2017

Annual Report 2017

Central 1®

2017 Financial Review

Table of Contents

Management's Discussion and Analysis

Consolidated Financial Statements

Management's Discussion and Analysis

Overview

This Management's Discussion and Analysis (MD&A) reviews and analyzes the financial condition and results of operations of Central 1 Credit Union (Central 1) for the years ended December 31, 2017, 2016 and 2015. The financial information included in this MD&A should be read in conjunction with Central 1's Consolidated Financial Statements for the year ended December 31, 2017, which were authorized for issue by the Board of Directors (the Board) on February 23, 2018, which is the effective date of this MD&A.

The results presented in this MD&A and in the Consolidated Financial Statements that follow are reported in Canadian dollars. Except as otherwise indicated, financial information for Central 1 included in this MD&A has been prepared in accordance with International Financial Reporting Standards (IFRS) as described in Note 2 of the Consolidated Financial Statements. Additional information on Central 1 may be found on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

This MD&A also includes financial information about the credit union networks in British Columbia and Ontario. The British Columbia credit union network is made up of all credit unions in British Columbia while the Ontario credit union network is made up of only those credit unions that have contracted to become members of Central 1. In the discussions presented in this report, the two provincial networks are individually referred to as the "British Columbia (B.C.) credit union network" or "B.C. network" and the "Ontario credit union network" or "Ontario network". Where the term "network" appears without regional designation, it refers to Central 1's total membership, encompassing credit unions in both provinces.

Financial information for the B.C. and Ontario networks has been provided by their provincial regulators, the Financial Institutions Commission of British Columbia (FICOM) and Deposit Insurance Corporation of Ontario (DICO), respectively. The differing provincial regulatory guidelines reduce the comparability of the information between the two provincial networks. Central 1 has no means of verifying the accuracy of information provided by credit unions to FICOM or DICO or the subsequent compilation of that information by FICOM or DICO. This information is provided purely to assist the reader with understanding Central 1's results and should be read in the proper context. Financial information provided by B.C. credit unions to FICOM and by Ontario credit unions to DICO has been prepared using reporting templates developed by FICOM and DICO, respectively. The format and accounting principles used to complete these templates are not fully consistent with IFRS. The net operating income of the B.C. and Ontario credit union networks reported herein is not equivalent to income from continuing operations as would be reported under IFRS.

Through 2017, Central 1 did a deep dive to explore how we need to evolve as an organization to continue to reimagine and empower the digitalization of Canadian credit unions' business processes. In order to support our members and clients in their success, we created a Transformation Office as a mechanism to accelerate delivery of key initiatives through sustained focus and cross-functional collaboration. Several key outcomes from the Transformation Office included:

- Obtaining FICOM and member (by a margin of more than 95.0 per cent voting in favour) approval for a change to our bylaws to permit tiered pricing for commercial bill payments. This change unlocks a major opportunity for Central 1 to offer more competitive market pricing to our clients and increase value to the whole network.
- Establishing a Product Advisory Council to provide client input into all of Central 1's digital banking and payments products and services, and as a consequence, sunsetting the Digital Banking Steering Committee.
- Defining a new evaluation, prioritization and governance process for the digital and payments product roadmap. This will help move to a more agile, transparent and consistent operating model for product development.

On November 1, 2017, Everlink Payment Services Inc. and Central 1 announced that, through a multi-year agreement between the two companies, B.C. and Ontario credit unions and other financial institutions will have access to sophisticated, enhanced, and real-time fraud monitoring measures to detect and combat debit card fraud. By compiling and integrating transaction and demographic data and consumer profiling, this service allows credit unions to lower fraud losses, improve brand reputation, and increase member trust and security by reducing the frequency of compromised cards. Management believes this will create the largest in-market fraud management services bureau delivery in Canada.

