Board of Directors.

Operating Net Income
Operating net income (or income before patronage allocation and income taxes) decreased by $8.9 million or 10.4% in 2011. The decrease is attributed to the impairment of costs directly related to the core banking system software, a higher provision for credit losses, and increased operating costs. The decrease was offset by higher net interest income.

Net Income
Net income fell $9.2 million or 18.6%. The larger percentage decrease in net income is because the patronage payment to members was slightly higher than last year – or a larger percentage of income. The Board of Directors considered whether a large payout to members would negatively impact the long term viability of the credit union and its capital adequacy. Management and the Board came to the conclusion that the patronage and dividend payments still result in a strong capital position for the credit union and are comfortably sustainable in the long run.

Capital
Servus enjoys a strong capital position that was well-managed and continued to strengthen in 2011:

- At 7.98% of total assets, the credit union's capital is almost double the 4% required by regulations.
- Our capital as a percentage of risk weighted assets is 14.69% compared to 14.35% in 2010 and a required level of 8%.
- Retained Earnings, which is considered the credit union's primary source of capital, increased by $25.1 million to 3.71% of assets, up from 3.64% last year.
- We're close to achieving our plan of meeting the regulatory target of 4% capital to assets using Retained Earnings alone and expect to reach this mark in 2012 or early 2013.

Servus Credit Union is well positioned to satisfy capital requirements based on the new Basel III international standards when they are adapted for and introduced to the Alberta credit union system.

Overall, the credit union's growth in 2011 was sound and well balanced, and finished strong in the final half of the year. We see good opportunity in Alberta for 2012 and expect growth to improve slightly compared to 2011.

Moderation and Observation: Outlook for 2012

Forecasting the economic and competitive environment is always challenging, and the 2012 fiscal year is no exception. Both the short-term forecast for the year and the mid-term forecast to 2015 are tied so closely to policy decisions by governments and financial bodies that it is very difficult to anticipate outcomes with any confidence.

We believe that the next few years will be a period of very moderate growth and compressed revenues interrupted by periods of economic crisis. Whether these crises develop into full scale recession will depend on the actions of governments and central banks. Here are some of the key factors that we expect will influence Servus' actions and results in 2012.

Our World

We expect China, India and emerging markets to remain sound, which will support commodity prices. The Chinese situation in particular is difficult to forecast given their unusual mix of state economy and capitalism. Given the experience of aggressive growth in this region there is some risk of an unexpected negative economic event in the next three years but at this point there is no indication this risk is imminent.

Fiscal restraint in developed nations will be a material drag on economic growth for many years to come. There is very real risk of recession in Europe and the United States if fiscal restraint is not balanced with shorter term stimulus and if political considerations interfere with difficult but necessary policy decisions. It is hard to anticipate how the European debt situation would unravel should Germany fall into recession, but it would likely trigger a global crisis of confidence.

Despite these risks we still believe that overall there is a strong case to be made for a moderate growth environment, recognizing the significant concerns in Europe and the United States. The factors are still in place to allow for a slower but positive global growth environment if a regimen of long-term spending cuts, tax changes and short-term economic stimulus is put in place. Without these, there is significant risk of a decline in economic growth in Europe and the United States.

Our Nation

On balance, Canada is in a good economic position but there are risks. We expect moderate economic growth with the lift from emerging economy demands being offset by weak exports to the United States. Canada should fare better than most developed countries but will be hurt by a weaker American economy.

Any material slowdown in the emerging markets would have a significant impact on the demand for and value of commodities, which would damage our economy.

Should the American economy fall into recession, Canada would undoubtedly feel the effects but we note that the current federal fiscal situation positions our government well to provide offsetting stimulus.

Inflation is not a concern for 2012 but may become an issue as we head into the 2015 period. Employment levels in the United States and Canada would have to improve for inflation to become an issue, as would capacity utilization.

It would not be surprising to see the major Canadian banks shift more of their focus to the United States and other global markets where disruption in the global banking business may present compelling opportunities. Should European banks suffer a crisis of confidence, many quality customers may become available to more solid banks. In the United States there is already an interesting though risky opportunity to fill in where American banks are having to pull back due to financial difficulties. This may have some impact on the level of competition in the Canadian financial sector.

In the Canadian financial sector, we expect revenue growth to be constrained for a number of years due to moderate economic growth and historically low interest rates. Interest rates will likely remain at current levels until more progress is made in resolving the European situation.

Our Province

The forecast for Alberta is an economy that performs better than most of Canada, operating near full economic recovery but still below historic norms for this phase of the economic cycle. Forecast growth is lower than we had anticipated a year ago and the period of weaker performance could last for a number of years, depending on international developments.

The most compelling concerns are a significant recession in the United States, global disruption from a European sovereign debt crisis, much slower emerging market economies or the possibility that China has been stockpiling resources, which would cause a drop in price and demand when they stop.

We believe the major banks have identified Alberta as a top growth prospect for Canada, which means more intense competition for business as financial institutions seek to achieve their growth targets in this region.

Housing prices in Alberta are not as elevated as Vancouver or Toronto, however they are still quite high in terms of affordability. The most significant risk to housing prices is a large increase in interest rates or a sharp decrease in employment, which we do not foresee in 2012. Housing prices are not identified as an area of material risk for 2012, although we do recognize that they are high by historic standards and affordability measures, and the potential for correction is not insignificant.

Employment is strong in Alberta and the credit union believes that Alberta's economic prospects for the first half of 2012 are quite good. The credit union believes that Alberta should continue to benefit from demand in emerging markets and that the American economic situation has potential to deliver a gradual recovery but the real risk of significant global upheaval should the situation in Europe deteriorate further makes forecasting longer term more challenging.

2012-2014 Strategic Business Plan

In 2011, our credit union maintained an organizational-wide focus on several strategic priorities including Members First, Value Proposition, Long-Term Delivery Strategy, Leadership Development Strategy and the Fusion Program. In 2012, we'll continue to deliver on these priorities with the addition of two new priorities, Succession Planning and the development of a Corporate Social Responsibility Strategy. These strategic priorities are fundamental to our credit union making progress towards achieving our vision.

Servus selected its new banking system platform in 2010 and in 2011 embarked on a new program called Fusion. One of the 18 projects within Fusion is focused on harmonizing our operations on one core banking system. The implementation of the banking system is not simply a conversion to a new computer program. Rather, it is an opportunity to bring our three legacy credit unions together under one operating process and provide enhanced levels of service to our members. The name Fusion Program reflects the impact this program will have on our operations.

The program reached a checkpoint where the results of the core banking project were reviewed to ensure the expected functionality and timeline were still aligned with the original plan. Management concluded that the development effort required and risks associated with the conversion of three separate banking systems to the system originally selected cannot be resolved in a cost-effective and timely basis. Management will likely recommend an alternative core banking software solution for the banking system in 2012.

Servus will continue to use a balanced scorecard system, which allows us to measure and track our success. Also an effective and comprehensive forward-looking tool, the balanced scorecard provides Servus employees with a clear line of sight to what success means for our organization and our progress on achieving the plan under the following categories:

Member Experience
We will continue to enhance member experience by providing the most appropriate products, programs and services to meet members' expectations, diverse needs and changing lifestyles.

Employee Experience
We are proud that employees feel Servus provides a positive, safe, rewarding and engaging work environment. We will continue to invest in our employees through on-the-job experience, career opportunities, mentoring and leadership development programs. We will continue developing our employees to meet the plans of our credit union and to help them reach their potential.

Financial Performance
A credit union is a generational trust and must be operated with a plan to ensure long-term financial viability so that we are available to help the next generation of members. The stronger our performance and profitability, the more our member-owners gain through investment in products, services, our communities and our employees. In order to succeed in the long-term, we must reduce our dependency on interest-based income, broaden other sources of revenue and leverage our assets profitably.

Business Processes
We will continue to review and improve our business processes as measured by the operating efficiency ratio and operating expenses as a percent of average assets to ensure we can successfully address ongoing competition in price and service levels.

Governance and Credit Union Relations
Our Board of Directors is committed to providing guidance and direction through a superior governance model. As an organization, we are committed to being a leader in providing support and guidance to the entire credit union system.

In planning for our future, it remains crucial that we keep our focus on our vision, mission and values. We should celebrate the progress we have made in these past years and recognize that we continue to build the foundations of our organization so that, when we are fully integrated, we are ready to seize opportunities that will bring us closer to our vision.

Risk Management

Servus has in place a risk management structure that enables us to adapt to changes in economic and operational environments. The following is an overview of this structure and the types of risk we are typically exposed to. (See Note 25 on Financial Risk Management in the 2011 Consolidated Financial Statements for more details.)

Enterprise Risk Management
Servus uses an enterprise-wide approach to identify, measure, monitor and manage risk. We based this approach on the framework developed by the Committee of Sponsoring Organizations of the Treadway Commission, the recognized risk management control standard in the financial services sector.

The primary goals of risk management are to ensure that the outcomes of risk-taking activities are predictable and consistent with our credit union's objectives and risk tolerance, and that there is an appropriate balance between risk and reward to maximize value for our member-owners.

We believe that effective enterprise risk management is a journey and not a destination, so we continue to grow, evolve and adapt our risk management program. The framework we use provides processes to identify risks, assess the likelihood of their occurrence along with the impact of the risk, the potential impact on our operations, and to establish policies, procedures and controls to ensure that we manage risk within acceptable tolerances.

Servus' enterprise risk management governance model begins with oversight by the Board of Directors, either directly or through its committees, as shown in Figure 1.

The President and Chief Executive Officer (CEO) is responsible and accountable for risk management. Day-to-day responsibility is delegated to the Chief Risk Officer. Three management committees, the Asset Liability Committee, the Management Credit Committee and the Management Risk Committee identify, assign and monitor risks through their work. Ownership of key risks is delegated to the appropriate Executive Leadership Team member.

Risk Management Framework
Traditional risk management solutions tend to focus on negative events and often depend on diligent corporate compliance programs. Servus Credit Union's Enterprise Risk Management framework proactively elevates material risk issues to senior management and the Board. This helps Servus find a better balance between loss prevention, risk mitigation efforts and entrepreneurial risk-taking.

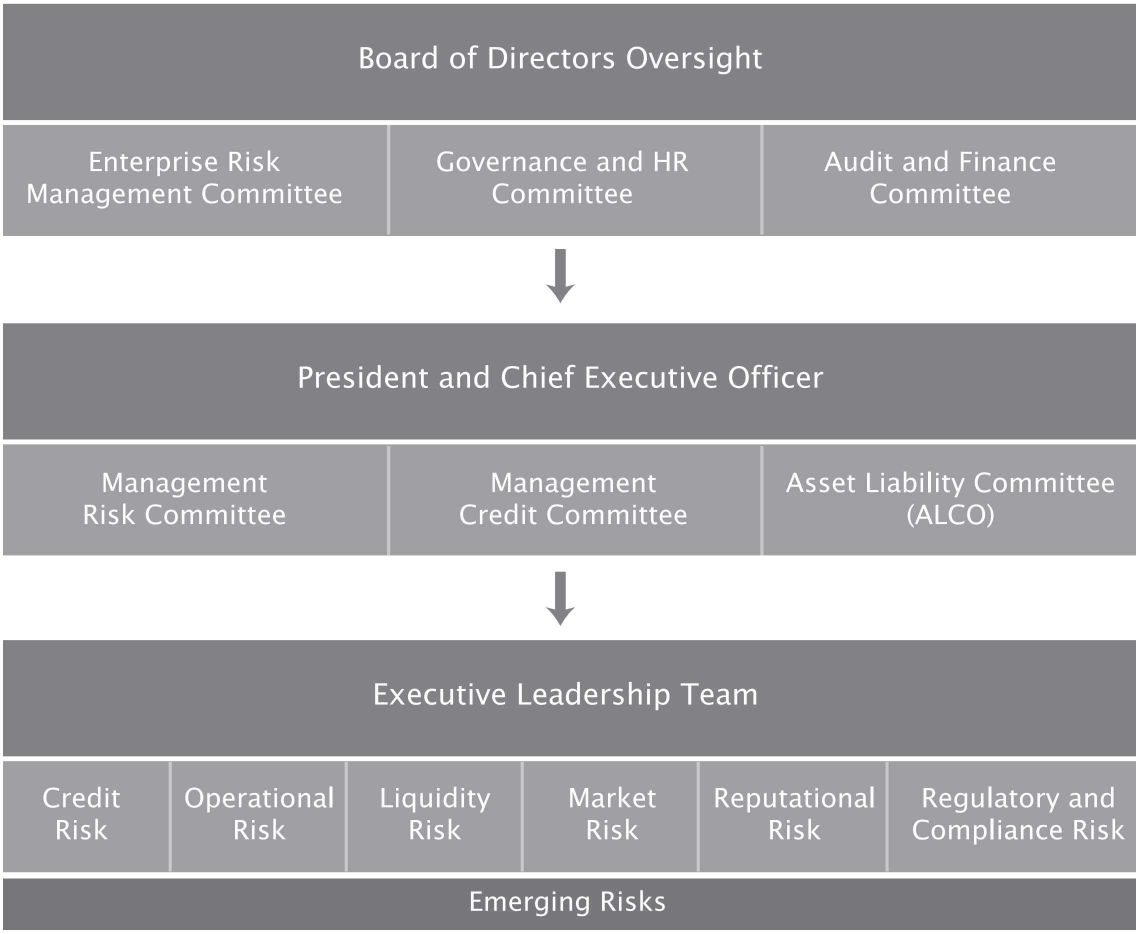

Figure 1—Servus Credit Union's Enterprise Risk Management Governance Model

Servus Credit Union's risk management framework has four cornerstones (see Figure 2). We review and update each cornerstone to ensure consistency with risk taking activities and relevance to our business and financial strategies, the Credit Union Deposit Guarantee Corporation (CUDGC) Standards of Sound Business Practices and the legislative environment.

Policies, Strategies and Limits
The governance, risk management direction and extent of Servus Credit Union's risk taking activities are established through policies, strategies and limits. Policies are also developed based on the requirement of the regulator and require input from the Board of Directors and senior management.

Guidelines
Guidelines are the directives provided to implement the policies. Generally, these describe types of risks and exposures, whether geographic or industry related.

Processes and Standards

Processes are the activities associated with identifying, evaluating, documenting, reporting and controlling risk. Standards define the breadth and quality of information required to make a decision and the expectations in terms of quality of analysis and presentation.

Measurement and Reporting

Servus monitors its risk exposure to ensure it is operating within approved limits or guidelines. Breaches, if any, are reported to senior management or Board committees (depending on the limit or guideline). Servus' internal audit department independently monitors the effectiveness of risk management policies, procedures and internal controls.

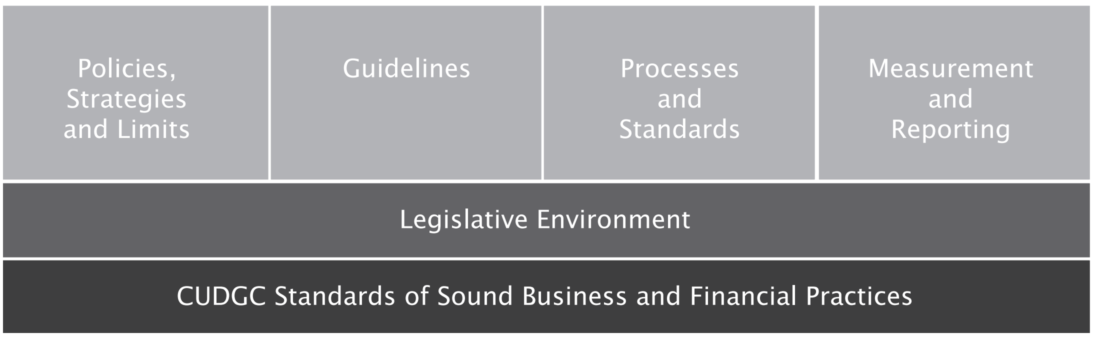

Figure 2—Servus Credit Union' Risk Management Framework

These four cornerstones, layered on the CUDGC framework and legislative environment, form the foundation of the Servus Risk Management Framework.

Types of Risk

Servus groups its major risks into seven categories:

1. **Credit Risk**

   Credit risk is the risk of financial loss resulting from the failure of an individual or business to honour an obligation to our credit union. Credit risk arises any time credit union funds are extended, committed, invested or otherwise exposed through actual or implied contractual agreements. Credit risk is found primarily in the lending portfolio but is also present in other transactions.

   Servus manages credit risk through policies and limits to ensure broad diversification across Alberta and within various industries and product mixes. We also manage risk through maximum limits on individual and connected accounts, participation in syndicated loans and minimum standards for loan quality. As well, Servus manages this risk through experienced and skilled lenders who have demonstrated experience, education and clearly documented decision-making authority, and through approval processes that include a Management Credit Committee.

2. **Operational Risk**

   Operational risk is the possibility that Servus may not be able to offer its products and services to members or continue to operate its business. It is also the risk of loss resulting from inadequate or failed internal processes, people and systems, or external events. While operational risk cannot be completely eliminated, proactive operational management is a key strategy to mitigate this risk.

Servus manages operational risk through a knowledgeable and experienced management team who are committed to the risk management policies and to promoting an ethical culture with clear communication to reinforce and guide our operational risk-taking activities. Our implementation of supporting policies and procedural controls include (among others) the segregation of duties and built-in systemic checks and balances. Additional controls include an established "whistleblower" process, an employee code of conduct, regular internal audits by an independent audit team and continual review and upgrade of systems and procedures.

3. Liquidity Risk

Liquidity risk is the possibility that Servus is unable to meet its financial obligations as they fall due. It entails:

- The sufficiency of the deposit base and/or other funding sources to maintain the asset base
- The risk of having insufficient liquid resources to meet our credit union's cash or funding requirements
- The risk of having insufficient liquid investments to meet statutory liquidity requirements

Servus' liquidity policies include the measurement and forecast of cash flows, a stable base of core deposits from retail and commercial customers, limits on single deposits and sources of deposits, and monitoring of wholesale demand and term deposits. The Servus liquidity management strategy includes the daily monitoring of expected cash inflows and outflows, and tracking and forecasting the liquidity position of our credit union on a forward 90-day rolling basis.

4. Market Risk

Market risk is the risk of financial loss resulting from changes to the value of assets or liabilities of Servus, most commonly through interest rate changes.

To manage interest rate risk effectively, the Asset Liability Committee establishes policy guidelines and meets regularly to monitor the Bank of Canada's position and to determine future strategies. The Board of Directors approves and reviews interest rate risk policies at least annually, with regular reporting provided to the Board's Enterprise Risk Management and Audit and Finance Committees.

5. Reputation Risk

Reputation risk is the risk to earnings and capital arising from negative public or stakeholder opinion. This can result from actual or alleged conduct in any number of activities, but often involves questions about business ethics and integrity, competence, corporate governance practices, quality and accuracy of financial reporting disclosures, or quality of products and service. Negative public or stakeholder opinion could adversely affect our ability to attract and keep members and could expose Servus to legal or regulatory action.

Servus manages and measures reputation risk by monitoring the external media environment, conducting regular surveys of members, non-members and employees, and through regular reporting by the Management Risk Committee. In addition, an employee code of conduct and corporate values enhance awareness of the types of behaviour that have the potential to harm our reputation and reinforce the standards and sound business practices we believe are essential to maintaining our reputation.

6. **Regulatory and Compliance Risk**
   Regulatory and compliance risk is the risk of Servus not fulfilling the requirements of external or internal regulatory functions. Regulatory risk differs from other banking risks such as credit risk or market risk in that it is typically not a risk actively or deliberately assumed by management in expectation of a return. Rather, it occurs as part of the normal course of operating our credit union.

   The Servus philosophy is to manage regulatory risk through a strong culture of integrity and sound controls. Business units and corporate areas are responsible for managing day-to-day regulatory and legal risk, while the compliance departments assist them by providing advice and oversight. Again, our code of conduct and corporate values help set the tone for a culture of integrity. The code stipulates that concern for what is right, including compliance with the law, should be the first consideration in all business decisions and actions. All directors, officers and employees are required to attest annually that they understand the code of conduct and comply with its provisions.

7. **Emerging Risks**
   Servus monitors and reports to both the Management Risk Committee and the Board Enterprise Risk Management Committee on risks that, although not fitting in any of the previous risk categories, may have an impact on its operations. These include changing economic conditions, impacts of geographic concentration within single industry locations, fraud and crime trends, and issues relating to the continuing consolidation through amalgamations.

   Although the use of metrics to measure emerging risk is relatively new and there are few proven methods for detecting leading indicators, we are working on developing qualitative and quantitative measures. Meanwhile, Servus uses measures such as personal bankruptcy rates, increases in unemployment and layoffs, changes in oil prices, housing starts and prices, and other indicators to identify issues and trends.

Corporate Governance

Servus Credit Union's Board of Directors represents our member-owners, ensuring they have a voice in the direction of their credit union. By adhering to the principles of openness, transparency, accountability, ethics and rule of law, they are a strong and effective governing body that keeps the best interests of our members top-of-mind.

Board Mandate

The Board of Directors ensures that Servus creates and maintains value for stakeholders and serves the needs of our member-owners and their communities. The Board sets our strategic direction, formulates and monitors policies, evaluates organizational performance and ensures that an effective risk management framework is in place.

The Board has adopted a policy governance model and functions in accordance with the Credit Union Act and Servus Credit Union bylaws. It is responsible for the election of the Board Chair and Vice Chair, and for selecting Directors to represent Servus on the Board of Credit Union Central of Alberta.

Board Structure

Servus Credit Union's Board of Directors is made up of 12 Servus member-owners. The Board has established committees to help govern the organization effectively and to better manage risk. There are three Board committees:

Audit and Finance Committee

The Audit and Finance Committee oversees the financial reporting process, reviews financial statements, liaises with internal and external auditors and regulators, and reviews internal control procedures. The committee consists of four Directors and the Board Chair, who serves as an ex-officio member, and an external resource who functions as an advisor to the Committee. Servus' senior management and external auditors also attend the Audit and Finance Committee meetings. The committee's terms of reference, guidelines and requirements are outlined in the Credit Union Act, regulations and bylaws. The Board defines the skills and abilities needed on the Committee and chooses its members accordingly.

Governance and Human Resource Committee

The Governance and Human Resource Committee establishes and maintains effective governance guidelines, ensures the performance and succession of senior leadership, and ensures compliance with the Credit Union Act, governance policies and Servus bylaws. This committee also serves as the Nominating Committee for the Director elections. It consists of four Directors and the Board Chair, who serves as an ex-officio member. The Board outlines their terms of reference, guidelines and requirements.

Enterprise Risk Management Committee

The Enterprise Risk Management Committee oversees the identification, understanding and management of risks that may affect Servus. It consists of four Directors and the Board Chair, who serves as an ex-officio member. The Board determines the Committee's terms of reference, guidelines and requirements.

The Board of Directors reviews the roles, responsibilities and membership of each Board committee on a yearly basis. In addition to these committees, the Board of Directors appoints qualified employees, as recommended by the President and Chief Executive Officer (CEO), to a Credit Committee. This committee authorizes loans within the limits established by the Board of Directors and provides a monthly written report to the Board.

Position Descriptions

Servus Credit Union's Directors provide strategic advice and business oversight of our operations. They are required to act honestly and in good faith with a view to the best interests of our credit union. They must exercise care, diligence and skill. The Board reviews the position descriptions for the Board Chair, Committee Chairs, Directors and the CEO annually.

Orientation and Education

New Directors of Servus Credit Union must complete an orientation session within two months of election and are encouraged to complete a policy governance course during their first year in office. We also expect our Directors to complete the online training curriculum of the Credit Union Director Achievement program within one year of their election.

We encourage all Directors to take part in educational opportunities such as those offered by the Institute of Corporate Directors, and industry related conferences, meetings and seminars. Further, we ask our Directors to participate in Community Council meetings.

These opportunities enable our Directors to develop their knowledge and skills and enhance their performance on the Board.

Ethical Conduct

The Board is committed to ethical, professional and lawful conduct. Our Directors work to ensure that Servus meets all public, regulatory and member expectations in compliance with existing laws.

Directors must represent loyalty without conflict to the interests of our members. This accountability comes before any personal interest. We require our Directors to declare any conflicts or perceived conflicts of interest immediately upon becoming aware of them.

Nomination

Servus holds an annual election to fill vacancies on the Board. Our member-owners elect Directors to a three-year term at the end of which they may run for re-election. Servus has no limit on the number of terms a Director may serve. The Governance and Human Resource Committee plays an active role in identifying potential candidates for the Board. Individuals interested in serving on the Board must submit nomination papers that provide detailed information such as educational background, a self-assessment of skills, knowledge and experience, and previous board experience. Candidates must also undergo a criminal records check.

We provide profiles on all Board candidates to our members in statement mailings, on the website and in our branches. Voting is held at every branch and online.

Director Remuneration

Servus provides each member of the Board with an honorarium for their activities during the course of their term. These activities include attending Board, committee and general meetings, branch openings, education and planning sessions and credit union system conferences. In addition, we reimburse Board members for all travel expenses and pay a meeting per diem.

Honorarium

Directors	$30,000 per annum
Vice Chair	$35,000 per annum
Chair	$40,000 per annum

Servus Credit Union's management (or a third-party consultant on behalf of Servus) conducts regular compensation reviews to help determine the appropriate rate of remuneration for the Board. We also participate in bi-annual national credit union surveys that look at Board remuneration.

Performance Evaluation

We evaluate the Board of Directors and the CEO each year to assess their effectiveness and to identify opportunities for improvement. Performance evaluations for the Board include a self-assessment tool as well as a peer review. Additional feedback is gathered for the Board Chair and each Board Committee regarding their performance and areas for improvement.

The Board assesses the CEO's performance each year by reviewing results against the Balanced Scorecard targets as well as looking at overall performance.

Board and Committee Meetings

The Board of Directors held six regular meetings in 2011 plus a two-day planning session in April.

During the year, the Audit and Finance Committee met 10 times, the Enterprise Risk Management Committee met 6 times, and the Governance and Human Resources committee met 8 times.

Directors participated in Servus' Annual General Meeting held in Edmonton in March 2011, the Credit Union Central of Alberta Conference and Annual General Meeting in April 2011, the Annual Canadian Credit Union Conference in May 2011 and the World Credit Union Conference in July 2011.

Future Changes in Accounting Policies

International Financial Reporting Standards

In February 2008, the Canadian Accounting Standards Board announced that Canadian Generally Accepted Accounting Principles (GAAP) for publicly accountable enterprises would be replaced by International Financial Reporting Standards (IFRS) for fiscal years beginning on or after January 1, 2011. Servus Credit Union meets the definition of a publicly accountable enterprise and will be required to transition its basis of accounting accordingly for the fiscal year ending October 31, 2012, as well as the October 31, 2011 comparative data. The date of transition is November 1, 2010.

IFRS uses a conceptual framework similar to Canadian GAAP; however, significant differences exist in certain matters of recognition, measurement and presentation. Adjustments required on transition to IFRS will be made retrospectively against opening retained earnings on the first comparative balance sheet. Transitional adjustments relating to those standards where comparative figures are required to be restated and applied retrospectively, will only be made as of the first day of the year of adoption. IFRS 1 "First-Time Adoption of International Financial Reporting Standards", provides entities adopting IFRS for the first time with a number of optional and mandatory exceptions in certain areas to the general requirement for full retrospective application of IFRS.