Effective August 16, 2017, FICOM amended the borrowing multiple requirements to no more than 17.0:1 for the Mandatory Liquidity Pool (MLP) segment and no more than 15.0:1 for the Wholesale Financial Services (WFS) segment. Following this amendment, Central 1 amended its capital limits which allowed Central 1 to return $50.0 million in capital to its Class A members. On September 29, 2017, Central 1 redeemed $30.0 million of Class A shares and paid $5.0 million dividends to Class A shareholders. On October 27, 2017, Central 1 reacquired $15.0 million of Class E shares.

As a result of members' approval of changes to Central 1's Rules, Class A shares will be reduced and Class F shares will be issued to Class A members in proportion to their share of mandatory deposits. The remaining aggregate level of Class A shares will be based on Central 1's estimate of regulatory capital required to support strategic and operational initiatives over its planning cycle, which is currently $50.0 million. The credit union members' holding of these Class A shares will continue to be based on their share of the network assets. On December 5, 2017, Central 1 received FICOM approval of these Rule changes. Central 1 plans to reacquire 750 thousand of Class E shares with an aggregate value of $75.0 million, which would reduce Central 1's regulatory capital. This series of transactions is anticipated to be completed by March 31, 2018.

Medium-term notes are an important component of Central 1's overall funding strategy and increased from $750.0 million at December 31, 2016 to $1,350.0 million at December 31, 2017. On January 31, 2018, Central 1 issued $350.0 million principal amount of Series 16 medium-term floating rate notes due February 5, 2021. The notes bear interest at 3-month Canadian Dollar Offering Rate (CDOR) plus 35 bps payable and reset quarterly on the 5th of February, May, August and November of each year, commencing May 5, 2018.

Central 1 had a strong capital position throughout 2017 and held sufficient capital at year-end to meet all regulatory requirements.

In December 2017, Desjardins Financial Holding Inc. (Desjardins), The CUMIS Group (CUMIS) and Canada's five provincial credit union centrals (Centrals) including Central 1 entered into a master merger agreement to merge the businesses of Credential Financial Inc., Northwest & Ethical Investments L.P., and Qtrade Canada Inc. This transaction, when complete, is expected to create one of Canada's largest independent wealth management firms with more than 500 thousand clients across the country and over $55.0 billion in combined client assets under administration.

The new entity, Aviso Wealth, will be jointly owned by Desjardins and a limited partnership comprised of the Centrals and CUMIS, with each holding a 50.0 per cent stake. Aviso Wealth will give credit unions access to a vertically integrated wealth management organization that is owned by the network and that will focus on meeting the expanding wealth management needs of credit union partners and their members across Canada. The merger of these businesses will offer a significant opportunity for credit unions to grow their wealth business and compete with the large banks. The transaction is expected to close in the first quarter of 2018.

Business Profile

Central 1's vision is to be a partner of choice for financial, digital banking and payment products and services – fueling the success of businesses across Canada for over 75 years.

Central 1's role is to support the success of credit unions and by extension, the financial well-being of all Canadians. Central 1 provides wholesale financial products, trust services, payment processing solutions and digital banking technologies and services to almost 300 credit unions and institutional clients from coast to coast. At Central 1, we work with members to understand their unique needs and leverage our network's scale to anticipate and deliver the holistic solutions to meet our members' needs. Central 1 has earned a reputation for innovation, with deep expertise in providing services and products that create a competitive edge for our members and enable them to reach their greatest potential.

Central 1's 109 member credit unions (as at December 31, 2017) represent a member-oriented, full-service retail financial network that collectively serves 3.4 million individual or organizational members and holds more than $126.8 billion in assets.

Central 1's products and services that are provided to its members are delivered through three core lines of businesses: MLP, WFS, and Digital & Payment Services. In addition, Central 1 offers a variety of additional services that are funded by membership dues.

Credit unions are required, by legislation in B.C., and by agreement in Ontario, to maintain a minimum balance of deposits with Central 1. These deposits, and the associated capital, form the basis of the MLP. Central 1 manages the MLP within regulatory constraints and leverages its economies of scale to reduce costs associated with managing the pool. Members receive interest income from their deposits as well as the net earnings of the MLP by way of a dividend. Central 1 does not profit from the management of the MLP. Assets in the MLP are subject to specific regulatory restrictions. Returns on the MLP are consistent with Central 1's risk profile.