Project Scope

Servus Credit Union's project plan includes three phases: (1) scope and plan, (2) design and build, and (3) implement and review.

Scoping and planning includes the formation of a project team and the framework for completion of the project. It also includes identification of the standards that are expected to have a significant impact on the recognition, measurement, presentation and disclosure of our financial statements.

Design and building involves analysis of the policy choices and IFRS 1 elections required to be made at transition; identification and design of changes required to support accounting and reporting processes; identification and design of modifications to information technology systems and identification of data and training needs.

Key elements in the implementation and review phase are the implementation of changes to accounting policies and practices, updating of documentation and delivery of required training to staff.

Progress towards completion

Servus completed the scope and plan phase in 2010. A project team was set up and a timeline for key deliverables established. A steering committee was also established, which meets monthly and the Audit and Finance Committee receive updates on a monthly basis.

Servus assessed and selected its accounting policy choices under IFRS, including the IFRS 1 elections and communicated those choices to the Audit and Finance Committee. In addition we assessed the differences between all the standards that were considered to have an impact on the credit union and are working on finalization of the quantitative adjustment on transition.

No significant changes to information technology systems have been identified. Minor changes to accounting systems, including amendment of reports, along with changes to procedures and policies have been identified and are in the process of being implemented. Training to staff affected by the changes has begun and will continue to be provided during 2012. Changes to policies, procedures and documentation will be introduced in conjunction with the credit union's control environment project during 2012.

Transition Adjustments

During 2011 the project team worked on quantifying the impact of transition on Servus Credit Union's opening balance sheet. The following have been identified as the areas where an adjustment will be made on transition. The areas have not been audited by the credit union's external auditor and the final amounts are still subject to change:

Allowance for credit losses

Under both Canadian GAAP and IFRS, allowances for credit losses are determined based on an incurred loss model. Management is in the process of updating its loan loss model to provide greater justification for support for the specific and collective allowances based on indicators of delinquency.

In addition, unlike Canadian GAAP, IFRS requires that interest on impaired loans continues to be accrued and allows impairment losses to be reversed when events confirm that a recovery has occurred. These differences are being addressed as part of the update of the loan loss allowance model and should any transactional differences be identified, they will be reflected in the allowance for credit losses and retained earnings on the statement of financial position.

Transaction costs on financial instruments
Under Canadian GAAP, the credit union was able to capitalize transaction costs on derivative financial instruments and amortize the costs over the life of the instrument. Under IFRS transaction costs on any instrument that is classified as held at fair value through profit or loss must be expensed on recognition. On transition Servus will recognize a reduction in other assets and retained earnings.

Embedded derivatives
Under IFRS, contracts that contain embedded derivatives must be assessed to determine whether the embedded derivative should be separately recognized as a derivative financial instrument. Similar requirements existed in Canadian GAAP when CICA Handbook Section 3855, Financial Instruments was issued. However as allowed by Canadian GAAP, Servus was permitted to limit its search for embedded derivatives to transactions occurring after November 1, 2002. Management is in the process of reviewing its remaining contracts for embedded derivatives. Based on items currently identified Servus expects to recognize an increase in derivative financial assets and retained earnings on transition.

Classification of member shares
Under Canadian GAAP, Servus classified its member investment shares as equity. However, under IFRS member shares that contain a right to redemption are treated as a compound instrument. Servus has identified only one class of shares that contain a right to redemption and on transition a portion of the Investment Shares Series E will be classified as a financial liability. This financial liability will be designated as held-at-fair-value through profit or loss. On transition there is no impact on retained earnings from the reclassification.

Website costs
IFRS provides different criteria than Canadian GAAP on the ability to capitalize website costs, at each stage of the project. Servus has reviewed and amended its capitalization policy in line with the additional guidance. On transition Servus will recognize a reduction in intangible assets and retained earnings.

Impairment of non-financial assets
IFRS requires an impairment to be recognized when the recoverable value of an asset is lower than its carrying amount and does not contain an initial review of whether undiscounted cash flows exceed an asset's carrying amount. There are also differences in the level at which assets are grouped into a cash generating unit under IFRS compared to an asset group under Canadian GAAP. IFRS also allows an impairment to be reversed if the circumstances that caused the impairment no longer exist, which was not allowed under Canadian GAAP. On transition Servus will recognize an increase in retained earnings and property and equipment as a result of the reversal of impairments previously recognized under Canadian GAAP.

Employee benefits
Under IFRS Servus has the accounting policy choice to continue with the corridor method for recognition of actuarial gains and losses on its defined benefit plans or to recognize all them as they arise in other comprehensive income. Servus has elected to change its policy on transition to immediate recognition in other comprehensive income. As allowed by IFRS 1, Servus has also elected to recognize all previously unrecognized actuarial gains and losses at the date of transition, resulting in an increase in employee benefits liability and a reduction in retained earnings.

The following IFRS 1 elections will be taken that did not have any impact on retained earnings on transition:

Securitization
Under Canadian GAAP, recognition of an asset is dependent on which party has control over the asset. IFRS considers whether the risks and rewards of ownership have been retained in determining whether an asset should be derecognized. IFRS 1 contains an election to not re-recognize an asset at transition that was derecognized under previous Canadian GAAP. Servus has chosen to take this IFRS 1 election and, as a result, mortgages that were the subject of securitization transactions prior to transition will not be brought back onto the balance sheet.

Classification of financial instruments
IFRS 1 permits the re-designation of any financial asset of liability as either available-for-sale or held-at-fair-value through profit or loss. Under previous Canadian GAAP, Servus had classified its retained rights to future excess spread financial asset as held for trading. As there is no recent history of profit taking the asset does not meet the criteria for classification as held for trading under IFRS. As a result Servus has chosen to reclassify the retained rights to future excess spread as designated at fair value through profit or loss on transition. As the asset was previously classified as held-for-trading and measured at fair value there will be no impact on retained earnings on transition.

Other adjustments
Servus Credit Union has investment in associates that are also transitioning to IFRS, and is working with its associates to identify the impact of their transition adjustments on Servus' financial statements.

Deferred taxes have also been reviewed to consider the adjustments identified.

In addition to the adjustments noted above, there will be a number of presentation adjustments in order to comply with IFRS disclosure requirements. These will have no impact on retained earnings. As part of the design and build phase Servus has developed a mock set of financial statements prepared under IFRS disclosure requirements and has identified changes to documentation and procedures in order to collect information required to support additional disclosure requirements.

The impact on transition and future impact of each change is being finalized and will be reported in fiscal 2012.

SERVUS CREDIT UNION LTD.
Consolidated Financial Statements

For the year ended October 31, 2011

SERVUS CREDIT UNION LTD.
Management's Responsibility for Financial Reporting

These Consolidated Financial Statements have been prepared by the management of Servus Credit Union Ltd. (the Credit Union) who are responsible for their reliability, completeness and integrity. They were developed in accordance with requirements of the Credit Union Act of Alberta and conform in all material respects with Canadian generally accepted accounting principles.

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 organization. These systems include establishment and communication of standards of business conduct through all levels of the organization to prevent conflicts of interest and unauthorized disclosure and to provide assurance that all transactions are authorized and proper records maintained. Internal audit is one method that provides management with the ability to assess the adequacy of these controls. Further, the systems of internal control are reviewed by the Credit Union's external auditors to the extent necessary to render their opinion on the Consolidated Financial Statements.

The Board of Directors has approved the Consolidated Financial Statements. The Audit and Finance Committee of the Board has reviewed the Consolidated Financial Statements with the independent external auditors in detail, and received regular reports on internal control findings from the internal auditor. Deloitte & Touche LLP, the independent external auditors appointed by the Board of Directors, examined the Consolidated Financial Statements and accompanying notes of the Credit Union in accordance with Canadian generally accepted auditing standards. They have had full and free access to the internal audit staff, other management staff and the Audit and Finance Committee. Their audit report outlines the scope of their examination and their opinion.

Garth Warner
President & Chief Executive Officer (CEO)

Ian Glassford, MBA, CMA
Chief Financial Officer (CFO)

Edmonton, Alberta
January 26, 2012

SERVUS CREDIT UNION LTD.
Independent Auditor's Report

To the Members of
Servus Credit Union Ltd.

We have audited the accompanying consolidated financial statements of Servus Credit Union Ltd., which comprise the Consolidated Balance Sheet as at October 31, 2011, and the Consolidated Statements of Income and Comprehensive Income, Changes in Members' Equity, and Cash Flows for the year then ended, and 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 Canadian generally accepted accounting principles, 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.

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Servus Credit Union Ltd. as at October 31, 2011 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Edmonton, Alberta
January 26, 2012

SERVUS CREDIT UNION LTD.
Consolidated Balance Sheet
As at October 31, 2011
($ thousands, except share information)

	Notes	2011	2010
Assets			
Cash		$ 118,667	$ 144,231
Investments	5	770,030	890,647
Investment under equity method	5	124,288	115,077
Member loans	6,7,8	9,957,017	9,364,724
Foreclosed assets	6	16,136	9,993
Property and equipment	9	199,380	198,322
Property and land available for sale	9	3,155	9,352
Intangible assets	10	13,606	13,112
Other assets	11	32,252	41,290
Total assets		11,234,531	10,786,748
Liabilities			
Member deposits	12	10,208,814	9,831,908
Accounts payable and other liabilities	13	142,440	122,645
Term loans payable	14	4	—
Total liabilities		10,351,258	9,954,553
Guarantees, commitments and contingent liabilities	20		
Member Equity			
Share capital	15	464,896	439,967
Retained earnings		417,343	392,228
Total equity attributable to equity holders of the Credit Union		882,239	832,195
Non-controlling interest		1,034	—
Total member equity		883,273	832,195
Total liabilities and member equity		$ 11,234,531	$ 10,786,748

The accompanying notes are an integral part of the Consolidated Financial Statements.

Approved on behalf of the Board of Directors

Peter Elzinga
Chair, Board of Directors

Alison L. C. Starke

Alison Starke
Chair, Audit and Finance Committee

SERVUS CREDIT UNION LTD.
Consolidated Statement of Income and Comprehensive Income
For the year ended October 31, 2011
($ thousands, except share information)

	Notes	2011	2010
Interest income			
Member loans		**$ 442,143**	$ 419,648
Investments		**8,567**	4,722
Total interest income		**450,710**	424,370
Interest expense			
Member deposits		**149,635**	140,286
Term loans		**311**	1,916
Total interest expense		**149,946**	142,202
Net interest income		**300,764**	282,168
Provision for credit losses	7	**16,416**	11,405
Net interest income after provision for credit losses		**284,348**	270,763
Other Income - equity investments	5	**6,121**	4,623
Other Income	17	**70,769**	70,666
Net interest income and other income		**361,238**	346,052
Operating expenses			
Personnel		**157,717**	146,801
General	18	**69,087**	56,628
Occupancy		**18,373**	17,667
Member security		**17,920**	18,719
Depreciation	9	**15,108**	14,694
Organization		**4,602**	4,198
Amortization	10	**2,047**	2,048
Total operating expenses		**284,854**	260,755
Income before patronage allocation to members and income taxes		**76,384**	85,297
Patronage allocation to members	15	**25,121**	23,642
Income before income taxes		**51,263**	61,655
Income taxes	19	**10,946**	12,135
Net income		**40,317**	49,520
Other comprehensive income		**—**	—
Total comprehensive income		**$ 40,317**	$ 49,520

The accompanying notes are an integral part of the Consolidated Financial Statements.

SERVUS CREDIT UNION LTD.
Consolidated Statement of Members' Equity
For the year ended October 31, 2011
($ thousands, except share information)

	Notes	2011	2010
Share Capital			
Common Shares			
Balance, beginning of year	15	**$ 334,745**	$ 303,950
Issued and redeemed for cash, net	15	**9,422**	17,156
Provision for dividends distributable	15	**13,912**	13,639
Balance, end of year	15	**358,079**	334,745
Investment Shares			
Balance, beginning of year	15	**105,222**	102,790
Issued and redeemed for cash, net	15	**(3,119)**	(2,484)
Provision for dividends distributable	15	**4,714**	4,916
Balance, end of year	15	**106,817**	105,222
Share Capital, end of year		**464,896**	439,967
Retained Earnings			
Balance, beginning of year		**392,228**	357,913
Net income		**40,317**	49,520
Provisions for dividends on common shares		**(13,912)**	(13,639)
Provisions for dividends on investment shares		**(5,332)**	(5,606)
Income tax recovery thereon		**4,042**	4,040
Retained Earnings, end of year		**417,343**	392,228
Total Equity Attributable To Equity Holders of the Credit Union		**882,239**	832,195
Non-Controlling Interest			
Non-controlling Interest		**1,034**	—
		1,034	—
Accumulated Other Comprehensive Income, end of year		—	—
Total Member's Equity		**$ 883,273**	$ 832,195

The accompanying notes are an integral part of the Consolidated Financial Statements.

SERVUS CREDIT UNION LTD.
Consolidated Statement of Cash Flows
For the year ended October 31, 2011
($ thousands, except share information)

	Notes	2011	2010
Cash Flows From (Used in) Operating Activities:			
Operating net income		**$ 40,317**	$ 49,520
Adjustments for:			
Depreciation	9	**15,108**	14,694
Amortization	10	**2,047**	2,048
Impairment on property and equipment	9	**1,036**	725
Impairment on intangible assets	10	**10,281**	—
Future income taxes	19	**(1,466)**	1,511
Provision for credit losses	7	**16,416**	11,405
Investment income from equity method investments	5	**(6,121)**	(4,623)
Loss on acquisition of Apex Credit Union Ltd		—	1,550
Loss/(Gain) on sale of property and equipment		**472**	(535)
Net change in other assets and accounts payable and other liabilities		**27,308**	(1,200)
Net change in accrued interest on member loans		**325**	(3,467)
Net change in accrued interest on member deposits		**(7,109)**	(11,027)
Net change in accrued interest on term loans		—	(4)
Net change in accrued interest and dividends on investments		**(196)**	24
Operating Activities		**98,418**	60,621
Cash Flows From (Used in) Investing Activities			
Additions to intangible assets		**(12,822)**	(9,144)
Additions to property, equipment and property available for sale		**(14,179)**	(23,410)
Acquisition of 1358938 Alberta Ltd		—	(535)
Proceeds on disposal of property, equipment and available for sale assets		**2,702**	9,073
Member loans		**(615,177)**	(411,323)
Cash acquired from business combinations		**3,250**	355
Investments, net		**117,723**	(161,324)
Investing Activities		**(518,503)**	(596,308)
Cash Flows From (Used in) Financing Activities			
Advances of term loans payable and line of credit		**4**	284,050
Repayment of term loans payable		—	(303,608)
Member deposits		**384,015**	508,937
Repayment of obligation under capital lease	13	**(259)**	(249)
Non-controlling interest		**1,034**	—
Dividends paid on investment shares	15	**(618)**	(690)
Shares, issued and redeemed, net	15	**6,303**	11,951
Income tax recovery		**4,042**	4,040
Financing Activities		**394,521**	504,431
Decrease in Cash		**(25,564)**	(31,256)
Cash, beginning of year		**144,231**	175,487
Cash, End of year		**$ 118,667**	$ 144,231
Supplementary cash flow information			
Interest paid during the year		**$ 157,055**	$ 153,233
Interest and dividends received during the year		**450,839**	422,169
Income taxes paid during the year		**6,831**	14,125

The accompanying notes are an integral part of the Consolidated Financial Statements.

1. INCORPORATION AND GOVERNING LEGISLATION

Servus Credit Union Ltd. (Servus or the Credit Union) is incorporated under the Credit Union Act of the Province of Alberta (the Act). The Credit Union serves members across Alberta.

The Credit Union Deposit Guarantee Corporation (the Corporation), a provincial corporation, guarantees the repayment of all deposits with Alberta credit unions, including accrued interest. The Act provides that the Province will ensure that the Corporation carries out this obligation.

2. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES

CICA Handbook Section 3855, Financial Instruments – Recognition and Measurement (Section 3855) - In June 2009, the CICA provided a clarification to Section 3855 with respect to the embedded prepayment option. An embedded prepayment option is an interest-only or principal-only strip that is closely related to the host contract, provided the host contract initially resulted from separating the right to receive contractual cash flows of a financial instrument that, in and of itself, did not contain an embedded derivative; and does not contain any terms not present in the original host debt contract. The Credit Union concluded that the impact of the clarification is not material to the Consolidated Financial Statements.

3. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation
The Consolidated Financial Statements of the Credit Union have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP) on a going concern basis.

The preparation of the Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income, expenses and disclosures at year end. Certain estimates, including allowance for credit losses, fair value of financial instruments, income taxes, accounting for securitizations, defined benefit pension plans, post retirement benefits, contingent liabilities, accrued liabilities, and the useful life of property, equipment, intangible assets and impairment of long lived assets require management to make subjective or complex judgements. Accordingly, actual results could differ from those estimates.

The significant accounting policies and practices used by the Credit Union are:

Basis of Consolidation
The Consolidated Financial Statements include the assets, liabilities, income and expenses of subsidiaries, and variable interest entities of which the Credit Union is determined to be the primary beneficiary. All intercompany balances and transactions are eliminated on consolidation.

Included in the Consolidated Financial Statements are the accounts of the Credit Union and the following entities:

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Subsidiaries
The Credit Union has 100% ownership in Home Start Financial Ltd., Community Agencies Ltd. operating as All Source Mortgages and Servus Wealth Strategies Ltd. These entities provide mortgage brokerage and wealth management services to a number of lenders, including the Credit Union. The Credit Union also has 100% ownership of 135938 Alberta Ltd. which provides the Credit Union with air transportation services. During 2011, the Credit Union has obtained a 51% ownership of 1626210 Alberta Ltd., which is a start-up company and owns properties on behalf of the Credit Union.

Interest in the equity of a subsidiary not attributable to the parent of $1,034 is reported in Member Equity as Non-controlling interest.

Variable Interest Entities
The Credit Union is considered to be the primary beneficiary of three registry services which have been consolidated.

Financial Instruments - Recognition and Measurement
Financial assets and financial liabilities, including derivatives, are recognized on the Consolidated Balance Sheet when the Credit Union becomes a party to the contractual provisions of a financial instrument or non-financial derivative contract. The Credit Union recognizes financial instruments at the trade date. All financial instruments are initially measured at fair value. Subsequent measurement is dependent upon the financial instrument's classification. Transaction costs are capitalized on initial recognition.

Held-For-Trading
Financial assets and financial liabilities classified as Held for Trading are measured at fair value with changes in those fair values recorded in Other income. Cash, retained rights to future excess spread on securitized residential mortgages and derivative financial instruments are classified as held for trading.

Held-To-Maturity
If the Credit Union has positive intent and ability to hold the investment to maturity, then they are classified as held-to-maturity. Held-to-maturity investments are measured at amortized cost.

Available-For-Sale
Debt securities and equity securities are classified as available-for-sale and are measured at estimated fair value. The Credit Union uses current market interest rate quotation to estimate the fair values of these investments. Unrealized gains and losses, net of taxes, are reported in Other comprehensive income.

Other investments (Note 5) include investments in companies that are not traded on an active market and these investments are classified as available-for-sale. These investments are carried at cost. Gains, losses and realized sales are recognized in the Net income when the investment is derecognized or impaired.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Loans and Receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortized cost. Loans and receivables include Credit Union Central of Alberta (Alberta Central) term deposits, debentures, mortgage pools, accounts receivable and member loans.

Financial Liabilities
Financial liabilities are measured at amortized cost. Financial liabilities include member deposits, accounts payable, term loans payable and other liabilities.

Impairment of Financial Assets
Financial assets, other than loans and receivables, are assessed at each reporting date to determine whether there is any objective evidence that they are impaired. Financial assets are considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset. An impairment loss in respect of financial assets measured at amortized cost is calculated as the difference between the carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. An other than temporary impairment loss in respect of an available-for-sale financial asset is calculated by reference to its current fair value. Any cumulative loss in respect of available-for-sale financial assets recognized previously in Accumulated other comprehensive income is transferred to the Net income. All impairment losses are recognized in the Net income for the year. The Credit Union has not recorded any impairment on financial assets other than Member loans as of October 31, 2011.

Cash
Cash is comprised of cash on hand, the current account with Alberta Central and items in transit.

Investments under Equity Method
Investments in entities over which the Credit Union exercises significant influence are accounted for using the equity method and are presented in Investments in the Consolidated Balance Sheet. The Credit Union's share of income (loss) from these entities is included in Interest income-investments in the Consolidated Statement of Income and Comprehensive Income. Dividends received are recorded as a reduction in Investments.

Investment Income
Interest is recorded on an accrual basis using the effective interest method. Dividends are recorded as declared. Gains and losses on the sale of investments are reflected in Interest income on disposition in the Consolidated Statement of Income and Comprehensive Income.

Derivative Financial Instruments
Derivative financial instruments are financial contracts whose value is derived from an underlying interest rate, foreign exchange rate, equity instrument or index. The Credit Union periodically enters into derivative contracts to manage financial risks associated with movements in interest rates and other financial indices. The Credit Union does not use derivative financial instruments for trading or speculative purposes. The Credit Union uses quotations based on current observable market data to estimate the fair value of all derivative financial instruments.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivative Financial Instruments (continued)

Derivative financial instruments are measured at fair value and are recorded on the Consolidated Balance Sheet. Derivatives with a positive fair value are recorded in Other assets. Derivatives with a negative fair value are recorded in Accounts payable and other liabilities. Gains and losses on derivative financial instruments are recorded in Other income on the Consolidated Statement of Income and Comprehensive Income.

Derivative financial instruments may also be embedded in other financial instruments. Derivative financial instruments embedded in other financial instruments are separated from the host contracts and are accounted for as a derivative financial instrument when their economic characteristics and risks are not closely related to those host contracts, when it meets the definition of a derivative financial instrument and when the host contract is not accounted for as held-for-trading.

Term deposit obligations that are linked to the performance of certain equity indexes contain embedded derivatives and are measured at fair value with changes to those fair values recorded in Other income on the Consolidated Statement of Income and Comprehensive Income. This income item is offset by the derivatives used to hedge the deposit and these derivatives are measured at fair value.

Foreign currency forward agreements are used to manage the foreign exchange rate exposure from foreign currency denominated assets and liabilities. These derivative financial instruments are recorded at fair value and changes in those fair values are recorded in Other income on the Consolidated Statement of Income and Comprehensive Income. The Credit Union does not have any foreign currency forward agreements as of October 31, 2011.

The premiums paid to enter into these contracts are recorded in Other assets and are amortized over the contract life. Income and expenses associated with these contracts are accounted for on an accrual basis and recognized over the life of the contract as an adjustment to Other income.

Member Loans

Member loans are recorded at amortized cost, less any allowance for credit losses plus accrued interest. Member loans considered uncollectible are written off.

Interest income from loans is recorded using the accrual method basis, except when a loan is impaired. A loan is classified as impaired when, in management's opinion, there has been deterioration in credit quality to the extent that there is no longer reasonable assurance as to the timely collection of the full amount of principal and interest. Loans where interest or principal is contractually 90 days past due are recognized as impaired unless management determines that the loan is fully secured and in the process of collection. Fully secured loans are classified as impaired after a delinquency period of 180 days. Once a loan is classified as impaired, all previously accrued interest is reversed and charged against current income, except for loans fully secured.

Foreclosed assets are recorded initially at the lesser of outstanding loan principal or fair value less costs to sell. Any subsequent decline in fair value impacts the specific provision for foreclosed assets.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Member Loans (continued)

Certain loan fees are deferred and recorded as Interest income over the terms of the underlying loans using the effective interest method. Mortgage prepayment penalties are included in income when charged.

Allowance for Credit Losses

The Credit Union maintains an allowance for credit losses in an amount considered adequate to absorb credit losses existing in its loan portfolio. The allowance is increased by a provision for credit losses which is charged to the Consolidated Statement of Income and Comprehensive Income, and reduced by write-offs net of recoveries.

The allowance for credit losses consists of specific allowances and a general allowance, each of which is reviewed on a regular basis. Specific allowances include all the accumulated allowances for losses on particular loans required to reduce the carrying amount of these loans to their estimated realizable values. Estimated realizable values are generally determined by discounting the expected future cash flows at the effective interest rate inherent in the loans. When the amounts and timing of future cash flows cannot be reliably established, estimated realizable values are determined by reference to market prices for the loans or their underlying security.

Specific allowances are determined on a loan by loan basis except for certain groups of loans which are determined by a method taking into account recent loss experience. The general allowance is established by taking into consideration historical trends in the loss experience during economic cycles, historical experience in the industry, the current portfolio profile, and management's evaluation of other conditions existing at the balance sheet date which are not reflected in historical trends.

During 2011, management refined its methodology to estimate the general allowance for credit losses. The changes made to the methodology were based on experience with write offs and consideration of larger specific allowances for credit losses.

Mortgage Securitizations

The Credit Union periodically securitizes groups of residential mortgages by selling them to unrelated third parties. These transactions are accounted for as sales and the related mortgages are removed from the Consolidated Balance Sheet when control over the mortgages is surrendered and consideration other than beneficial interests in the transferred mortgages is received in exchange. The third parties, as holders of the securitized mortgages, have recourse only to cash flows for the securitized mortgages. The investors and the third parties have no recourse to the Credit Union's other assets.

The fair values of mortgages sold and retained interests are determined using pricing models based on key assumptions such as expected losses, prepayments and discount rates that are commensurate with the risks involved. The carrying value of retained interests is reviewed annually for impairment which is charged to the Consolidated Statement of Income and Comprehensive Income. These financial instruments are designated as held-for-trading and are measured at fair value, and changes in fair value are recognized to Other income.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Mortgage Securitizations (continued)

Gains and losses on these transactions are recorded in Other income in the Consolidated Statement of Income and Comprehensive Income and are recorded on the date of the transaction. The amount of these gains or losses are based on the present value of expected future cash flows using management's best estimates of key assumptions such as prepayment rates, excess spread, credit losses and discount rates. Gains and losses on these transactions that have retained interest are based on the carrying value of the mortgages transferred allocated between the assets sold and the retained interests in proportion to their fair value at the date of transfer. Gain and losses on transactions that do not have a retained interest are based on the proceeds of the sale compared with the carrying value of the mortgages at the date of the sale.

The premiums and retained servicing liability are recorded in Accounts payable and other liabilities on the Consolidated Balance Sheet and are amortized over the term of the transferred mortgages to Other income.

Property and Equipment

Land is carried at cost. Buildings, furniture, office equipment, vehicles, leasehold improvements, computer equipment, equipment under capital lease, airplane and real estate investment properties are carried at cost, less accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the related assets as follows:

Buildings	20 to 40 years
Furniture, office equipment and vehicles	3 to 20 years
Leasehold improvements	Term of lease
Computer equipment	3 to 5 years
Equipment under capital lease	5 years
Airplane	10 years
Real estate investment properties	30 years

Depreciation is recorded commencing in the month after the acquisition; no depreciation is recorded in the month of the disposal. Gains and losses on disposal are recorded in Other income in the Consolidated Statement of Income and Comprehensive Income.