WFS puts our clients at the forefront of the market and positions them as the financial institution of choice, offering funding solutions so clients can grow their balance sheets, increase margins and manage liquidity. WFS provides lending services, capital market access to foreign exchange and derivative capabilities, investment and deposit options, as well as securitization and mortgage funding options to financial institution clients. Aimed at diversifying product offerings and

Jump to table of contents

growing revenue for our clients, WFS also offers foreign exchange and registered financial services products, and commercial real estate lending syndication services.

With a focus on expanding our markets, solidifying our funding and providing holistic and proactive solutions to our members and clients, Central 1 reorganized its Trade Services function in September 2017 and moved a number of functions into WFS, including risk solutions and product compliance & design.

Central 1's Digital & Payment Services develops and operates innovative digital banking technologies and payment processing solutions for member credit unions, other financial institutions and corporate clients. These secure and reliable tools allow financial and corporate-sector clients to complete a variety of digital, paper and remittance transactions. They also provide cash management services, including automated funds transfers, bill payments and wire transfers.

Digital & Payment Services also offers *MemberDirect®* services, a hosted digital banking solution used by nearly 300 financial institutions across Canada. It is a multi-platform solution that allows clients to offer a variety of digital banking services to credit union members through their online banking platform. The products and services offered through *MemberDirect®* help credit unions attract new members, deepen their relationships with existing members and support them in delivering high quality member services.

Central 1's innovative solutions are scalable and adaptable to provide custom solutions to member credit unions and clients. By investing in leading edge technologies, Central 1 continues to improve the way it serves members and clients, enabling them to stay ahead of their evolving needs. Central 1's mobile app can be fully integrated with an organization's visual brand, so that each organization can provide its members with a recognizable and trustworthy mobile banking experience. Central 1's *Deposit Anywhere™* product, Canada's first mobile cheque deposit service, was developed through collaboration with credit union members based on Central 1's ground-breaking image capture recognition technology.

To accelerate Central 1's *MemberDirect®* roadmap and evolve its platform for credit unions, Central 1 launched a strategic initiative to develop a new digital User Experience (UX) omni-channel platform that will enable Central 1 to provide a leading-edge digital experience to its members for them to remain competitive in the future. It will deepen customer engagement through powerful, market-leading user experience management tools. The UX Platform will allow credit union self-service capabilities for a flexible, customizable digital experience to connect with their members across Canada.

Central 1 is also a Group Clearer that acts as the credit union network's connection to the Canadian payments system. It provides payment services to the credit union centrals of Alberta, Manitoba, Saskatchewan and Atlantic Canada.

While Central 1's primary focus is serving member credit unions to power their success, Central 1 has diversified its external client base with payments processing and technology services to other financial institutions. The benefits resulting from increased volumes flow through to member credit unions via lower fees on certain products. Central 1 also prices many of its services to Class A members on a cost-recovery basis which allows its members to benefit from Central 1's economies of scale.

The Dues Funded Activities put the needs of credit unions and clients first. This function works as a trusted partner for relevant solutions in areas of expertise including economics, marketing, market research and creative services, strategic and people solutions, and communications. These value-added, auxiliary services give member credit unions access to a wealth of expertise, while remaining affordable through economies of scale. Putting credit unions first using integrated programs and informed decisions, Central 1 delivers better outcomes for member credit unions while promoting the success and reputation of the credit union network to the public.

Factors That May Affect Future Results

In addition to the risks described in subsequent sections of this MD&A, there are numerous factors – systemic, political and economic – that may affect Central 1's performance, many of which are outside Central 1's immediate control and influence. The effects of these factors can be difficult to predict, and could cause Central 1's results to differ significantly from its plans, objectives and estimates. Readers are cautioned that the list of risk factors below is not exhaustive and should be reviewed in conjunction with the Cautionary Note Regarding Forward-Looking Statements section of this MD&A.