Property and Land Available For Sale

Property and land classified as available for sale are those assets whose carrying amounts will be recovered principally through a sale transaction rather than through continuing use. These assets are stated at the lower of their carrying amount and fair value less costs to sell and are not depreciated. An impairment loss is recognized for any initial or subsequent write-down of the asset to fair value less costs to sell. A gain is recognized for subsequent increases in fair value less costs to sell an asset but not exceeding any cumulative impairment losses previously recognized.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible Assets

Intangible assets with a finite life are amortized to the Consolidated Statement of Income and Comprehensive Income over their expected lives not exceeding five years. These intangible assets are tested for impairment whenever circumstances indicate that the carrying amount may not be recoverable. Any impairment of other intangible assets will be charged to Operating expenses — general in the Consolidated Statement of Income and Comprehensive Income in the period of impairment. The estimated useful life on software under development will be determined when the assets are placed in use, therefore no amortization has been taken on these assets. Intangible assets with an indefinite life are not amortized, but are subject to a fair value impairment test at least annually.

Leases

Leases that transfer substantially all the benefits and inherent risks of ownership of the property to the Credit Union are recorded as capital leases. The present value of the payments under the leases is included in Property and Equipment and the obligation under capital lease is included in Accounts payable and accrued liabilities on the Consolidated Balance Sheet. All other leases are classified as operating leases, in which case the total expense to be paid over the lease term is amortized on a straight line basis over the lease term.

Impairment of Long-Lived Assets

The Credit Union evaluates the carrying value of long lived assets including property and equipment and finite life intangible assets including those under development whenever events or changes in circumstances indicate that the carrying value may not be recoverable. In cases where the undiscounted expected cash flows are less than the carrying amount, an impairment loss is recognized. Impairment losses on long-lived assets are measured as the amount by which the carrying value of an asset group exceeds its fair value, as determined by discounted cash flows of the asset group.

Employee Future Benefits

The Credit Union provides certain pension and other benefits to employees as follows:

Defined Contribution Registered Retirement Savings Plan

The Credit Union offers employees a defined contribution registered retirement savings plan where contributions are made by both the Credit Union and the employee. Contributions are based on a percentage of salary and no further contributions are required once the employee retires or leaves the Credit Union.

Defined Benefit Plans

The Credit Union provides a defined benefit supplemental plan and a post-retirement benefits plan to qualifying employees. Post-retirement benefits include extended health care, dental and life insurance. The cost of benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of turnover rates, salary escalation, retirement ages, expected health care costs, and other actuarial factors. Net actuarial gains or losses in excess of 10% of the greater of the accrued benefit obligation and the fair value of plan assets at the beginning of the year are amortized over the expected average remaining service life of the employee group. Transitional obligations are amortized in the same manner.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Variable Interest Entities
Variable interest entities (VIEs) are entities in which equity investors do not have a controlling financial interest or the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support provided by other parties. On an annual basis, the Credit Union identifies VIEs in which it has an interest, determines whether it is the primary beneficiary of such entities, and if so, consolidates them. The primary beneficiary is an entity that is exposed to a majority of the VIEs' expected losses or entitled to a majority of the VIEs' expected residual returns or both.

Income Taxes
The Credit Union follows the asset and liability method of accounting for income taxes whereby future income taxes are determined based on the difference between the carrying values of assets or liabilities and their tax basis using the substantively enacted tax rates expected to be in effect when the asset or liability is expected to be settled. Future income taxes are reported in Other assets or Accounts payables and other liabilities on the Consolidated Balance Sheet.

Translation of Foreign Currencies
Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates prevailing on the balance sheet date. Income and expenses denominated in foreign currencies are translated into Canadian dollars at average exchange rates for the year. Gains and losses resulting from translation are recorded in Other income in the Consolidated Statement of Income and Comprehensive Income.

Comparative Figures
Certain comparative figures are reclassified, where appropriate, to conform to the current's year Consolidated Financial Statement presentation.

4. FUTURE ACCOUNTING CHANGES

Future Changes in Accounting Policies – Transition to International Financial Reporting Standards
Canadian publicly accountable enterprises must transition to International Financial Reporting Standards (IFRS) for fiscal years beginning on or after January 1, 2011. As a result, the Credit Union will adopt IFRS commencing November 1, 2011. Upon adoption, the Credit Union will provide comparative financial information also prepared in accordance with IFRS.

($ thousands, except share information)

5. INVESTMENTS AND INVESTMENTS UNDER EQUITY METHOD

Investments

	2011	2010
Alberta Central term deposits (Note 27)	**$ 764,885**	$ 879,635
Mortgage pools	**1,869**	8,034
Debentures	**1,250**	1,250
Other investments	**996**	894
	769,000	889,813
Accrued interest	**1,030**	834
Total	**$ 770,030**	$ 890,647

As required by the Act, the credit union maintains its statutory liquidity investments in Alberta Central.

Investments under Equity Method

	2011	2010
Alberta Central shares (Note 27)	**$ 123,448**	$ 113,439
Investment in Crelogix (Note 27)	**840**	1,638
Total	**$ 124,288**	$ 115,077

As of October 31, 2011, the Credit Union owned 55.5% (2010 – 54.7%) of the common shares outstanding of Alberta Central. Due to the governance structure of Alberta Central, management has determined that the Credit Union has significant influence, but not control, over Alberta Central. The investment in Alberta Central shares is accounted for using the equity method. In 2011, the Credit Union bought $5,073 in Alberta Central shares, acquired additional Alberta Central shares of $333 from the acquisitions of Credit Unions (Note - 28), and recorded a dividend of $1,305 (2010 - $1,350) (Note - 11). Included in Other income for 2011 is net income of $5,908 (2010 - $4,388) which represents the Credit Union share of the net income from Alberta Central.

As of October 31, 2011, the Credit Union owned 36.0% (2010 – 36.0%) of the common shares outstanding of Crelogix and this investment is accounted for using the equity method. During the year, Crelogix repurchased shares from all the shareholders. The Credit Union’s percentage of ownership in Crelogix remained the same before and after the repurchase. Included in Other income for 2011 is net income of $213 (2010 - $235) which represents the Credit Union’s share of the net income from Crelogix. In 2011, the Credit Union sold $1,011 in Crelogix shares and recorded a loss on the sale of shares of $21 (2010 - $nil) which is recorded in Other income. The cost of the shares sold was $782.

As of October 31, 2011, the cost of the investment in Alberta Central and investment in Crelogix is respectively $107,859 (2010 - $102,453) and $718 (2010 - $1,500).

($ thousands, except share information)

5. INVESTMENTS AND INVESTMENTS UNDER EQUITY METHOD (continued)

Refer to Note 22 Interest Rate Sensitivity for a summarization of amounts of investments by maturity dates and weighted average effective rates and refer to Note 27 Related Party Transactions for a summarization of related party transactions of Investments accounted for under the equity method.

6. MEMBER LOANS, IMPAIRED LOANS AND FORECLOSED ASSETS

	2011				
	Member Loans Gross Amount	**Allowance for Credit Losses Specific**	**Allowance for Credit Losses General**	**Member Loans Net Amount**	**Gross Impaired Member Loans**
Residential mortgages	**$ 5,705,616**	**$ 884**	**$ 535**	**$ 5,704,197**	**$ 23,134**
Commercial mortgages and loans	**2,960,388**	**21,055**	**2,165**	**2,937,168**	**55,154**
Consumer loans	**1,018,100**	**4,378**	**3,507**	**1,010,215**	**11,767**
Agricultural mortgages and loans	**272,771**	**38**	**114**	**272,619**	**2,460**
Sub-total	**9,956,875**	**26,355**	**6,321**	**9,924,199**	**92,515**
Accrued interest	**32,818**	—	—	**32,818**	—
Total	**$ 9,989,693**	**$ 26,355**	**$ 6,321**	**$ 9,957,017**	**$ 92,515**

	2010				
	Member Loans Gross Amount	Allowance for Credit Losses Specific	Allowance for Credit Losses General	Member Loans Net Amount	Gross Impaired Member Loans
Residential mortgages	$ 5,333,289	$ 570	$ 754	$ 5,331,965	$ 39,271
Commercial mortgages and loans	2,792,662	7,083	4,616	2,780,963	41,485
Consumer loans	965,164	4,630	5,096	955,438	14,647
Agricultural mortgages and loans	263,651	23	413	263,215	4,509
Sub-total	9,354,766	12,306	10,879	9,331,581	99,912
Accrued interest	33,143	—	—	33,143	—
Total	$ 9,387,909	$ 12,306	$ 10,879	$ 9,364,724	$ 99,912

The total amount of loans delinquent over 30 days but not impaired is $145,777 (2010 - $123,651). Refer to Note 22 Interest Rate Sensitivity for interest rate risk.

($ thousands, except share information)

6. MEMBER LOANS, IMPAIRED LOANS AND FORECLOSED ASSETS (continued)

The total amount of the foreclosed assets is:

	2011	2010
Foreclosed assets - gross	$ 18,407	$ 12,242
Impairment provision	(2,271)	(2,249)
Foreclosed assets - net	$ 16,136	$ 9,993

The impairment provision for the foreclosed assets is recognized in the Provision for credit losses in the Consolidated Statement of Income and Comprehensive Income.

7. ALLOWANCE FOR CREDIT LOSSES

	2011	2010
Balance, beginning of year	$ 23,185	$ 22,293
Loans written off	(7,986)	(11,165)
Recoveries of amounts written off in prior years	1,061	652
Provision for credit losses	16,416	11,405
Balance, end of year	$ 32,676	$ 23,185

Refer to Note 25 Financial Risk Management for credit risk information.

8. SECURITIZATION AND PURCHASE OF RESIDENTIAL MORTGAGES

Securitization of Residential Mortgages

The following table summarizes cash flows related to securitized mortgages:

	2011	2010
Cash flows remitted on collections	$ 61,628	$ 69,976
Cash flows received on retained rights to excess spread	1,896	3,135

Sensitivity to Key Assumptions

The value of the retained rights to future excess spread is primarily impacted by changes in the actual prepayment rate on the residential mortgages compared to the estimate originally used. An increase in the actual prepayment rate would cause a reduction in the calculated value of this retained interest while a lower prepayment rate would increase the calculated value. The Credit Union estimates the future prepayment rate based on historic experience, adjusted for the expected impact of current factors such as prevailing interest rates.

($ thousands, except share information)

8. SECURITIZATION AND PURCHASE OF RESIDENTIAL MORTGAGES (continued)

	Prepayment Rate	Change in Value
Prepayment rate 10% higher	43.56%	$ (136)
Prepayment rate 20% higher	47.52%	(262)

The discount rate realized ranged from 2.050% to 4.530%. A 10% and 20% change in the discount rate would have the following impact to the value of the Retained rights to future excess spread.

	Discount Rate	Change in Value
Discount rate 10% higher	2.255% - 4.983%	(409)
Discount rate 20% higher	2.460% - 5.436%	(814)

These sensitivities are hypothetical and should be used with caution. Changes in fair value based on a variation of assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of retained interests is calculated without changing any other assumption; generally, changes in one factor may result in changes in another, which may magnify or counteract the sensitivities.

As of October 31, 2011, the total retained rights to future excess spread on all previous securitizations were $2,156 (2010 - $4,601) and are recorded in Other assets on the Consolidated Balance Sheet. The fair value is measured by calculating the present value of forecasted cash flows using the key economic assumptions noted above. During 2011, the Credit Union has increased the estimated prepayment rate from 28.0% to 39.6% which resulted in a decrease in retained rights to future excess spread of $468 which had been recognized in the Consolidated Statement of Income and Comprehensive Income as a reduction to Other income.

As of October 31, 2011, the mortgage securitization liabilities, premium and retained servicing liability were respectively $2,756 (2010 - $4,402), $276 (2010 - $311) and $91 (2010 - $277) and are recorded in Accounts payable and other liabilities on the Consolidated Balance Sheet.

($ thousands, except share information)

9. PROPERTY AND EQUIPMENT

2011	Cost	Accumulated Depreciation	Net
Land	**$ 31,200**	**$ —**	**$ 31,200**
Buildings	**164,583**	**37,549**	**127,034**
Furniture, office equipment and vehicles	**33,986**	**17,163**	**16,823**
Leasehold improvements	**30,134**	**14,749**	**15,385**
Computer equipment	**17,979**	**10,650**	**7,329**
Equipment under capital lease	**1,269**	**909**	**360**
Airplane	**975**	**196**	**779**
Real estate investment properties	**596**	**126**	**470**
Total	**$ 280,722**	**$ 81,342**	**$ 199,380**

2010	Cost	Accumulated Depreciation	Net
Land	$ 32,004	$ —	$ 32,004
Buildings	143,858	28,247	115,611
Furniture, office equipment and vehicles	49,064	31,207	17,857
Leasehold improvements	40,208	16,854	23,354
Computer equipment	25,291	17,988	7,303
Equipment under capital lease	1,269	656	613
Airplane	975	67	908
Real estate investment properties	798	126	672
Total	$ 293,467	$ 95,145	$ 198,322

Depreciation expense recorded in the Consolidated Statement of Income and Comprehensive Income for the year ended October 31, 2011 for property and equipment was $15,108 (2010 - $14,694).

The Credit Union has various properties of which portions have been leased to tenants. The cost of these buildings is $26,495 (2010 - $25,962) with accumulated depreciation of $11,641 (2010 - $12,861).

Rental income recognized in the Consolidated Statement of Income and Comprehensive Income for the year ended October 31, 2011 from operating leases was $1,348 (2010 - $813) and is recorded under Other income.

There was an impairment loss of $1,036 (2010 - $725) recognized in the Operating expenses general during the year ended October 31, 2011.

($ thousands, except share information)

9. PROPERTY AND EQUIPMENT (continued)

At October 31, 2011, the Credit Union had $1,838 (2010 - $3,408) of buildings and leases under construction not yet placed into service and, therefore, depreciation has not been recorded on these assets.

At October 31, 2011, the Credit Union has a total of $3,155 (2010 - $9,352) in three parcels of land available for sale, which they are actively pursuing to sale. During 2011, the Credit Union reclassified a property available for sale of $3,933 to property and equipment and depreciation of $279 was recorded.

10. INTANGIBLE ASSETS

2011	**Cost**	**Accumulated Amortization**	**Net**
Computer software	**$ 2,260**	**$ 1,972**	**$ 288**
Computer software internally developed	**21,337**	**18,831**	**2,506**
Computer software under development (1)	**10,812**	**—**	**10,812**
Total	**$ 34,409**	**$ 20,803**	**$ 13,606**

(1) Net of impairment of $10,281.

2010	Cost	Accumulated Amortization	Net
Computer software	$ 12,830	$ 10,976	$ 1,854
Computer software internally developed	13,532	12,677	855
Computer software under development	10,403	—	10,403
Total	$ 36,765	$ 23,653	$ 13,112

Amortization expense recorded in the Consolidated Statement of Income and Comprehensive Income for the year ended October 31, 2011 for intangible assets was $2,047 (2010 - $2,048).

The Credit Union is in the process of developing a single banking system platform. Management has come to the conclusion that the development effort required and risks associated with the implementation of the new product cannot be resolved on a cost effective and timely basis. In order to expedite the convergence of all operations to a single banking platform, management will likely recommend an alternative software solution. As a result, the Credit Union has determined that it is appropriate to record an impairment loss for the costs directly associated with the original software resulting in a write down of $10,281 ($8,122 after income taxes). The impairment has been recorded in Operating expenses general in the Consolidated Statement of Income and Comprehensive Income.

($ thousands, except share information)

11. OTHER ASSETS

	2011	2010
Corporate tax receivable	$ **8,647**	$ 13,774
Prepaid items	**7,978**	7,369
Derivative instrument assets (Note 24)	**6,979**	9,165
Accounts receivable	**5,008**	4,782
Retained rights to future excess spread (Note 8)	**2,156**	4,601
Dividend from Alberta Central (Notes 5 & 27)	**1,305**	1,350
Future income tax asset	**179**	249
Total	$ **32,252**	$ 41,290

12. MEMBER DEPOSITS

	2011	2010
Demand accounts	$ **4,974,705**	$ 4,431,594
Term deposits	**3,506,432**	3,763,576
Registered plans	**1,654,535**	1,556,194
Other deposits	**7,666**	7,959
Sub-total	**10,143,338**	9,759,323
Accrued interest	**65,476**	72,585
Total	$ **10,208,814**	$ 9,831,908

Refer to Note 22 Interest Rate Sensitivity for a summarization of member deposit amounts by maturity dates and weighted average effective interest rates.

13. ACCOUNTS PAYABLE AND OTHER LIABILITIES

	2011	2010
Cheques and other items in transit	$ **59,456**	$ 35,260
Accounts payable and accrued liabilities	**43,905**	46,670
Dividend and patronage allocation to members (Note 15)	**25,739**	24,332
Pension liability (Note 21)	**5,727**	5,627
Deferred income	**3,640**	3,513
Mortgage securitization liabilities (Note 8)	**2,756**	4,402
Corporate tax payable	**450**	—
Obligations under capital lease	**385**	644
Premium and retained servicing liability (Note 8)	**367**	588
Derivative instrument liabilities (Note 24)	**15**	73
Future income tax liability	**—**	1,536
Total	$ **142,440**	$ 122,645

($ thousands, except share information)

13. ACCOUNTS PAYABLE AND OTHER LIABILITIES (continued)

Included in Accounts Payable and other liabilities are obligations under capital lease as follow:

	2011	2010
Total obligations under capital lease, secured by equipment with a net book value of $359, interest at 3.89% blended monthly repayment of $23 maturing March 2013	**$ 385**	$ 644

Commitments of future minimum lease payments under the capital lease are $280 for year 2012 and $164 for year 2013. Commitments of payment for maintenance are $285 for year 2012 and $71 for year 2013.

14. TERM LOANS PAYABLE

Alberta Central

The Credit Union has a credit facility agreement with Alberta Central in the aggregate amount of $800,000 comprising a revolving operating demand loan of $400,000 and a revolving term loan of $400,000. Interest on the line of credit is payable monthly at Alberta Central's prime rate for Canadian dollar advances and Alberta Central's US base rate on US dollar advances, in both cases plus or minus the applicable discount or margin of Alberta Central in effect from time to time.

Revolving term loans are due on demand or repayable in terms of 1 to 24 months for each advance with interest calculated at Alberta Central's prime rate plus or minus the applicable discount or margin of Alberta Central in effect from time to time or, at the option of the Credit Union, for terms of more than 30 days a fixed rate equal to Alberta Central's money market deposit rate or the equivalent paid fixed swap rate for the term plus the applicable discount or margin. A general assignment of book debts and hypothecation of investments with Alberta Central are pledged as collateral.

	2011	2010
Line of credit	**4**	—
Total	**$ 4**	$ —

At October 31, 2011, the Credit Union had $nil (2010 - $nil) in accrued interest on outstanding term loans payable and line of credit.

Caisse Centrale Desjardins

On December 23, 2010, the Credit Union entered into a credit facility with Caisse Centrale Desjardins ("CCD"). The facility is a 364 day revolving credit facility available in Canadian Dollars renewable annually, with a maximum credit available of $100,000. Subsequent to year end the existing credit facility was renewed for one year.

14. TERM LOANS PAYABLE (continued)

The loans may be structured as either due on demand or repayable for periods of one to three months for each advance. Interest is calculated at CCD prime rate or CCD cost of funds depending on facility and duration chosen as determined from time to time.

The Credit Union has granted to CCD a pledge of debenture of $200,000 which will create a floating charge over eligible residential mortgages.

At October 31, 2011, the Credit Union has $nil in outstanding loans payable and line of credit with CCD

Concentra Financial Services
The Credit Union has a letter of credit with Concentra Financial Services for $1,000 in favour of MBNA Canada Bank as part of a contracted financial services agreement. Fees consist of 1% annually.

15. SHARE CAPITAL

Common Shares
Common shares have the following characteristics:

a) Issuable in unlimited number;
b) A par value of $1, but issuable as fractional shares;
c) Transferable in restricted circumstances;
d) Non-assessable;
e) Redeemable at par value, subject to the Credit Union's redemption policy which includes approval of the Board of Directors and restrictions contained in the Credit Union Act and Regulations, including limitation to 10% of outstanding balances;
f) Adult members must hold a minimum of 1 share to retain membership in the Credit Union; and
g) Carries the right to vote at a general meeting.

Series A to G Investment Shares
Series A to G Investment shares have the following characteristics:

a) No par value;
b) No voting rights;
c) Non-assessable;
d) Transferable under limited circumstances;
e) Callable at the discretion of the Credit Union upon 5 years written notice;
f) Dividends are not cumulative and subject to the Credit Union's dividend policy and approval of the Board of Directors; and
g) Redeemable at $1 subject to the Credit Union's redemption policy, which includes redemption once per year, no more than 10% of outstanding balance and approval by the Board of Directors.

($ thousands, except share information)

15. SHARE CAPITAL (continued)

	Issued and Outstanding as at October 31 2010	Issued and Redeemed in 2011	Provision for Dividends Distributable 2011	Issued and Outstanding as at October 31 2011
Common Shares Total	$ 334,745	$ 9,422	$ 13,912	$ 358,079
Investment Shares				
Series A	45,632	(1,338)	2,325	46,619
Series B	7,703	(298)	—	7,405
Series C	18,795	(471)	958	19,282
Series D	27,331	(825)	1,385	27,891
Series E	4,845	(148)	—	4,697
Series F	552	(29)	27	550
Series G	364	(10)	19	373
Investment Shares Total	105,222	(3,119)	4,714	106,817
Share Capital Total	$ 439,967	$ 6,303	$ 18,626	$ 464,896

	Issued and Outstanding as at October 31 2009	Issued and Redeemed in 2010	Provision for Dividends Distributable 2010	Issued and Outstanding as at October 31 2010
Common Shares Total	$ 303,950	$ 17,156	$ 13,639	$ 334,745
Investment Shares				
Series A	45,092	(1,935)	2,475	45,632
Series B	8,071	(368)	—	7,703
Series C	18,212	(392)	975	18,795
Series D	26,394	(481)	1,418	27,331
Series E	5,021	(176)	—	4,845
Series F	—	523	29	552
Series G	—	345	19	364
Investment Shares Total	102,790	(2,484)	4,916	105,222
Share Capital Total	$ 406,740	$ 14,672	$ 18,555	$ 439,967

Common shares and investment shares represent at-risk capital not guaranteed by the Corporation.

The Board of Directors declared a $25,121 (2010 - $23,642) patronage allocation to members, a common share dividend of 4.25% or $13,912 (2010 – 4.5%, $13,639) and an investment share dividend of 5.25% for a total of $4,714 (2010 - $4,916) issued in additional investment shares. Patronage allocation to members is calculated based on the volume of business the member has with the Credit Union and is recorded in accounts payable and accrued liabilities (Note 13) at October 31, 2011.

15. SHARE CAPITAL (continued)

Common share dividends are paid to members by the issuance of additional common shares and are allocated to members' accounts as determined by the Board of Directors. Series A, C, D, F and G investment share dividends are paid in additional Series A, C, D, F and G investment shares. Series B and E investment share dividends for $618 (2010 - $690) were paid in cash and are recorded in Accounts payable and other liabilities in the Consolidated Balance Sheet. Total patronage and dividends paid in cash or shares were $44,365 (2010 - $42,887) and were paid in December 2011.

16. CAPITAL MANAGEMENT

The Credit Union provides financial services to its members and is subject to capital requirements set out in the Act. During 2011, there have been no changes to the capital requirements and the Credit Union complied with these capital requirements.

Definition and calculation of capital
When determining sufficiency of capital, the Credit Union included in its calculation amounts permitted under the Act:

- Retained earnings;
- Common shares;
- Investment shares;
- General allowance for credit losses; and
- The Credit Union's portion of qualifying Retained earnings of Alberta Central as calculated and provided by Alberta Central.

The total value of the items above is then reduced by any amounts of future income taxes recoverable when performing the final calculation of capital. Accumulated other comprehensive income is not included in the calculation of capital according to the definitions provided by the Corporation.

The Credit Union's objectives when managing capital are:

- To ensure the long term viability of the Credit Union and the security of member deposits by holding an efficient level of capital deemed sufficient to protect against unanticipated losses.
- To comply at all times with the capital requirements set out in the Act.

The Credit Union measures the adequacy of capital using two methods:

- Total capital as a percent of total assets;
- Total capital as a percent of risk weighted assets. Under this method, the Credit Union reviews each loan and other assets and assigns a risk weighting using definitions and formulas set out in the Act and by the Corporation. As more risk is associated with an asset, a higher weighting is assigned. The balance of each asset is multiplied by the risk weighting with the result then added together. The total amount of capital is then divided into this figure. This method allows the Credit Union to measure capital relative to the possibility of loss with more capital required to support assets that are seen as being higher risk.

($ thousands, except share information)

16. CAPITAL MANAGEMENT (continued)

The Credit Union management ensures compliance with capital adequacy through the following:

- Setting policies for capital management, monitoring and reporting;
- Setting policies for related areas such as asset liability management;
- Reporting to the Board of Directors or its committees regarding financial results and capital adequacy;
- Reporting to the Corporation on its capital adequacy; and
- Setting budgets and reporting variances to those budgets.

In addition, under the terms of the Act, the Credit Union may not pay dividends on Common or Investment shares if there are reasonable grounds for believing that the Credit Union is, or would by that payment become, insolvent.

Capital Requirements

The Credit Union is required under the Act to hold capital equal to or exceeding the greater of:

- 4% (2010 – 4%) of total assets; and
- 8% (2010 – 8%) of risk weighted assets.

The Credit Union has a stated policy that it will maintain at all times capital equal to no less than 9.5% (2010 – 9.5%) of risk weighted assets. A 9.5% corporate minimum allows the Credit Union to practice more conservative standards of capital management than required by the Act or the Corporation and provides additional security for the Credit Union.

As at October 31, 2011 for regulatory purposes the Credit Union's total capital as a percent of assets was 7.98% (2010 – 7.81%) and the total capital as percent of risk weighted assets was 14.69% (2010 – 14.35%), therefore, the Credit Union has exceeded its minimum capital requirement.

Elements of risk weighted capital at the year-end are:

	2011	2010
Retained earnings	**$ 417,343**	$ 392,228
Common shares (Note 15)	**358,079**	334,745
Investment shares (Note 15)	**106,817**	105,222
Qualifying Alberta Central retained earnings	**7,052**	7,022
General allowance for credit losses (Note 6)	**6,321**	10,879
Future income tax liability (Note 13)	—	1,536
Future income tax asset (Note 11)	**(179)**	(249)
Total	**$ 895,433**	$ 851,383

Retained earnings increased as result of net income in excess of dividend and patronage distribution. Common and investment share balances fluctuate with the addition of new members and members leaving the Credit Union. Common and investment share balances also increase from the dividends settled in shares and the sale of shares and decrease from redemptions.

($ thousands, except share information)

16. CAPITAL MANAGEMENT (continued)

Should the Credit Union not comply with its legislated capital adequacy requirements the following actions would result:

- The Chief Executive Officer and Chief Financial Officer would immediately notify the Board Chair, the Audit Finance Committee Chair, and the Corporation;
- The Board of Directors would be informed at their next scheduled meeting;
- Per the Act, redemption of Common shares would be suspended;
- An explanation and action plan would be presented and enacted; and
- The Credit Union may be subjected to intervention by the Corporation as provided for in the Act.

17. OTHER INCOME

	2011	2010
Commissions and fees	**$ 37,543**	$ 36,414
Service charges	**25,979**	26,940
Foreign exchange income	**4,662**	3,953
Other	**2,585**	3,359
Total	**$ 70,769**	$ 70,666

18. GENERAL OPERATING EXPENSES

	2011	2010
Administration fees and expenses	**$ 29,573**	$ 30,703
Computer processing cost	**14,201**	11,374
Impairment of tangible and intangible assets (Notes 9 & 10)	**11,317**	725
Marketing and advertising	**10,087**	11,656
Consulting fees	**3,909**	2,170
Total	**$ 69,087**	$ 56,628

19. INCOME TAXES

	2011	2010
Current income tax expense	**$ 12,412**	$ 10,624
Future income tax expense	**(1,466)**	1,511
Total	**$ 10,946**	$ 12,135

($ thousands, except share information)

19. INCOME TAXES (continued)

Full provision for income taxes is made in the determination of net income. Income tax recoveries arising from common share dividends and investment share dividends are reflected in retained earnings. Income tax expense differs from the amount that would be computed by applying the federal and provincial statutory income tax rates of 14.33% (2010 - 14.23%) to income before profit share dividends and income taxes. The reasons for the differences are as follows:

	2011	2010
Income taxes calculated at the statutory rate	**38.00%**	38.00%
Income taxes adjusted for the effect of:		
Reduction for credit unions	**-17.00%**	-17.00%
Tax recovery from patronage dividends	**-6.33%**	-5.77%
Non-taxable income in excess of non-deductible expenses	**-0.34%**	-1.00%
	14.33%	14.23%

20. GUARANTEES, COMMITMENTS AND CONTINGENT LIABILITIES

Guarantees

A guarantee is a contract that contingently requires the guarantor to make payments to a third party based on:

(i) changes in an underlying interest rate or other variable, including the occurrence or non-occurrence of an event that is related to an asset or liability held by the guaranteed party;
(ii) an indemnification provided to a third party with the characteristics listed above;
(iii) another entity's failure to perform under an obligation agreement, or
(iv) another entity's failure to fulfill their related debt obligations.

The various guarantees and indemnifications that the Credit Union provides to its members and other third parties but cannot be recorded in the Consolidated Financial Statements are presented below.

Standby Letters of Credit and Letters of Guarantee

Standby letters of credit and letters of guarantee are issued at the request of a Credit Union member in order to secure the member's payment or performance obligations to a third party. These guarantees represent an irrevocable obligation of the Credit Union to pay the third party beneficiary upon presentation of the guarantee and satisfaction of the documented requirements stipulated therein, without investigation as to the validity of the beneficiary's claim against the member. Generally the term of these guarantees does not exceed three years. The types and amounts of collateral security held by the Credit Union for these guarantees is generally the same as for loans. Standby letters of credit and letters of guarantee outstanding were:

($ thousands, except share information)

20. GUARANTEES, COMMITMENTS AND CONTINGENT LIABILITIES (continued)

	2011	2010
Standby letters of credits	$ **72,645**	$ 61,899

This represents the maximum potential amount of future payments that can be quantified and excludes other guarantees that cannot be quantified.

Indemnification of Directors and Officers

The Credit Union has Directors and Officers insurance coverage that limits its exposure to certain events or occurrences while the Director or Officer is or was serving at the Credit Union's request. This insurance coverage enables the Credit Union to recover a portion of any future amounts paid. The maximum potential amount of future payments is $15,000 per claim and an annual maximum of $30,000.

Other Indirect Commitments

In the normal course of business, various indirect commitments are outstanding which are not reflected on the Consolidated Balance Sheet. These may include:

(i) Commercial letters of credit which require the Credit Union to honour drafts presented by a third party when specific activities are completed.

(ii) Commitments to extend credit which represent undertakings to make credit available in the form of loans or other financings for specific amounts and maturities, subject to specific conditions.

The financial commitments are subject to the Credit Union's normal credit standards, financial controls and monitoring procedures. The table below provides a detailed breakdown of the Credit Union's other indirect commitments expressed in terms of the contractual amounts of the related commitment or contract which are not reflected on the Consolidated Balance Sheet.

	2011	2010
Commitments to extend credit:		
Original term to maturity of one year or less	$ **1,622,191**	$ 1,397,858
Original term to maturity of more than one year	**582,177**	606,673
Total	$ **2,204,368**	$ 2,004,531

Contractual Obligations

The Credit Union has various obligations under long-term non-cancellable contracts, which include service contracts, operating leases for buildings and equipment and other leases. The future minimum payments for such obligations for each of the next five fiscal years and thereafter are as follows:

($ thousands, except share information)

20. GUARANTEES, COMMITMENTS AND CONTINGENT LIABILITIES (continued)

	Operating leases for buildings	Other contractual obligations	Total
2012	$ 6,486	$ 6,685	$ 13,171
2013	5,786	2,511	8,297
2014	4,922	834	5,756
2015	3,921	833	4,754
2016	3,657	—	3,657
2017 and thereafter	13,588	—	13,588
Total	$ 38,360	$ 10,863	$ 49,223

The Credit Union also has various building construction projects underway for a total estimated cost of $3,474 (2010 - $3,207), and to date has incurred costs of $1,335 (2010 - $1,770). The remaining $2,139 (2010 - $1,437) is the anticipated cost to complete these construction projects.

During 2010, the Credit Union selected a single banking system platform which will form the basis of operations in the future. The Credit Union currently operates on three different banking system platforms. The project to move to the new banking system will span many years. The Credit Union has already entered into contracts to effect this transition. Commitments for the banking system are included under other contractual obligations above and total $9,685.

Contingent Liabilities
In the normal course of its business activities, the Credit Union is subject to claims and legal actions that may be made by former employees, members, suppliers and others. An accrual is made in the Consolidated Financial Statements if it can be reasonably estimated and it is likely that a future event will confirm that the liability has been incurred. Accruals are not made if the occurrence of the confirming future event is not determinable.

21. EMPLOYEE BENEFIT PLANS

The Credit Union provides pension benefits to employees through defined contribution and defined benefit plans. Other post-retirement benefits, including life insurance, health care and dental benefits are provided to eligible retired employees. All amounts expensed in the year are included in Operating expenses personnel in the Consolidated Statement of Income and Comprehensive Income.

Information regarding the Credit Union’s defined benefit plans is as follows:

($ thousands, except share information)

21. EMPLOYEE BENEFIT PLANS (continued)

	Pension Plans	Other Benefit Plans	Total 2011	Total 2010
Net benefit plan cost				
Current service cost employer portion	$ 141	$ 46	$ 187	$ 170
Interest cost	179	72	251	269
Amortization of transitional obligation	—	—	—	105
Amortization of gain on plan benefit change	—	(54)	(54)	(54)
Amortization of net actuarial loss	69	140	209	157
Total net benefit plan cost	389	204	593	647
Defined contribution registered retirement savings plan— Credit Union contributions	7,220	—	7,220	6,705
Total	$ 7,609	$ 204	$ 7,813	$ 7,352

	Pension Plans	Other Benefit Plans	Total 2011	Total 2010
Accrued benefit obligation				
Balance, at beginning of year	$ 4,479	$ 2,787	$ 7,266	$ 6,963
Current service cost	141	46	187	170
Interest cost	179	72	251	269
Expected benefits paid	(398)	(95)	(493)	(509)
Actuarial loss (gain)	(141)	50	(91)	373
Accrued benefit obligation, at end of year	$ 4,260	$ 2,860	$ 7,120	$ 7,266

($ thousands, except share information)

21. EMPLOYEE BENEFIT PLANS (continued)

	Pension Plans	Other Benefit Plans	Total 2011	Total 2010
Accrued benefit liability				
Funded status-plan deficit	**$ (4,260)**	**$ (2,860)**	**$ (7,120)**	$ (7,266)
Unamortized net actuarial loss	**229**	**1,167**	**1,396**	1,696
Unamortized gain on plan benefit change	**—**	**(3)**	**(3)**	(57)
Accrued benefit liability (Note 13)	**(4,031)**	**(1,696)**	**(5,727)**	(5,627)
Valuation allowance	**—**	**—**	**—**	—
Accrued benefit liability, net of valuation allowance	**$ (4,031)**	**$ (1,696)**	**$ (5,727)**	$ (5,627)

Effect of Change in Assumed Health Care Cost Trend Rates

The annual health insurance inflation rate is assumed to be 9%. The following shows the effect on the Credit Union's post retirement benefit plan of a change in the assumed health care cost trend rates for the year ending October 31, 2011:

	2011	2010
Significant Assumptions		
Weighted average discount rate	**3.48%**	3.67%
Rate of compensation increase	**4.00%**	4.00%

Actuarial Valuations

The most recent actuarial valuation on the defined benefit pension plan for funding purposes was completed as at October 31, 2010.

22. INTEREST RATE SENSITIVITY

Interest rate risk refers to the potential impact of changes in interest rates on the Credit Union's earnings when maturities of its financial liabilities are not matched with the maturities of its financial assets. The table below summarizes amounts by maturity dates and weighted average effective interest rates.

($ thousands, except share information)

22. INTEREST RATE SENSITIVITY (continued)

	2011				
	Floating Rate	Within 1 Year	More Than 1 Year	Non Interest Sensitive	Total
Assets					
Cash	$ 91,541	$ —	$ —	$ 27,126	$ 118,667
Investments	1,869	764,885	1,250	126,314	894,318
Effective yield	2.20%	1.07%	5.82%		3.03%
Member loans	4,303,503	1,713,708	3,847,149	92,657	9,957,017
Effective yield	3.93%	5.00%	5.12%		4.68%
Other assets	—	—	—	264,529	264,529
	4,396,913	2,478,593	3,848,399	510,626	11,234,531
Liabilities and Equity					
Member deposits	4,059,340	3,020,467	2,265,523	863,484	10,208,814
Effective yield	1.10%	2.21%	2.03%		1.78%
Other liabilities	—	—	—	142,440	142,440
Term loans payable	4	—	—	—	4
Effective yield	2.05%				2.05%
Equity	—	—	—	883,273	883,273
	4,059,344	3,020,467	2,265,523	1,889,197	11,234,531
Off Balance Sheet					
Notional value of assets derivative financial instruments	24,164	100,000	50,000	—	174,164
Notional value of liabilities derivative financial instruments	—	(102,287)	(71,877)	—	(174,164)
Sub-total off balance sheet	24,164	(2,287)	(21,877)	—	—
Net 2011 Position	$ 361,733	$ (544,161)	$ 1,560,999	$ (1,378,571)	$ —

($ thousands, except share information)

22. INTEREST RATE SENSITIVITY (continued)

	2010				
	Floating Rate	Within 1 Year	More Than 1 Year	Non Interest Sensitive	Total
Assets					
Cash	$ 115,734	$ —	$ —	$ 28,497	$ 144,231
Investments	3,411	884,184	1,324	116,805	1,005,724
Effective yield	2.04%	0.96%	5.79%	—	0.86%
Member loans	4,228,286	1,374,924	3,651,644	109,870	9,364,724
Effective yield	4.02%	5.25%	5.27%	—	4.64%
Other assets	—	—	—	272,069	272,069
	4,347,431	2,259,108	3,652,968	527,241	10,786,748
Liabilities and Equity					
Member deposits	3,579,885	2,749,304	2,709,675	793,044	9,831,908
Effective yield	0.84%	1.94%	2.47%	—	1.53%
Other Liabilities	—	—	—	122,645	122,645
Term loans payable	—	—	—	—	—
Effective yield					
Equity				832,195	832,195
	3,579,885	2,749,304	2,709,675	1,747,884	10,786,748
Off Balance Sheet					
Notional value of assets derivative financial instruments	78,996	65,000	150,000	—	293,996
Notional value of liabilities derivative financial instruments	(30,000)	(55,000)	(208,996)	—	(293,996)
Sub-total off balance sheet	48,996	10,000	(58,996)	—	—
Net 2010 Position	$ 816,542	$ (480,196)	$ 884,297	$(1,220,643)	$ —

($ thousands, except share information)

23. FAIR VALUE OF FINANCIAL INSTRUMENTS

The amounts set out in the table below represent the fair values of the Credit Union's financial instruments using the valuations and assumptions described below. The amounts do not include the fair value of items that are not considered financial assets, such as Property and equipment and Investments accounted under the equity method.

The estimated fair value approximates amounts at which instruments could be exchanged in a current transaction between willing parties who are under no compulsion to act. However, many of the Credit Union's financial instruments lack an available trading market and are intended to be held to maturity. Therefore, fair values are based on estimates using present value and other valuation techniques, which are significantly affected by the assumptions used concerning the amount and timing of estimated future cash flows and discount rates which reflect varying degrees of risk. Because of the estimation process and the need to use judgement, the aggregate fair value amounts should not be interpreted as being necessarily realizable in an immediate settlement of the instruments.

The fair value of cash recorded on the Consolidated Balance Sheet was determined using market price (referred to as Level 1). The fair value of investment, derivative assets and liabilities recorded on the Consolidated Balance Sheet was determined using a valuation technique based on observable market data (referred to as Level 2).

	2011			2010		
	Book Value	**Fair Value**	**Fair value difference**	Book Value	Fair Value	Fair value difference
Assets						
Cash (a)	**$ 118,667**	**$ 118,667**	**$ —**	$ 144,231	$ 144,231	$ —
Investments	**770,030**	**770,030**	**—**	890,647	890,722	75
Member loans (b,c)	**9,957,017**	**10,094,704**	**137,687**	9,364,724	9,541,366	176,642
Other assets (a,d)	**15,448**	**15,448**	**—**	19,898	19,898	—
Liabilities						
Member deposits (b,c)	**$ 10,208,814**	**$ 10,252,960**	**$ (44,146)**	$ 9,831,908	$ 9,893,273	$ (61,365)
Other liabilities (a,d)	**132,623**	**132,623**	**—**	111,969	111,969	—
Term loans payable	**4**	**4**	**—**	—	—	—
Total			**$ 93,541**			$ 115,352

($ thousands, except share information)

23. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The following methods and assumptions were used to estimate the fair value of financial instruments:

(a) The fair values of cash, other financial assets and other liabilities are assumed to approximate book values, due to their short term in nature.

(b) The estimated fair value of floating rate member loans and member deposits are assumed to equal book value as the interest rates automatically re-price to market.

(c) The estimated fair value of fixed rate member loans and fixed rate member deposits is determined by discounting the expected future cash flows of these loans and deposits based on yield curves for similar terms and credit risks.

(d) The fair value of derivative financial instruments is calculated based on market conditions at a specific point in time and may not be reflective of future fair values.

24. DERIVATIVE FINANCIAL INSTRUMENTS

The notional amounts of derivative financial instrument contracts maturing at various times are:

	1 to 3 months	3 to 12 months	1 to 5 years	2011	2010
Interest rate swaps					
Receive floating, pay fixed	$ 2,287	—	$21,877	$24,164	$ 78,996
Receive fixed, pay floating	—	—	—	—	30,000
Interest rate cap options	—	100,000	50,000	150,000	185,000
Equity-linked options	—	11,381	59,368	70,749	55,531
Total	$ 2,287	$ 111,381	$ 131,245	$ 244,913	$ 349,527

The Credit Union enters into derivative transactions for risk management purposes.

Interest Rate Swaps and Interest Rate Cap Options
Interest rate swaps and interest rate cap options are used for asset liability management purposes against changes in interest rates. They involve the exchange of interest cash flows between two parties on a specified notional principal. The fair value of these instruments are $15 (2010 - $73, recorded in Other assets) and is recorded in Accounts payable and other liabilities.

Equity-Linked Options
Equity-linked options are used to fix costs on term deposit products which are linked to movements in equity market indexes. The embedded derivative in the term deposit product as well as the option derivatives are marked to market through Other income. The fair value of the equity-linked derivative contract is $6,979 (2010 - $8,963) and is recorded in Other assets. The fair value of the embedded derivatives is $6,551 (2010 - $8,637) and is recorded in Member deposits accrued interest.

25. FINANCIAL RISK MANAGEMENT

The Credit Union is exposed to the following risks as a result of holding financial instruments: credit risk, market risk and liquidity risk. The following is a description of those risks and how the Credit Union manages the exposure to them.

Credit risk

Credit risk is the risk that a financial loss will be incurred due to the failure of a counterparty to discharge its contractual commitment or obligation to the Credit Union. Credit risk may arise principally in lending activities that lead to loans and advances, and investments that bring debt securities, derivative counterparties and other investments into the Credit Union's asset portfolio.

Risk Measurement

The Credit Union employs a risk measurement process for its loan portfolio. Credit risk rating systems are designed to assess and quantify the risk inherent in credit activities in an accurate and consistent manner. Risk is measured by reviewing exposure to individual borrowers and by reviewing qualitative and quantitative factors that impact the loan portfolios. Qualitative and quantitative analysis of a borrower's financial information are important factors used in determining the financial state of the counterparty.

Loan exposures are managed and monitored through facility limits for individual borrowers and a credit review process. These reviews ensure that the borrower complies with internal policy and underwriting standards. The Credit Union relies on collateral security typically in the form of a fixed and floating charge over the assets and underwriting of its borrowers. Credit risk is also managed through regular analysis of the ability of members and potential members to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Credit risk for counterparties in other financial instruments, such as investments and derivatives, is assessed through published credit ratings.

Credit Quality Performance

Refer to Note 6 for additional information on the credit quality performance of the Members' loans.

Objectives, Policies and Processes

The Credit Union employs and is committed to a number of important principles to manage credit risk exposure as follows:

- Credit risk assessment includes policies related to credit risk analysis, risk rating and risk scoring;
- Credit risk mitigation includes credit structuring, collateral and guarantees;
- Credit risk approval limits includes credit risk limits and exceptions;
- Credit risk documentation focuses on policy, reporting and administration; and
- Credit review and deterioration includes monitoring and review.

Since October 31, 2010, there were no significant changes of the Credit Union's credit risk policies, processes and methodologies.

25. FINANCIAL RISK MANAGEMENT (continued)

Market risk

Market risk consists of interest rate risk and foreign exchange risk. Market risk arises from changes in interest rates that affect the Credit Union's net interest income. Exposure to this risk directly impacts the Credit Union's net income from its derivative, loan and deposit portfolios. The Credit Union's objective is to earn an acceptable return on these portfolios, without taking unreasonable risk, while meeting member-owner needs. Foreign exchange risk is the risk that the fair value of a financial instrument will fluctuate because of changes in foreign exchange rates. Foreign exchange risks exist mainly as a result of the existence of financial assets, derivatives and financial liabilities denominated in foreign currencies. The risk associated with changing foreign currency values is managed under the Credit Union's foreign exchange risk management policy. At October 31, 2011, the Credit Union's net exposure to foreign currencies was $2,344 (2010 - $217).

Risk Measurement

The Credit Union's risk position is measured based on rates charged to member-owners. The Treasury department manages day-to-day market risk within approved policies and reports on a regular basis to management's Asset Liability Committee (ALCO) to ensure policy compliance. Management provides quarterly reports on these matters to the Board's Audit Finance Committee. Tools to measure this risk include: gap analysis, which shows the sensitivity between interest sensitive assets and interest sensitive liabilities; and income sensitivity analysis.

Objectives, Policies and Processes

The Treasury Department is responsible for managing the Credit Union's interest rate risk, monitoring approved limits and compliance with policies. The Credit Union manages market risk by developing and implementing asset and liability management policies. These policies are approved by the Board and monitored by the ALCO. The Credit Union's goal is to achieve adequate profitability, liquidity and stability. The Credit Union makes use of financial modeling based on possible interest rate scenarios and matching analysis to measure and manage its market risk. At least annually, the Board's Audit Finance Committee reviews the Credit Union's investment and asset liability management policies.

Since October 31, 2010, there were no significant changes of the Credit Union's market risk policies and procedures.

The following table provides the potential before-tax impact of an immediate and sustained 1% increase or decrease in interest rates on net interest income. These measures are based on assumptions made by senior management and validated by experience. All interest rate risk measures are based upon exposures at a specific time and continuously change as a result of business activities and risk management initiatives.

25. FINANCIAL RISK MANAGEMENT (continued)

	2011	2010
Before tax impact of:		
1% increase in rates	**$ 3,887**	$ 8,693
1% decrease in rates	**(17,008)**	(24,024)

Liquidity risk
Liquidity risk is the risk of having insufficient financial resources to meet either, the Credit Union's cash and funding requirements, statutory liquidity requirements, or both.

Risk Measurement
The assessment of the Credit Union's liquidity position reflects management's estimates, assumptions and judgement pertaining to current and prospective market conditions and the related behaviour of its members and counterparties. The Credit Union measures and manages its liquidity position from three perspectives:

- Structural liquidity risk, which addresses the risk due to mismatches in effective maturities between assets and liabilities, more specifically the risk of over reliance on short-term liabilities to fund long-term illiquid assets;
- Tactical liquidity risk, which addresses the day-to-day funding requirements that are managed by imposing prudential limits on net fund outflows;
- Contingent liquidity risk, which assesses the impact of and the intended responses to sudden stressful events.

Objectives, Policies and Processes
The acceptable amount of risk is defined by policies approved by the Board and monitored by ALCO.

The credit union's liquidity policies and practices include:

- Measurement and forecast of cash flows;
- Maintenance of a pool of high quality liquid assets;
- A stable base of core deposits from retail and commercial customers;
- Limits on single deposits and sources of deposits;
- Monitoring of wholesale demand and term deposits; and
- Diversification of funding resources.

The Credit Union manages liquidity by monitoring, forecasting and managing cash flows and the concentration of loans and deposits within approved policies. The Treasury department manages day-to-day liquidity within these policies and reports regularly to ALCO to ensure policy compliance. Management provides monthly reports on these matters to the Board's Audit Finance Committee.

Key features of liquidity management include:

- Daily monitoring of expected cash inflows and outflows and tracking and forecasting the liquidity position, including the flows from off-balance sheet items, on at least a two-month rolling basis; and

($ thousands, except share information)

25. FINANCIAL RISK MANAGEMENT (continued)

- Consideration of the term structure of loans and deposits, with emphasis on deposit maturities, as well as expected loan funding and other commitments to ensure the Credit Union can maintain required levels of liquidity while meeting its obligations.

26. OFFICERS' REMUNERATION AND BENEFITS

	Salary	Bonus	Benefits	2011	2010
Chief Executive Officer (CEO)	**$ 422**	**$ 428**	**$ 220**	**$ 1,070**	$ 922
Chief Financial Officer (CFO)	**227**	**106**	**49**	**382**	332
Chief Operating Officer (COO) (1)	**236**	—	**26**	**262**	336
Acting Chief Operating Officer (COO) (1)	**23**	**17**	**5**	**45**	—
Chief Information Officer (CIO)	**244**	**106**	**51**	**401**	327
Chief Risk Officer (CRO)	**228**	**112**	**53**	**393**	308
Chief People Officer (CPO)	**213**	**81**	**47**	**341**	310
Chief Marketing Officer (CMO)	**213**	**73**	**49**	**335**	296

(1): The COO left in October 2011 and was replaced by the Acting COO.

Benefits include employer's share of all officers' benefits and allowances and contributions or payments made on their behalf including pension, health care, dental coverage, vision coverage, out of country medical benefits, group life insurance, accidental disability and dismemberment insurance, long and short term disability plans, professional memberships, concessionary loans, club memberships and automobiles provided.

27. RELATED PARTY INFORMATION

Directors, Management and Employees

The Credit Union makes loans, primarily residential mortgages, and offers deposits, primarily fixed term deposits, to its management and employees at various preferred rates and terms. Board of Director loans and deposits are at member rates. All loans are in good standing and are granted in accordance with the Credit Union's standard credit practices.

	2011	2010
Loans outstanding - directors, management and employees	**$ 290,748**	$ 270,572
Deposits - directors, management and employees	**162,938**	107,169
Shares - directors, management and employees	**2,451**	322
Remuneration paid to directors (a)	**730**	558
Expenses paid to directors	**137**	145

(a) Remuneration paid to directors range from $20 (2010- $15) to $83 (2010 - $56) with an average of $52 (2010 - $35).

($ thousands, except share information)

27. RELATED PARTY INFORMATION (continued)

Alberta Central

As of October 31, 2011, the summary of outstanding balances in the Consolidated Balance Sheet and transactions in the Consolidated Statement of Income and Comprehensive Income with Alberta Central is as follows:

	2011	2010
Cash	$ 94,862	$ 119,733
Alberta Central term deposits (Note 5)	764,885	879,635
Accrued interest on term deposits	1,011	792
Alberta Central shares (Note 5)	123,448	113,439
Accounts receivable dividend from Alberta Central (Notes 5 and 11) (1)	1,305	1,350
Alberta Central - line of credit (Note 14)	4	—
Interest income term deposits	8,262	3,886
Net income equity investment (Note 5)	5,908	4,388
Interest expense on term loans	311	1,912
Data processing, memberships fees and other	18,352	14,626

(1) Dividend from Alberta Central is paid in December.

Investment in Crelogix

As of October 31, 2011, the summary of outstanding balances in the Consolidated Balance Sheet and transactions in the Consolidated Statement of Income and Comprehensive Income with Crelogix is as follows:

	2011	2010
Investment in Crelogix (Note 5)	$ 840	$ 1,638
Loans purchased	38,002	31,626
Interest income - loans	2,104	1,527
Net income equity investment (Note 5)	213	235
Loss on the sale of shares (Note 5)	21	—

These above transactions are in the course of normal operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

($ thousands, except share information)

28. SEGMENTED INFORMATION

The Credit Union manages its business as one integrated operating segment as it operates principally in personal and commercial banking throughout Alberta.

29. BUSINESS COMBINATIONS

During 2011, the Board of Directors approved the acquisition of 100% of the common shares of four credit unions. The credit unions acquired were: Royglenor Savings and Credit Union Ltd., Strathfiner Credit Union Ltd., Industrial Savings and Credit Union Ltd and Edmonton Postal Credit Union Ltd. These credit unions were in the business of personal and commercial banking serving approximately 2,100 members.

The Credit Union paid and received cash proceeds of $8,750 and $12,000 respectively for the acquisition of certain assets and liabilities of the four credit unions. The fair value, which has been determined to approximate book value, of the identifiable assets and liabilities as at the date of the acquisition is as follows:

	2011
Cash proceeds paid	$ (8,750)
Cash proceeds received	12,000
Net cash proceeds received	$ 3,250

	Fair Value Recognized on Acquisition
Identifiable assets acquired and liabilities assumed	
Investments	$ 500
Member loans	7,900
Other assets	500
Member deposits	(12,000)
Common shares	(150)
Total net identifiable assets and liabilities	$ (3,250)
Goodwill	$ —

servus
credit union

CANADA'S
BEST
MANAGED
COMPANIES
PLATINUM MEMBER

feel good about your money.

FSC FPO