Industry and Non-Corporate Factors

Central 1, like other centrals across Canada, are actively participating in discussions with their members and one another about the design and expectations of key credit union support functions. These discussions have already led to cooperation in 2017 between Central 1, SaskCentral and Canadian Credit Union Association in bringing Marketing and Government Relations functions under the national banner to better support the network across Canada.

Through 2016, Central 1 remained dually regulated, provincially by FICOM, and by voluntarily subjecting itself to federal oversight by Office of the Superintendent of Financial Institutions (OSFI) via registration under Part XVI of the *Cooperative Credit Associations Act* (CCAA). In 2014, the Federal Government passed Bill C-43 in the

House of Commons repealing Part XVI of the CCAA effective January 15, 2017. As a result, Central 1 was no longer regulated by OSFI effective January 15, 2017. In addition, Part XVII of the CCAA and section 39 of the *Canada Deposit Insurance Act* is expected to be repealed such that the Canada Deposit Insurance Corporation would no longer provide loans from the Consolidated Revenue Fund of Canada to Central 1 and other centrals. The Bank of Canada (BOC) is also reviewing conditions for Emergency Lending Assistance to Central 1, other centrals and other provinces.

Legislative reviews that have been ongoing in both B.C. and Ontario continued throughout 2017. Central 1 continued to correspond with Ministry of Finance officials on the review of the *B.C. Financial Institutions Act and Credit Union Incorporation Act*, commenting on items such as residential mortgage lending, small business lending, governance, capital and liquidity throughout 2017. The Ministry of Finance has indicated that it will release a White Paper with initial policy positions sometime in early 2018.

The Ontario government has committed to a comprehensive re-write of the *Credit Unions and Caisses Populaires Act* (CUCPA). Central 1's Government Relations has assembled a Working Group of credit union representatives that has worked with the government to provide input for the re-write of the CUCPA. The first section of the CUCPA being reviewed is capital adequacy. The Working Group helped inform the network's position that will be submitted to the Ministry of Finance by the deadline of February 28, 2018.

The Ontario government has also moved forward with a number of positive changes for credit unions that came into force on January 1, 2018. These changes include increasing deposit insurance coverage for non-registered accounts from $100 thousand to $250 thousand, and increased subsidiary ownership and the operation of extra-provincial credit unions.

As a wholesale financial services provider to member credit unions, Central 1 is affected by prevailing economic and business conditions, including the impact of prices within financial markets. Factors such as interest rates, inflation, consumer and business spending not only impact residential real estate lending and the primary activities for B.C. and Ontario credit unions, but also influence demand for the majority of other credit union products and services.

Central 1's financial results are affected by the monetary policies of the BOC and, to a lesser extent, by those of the U.S. Federal Reserve (the Fed) system. Monetary policy decisions determine the level of interest rates which, in turn, may have a significant impact on Central 1's financial results.

The interest rate differential, or credit spread, between Government of Canada (GOC) securities and those issued by other participants in fixed-income markets also affects Central 1's financial results. Central 1 earns income from accepting mandatory credit union deposits at rates based on GOC securities and non-mandatory deposits based on senior bank deposit notes, and investing in securities issued by the GOC, other levels of government and corporations. To the extent that credit spreads and swap spreads change, Central 1's interest margin, as well as the fair value of its financial instruments, would be impacted.

The Competition Tribunal approved Interac's request to amend the Consent Agreement in 2013. This amendment permits Interac to restructure its operations into a single entity that can offer a single integrated portfolio of payment products under the direction of an independent board and with the ability to better fund innovation. The restructuring is a critical step in helping Interac to continue offering effective, convenient and secure payment products for Canadian merchants and consumers. The restructuring was completed by January 31, 2018.

Network-Specific Factors

Central 1's financial performance is heavily influenced by events in the network. There is strong competition for members and clients among Canada's financial services providers. The degree of such competition has an impact on the performance of Central 1 and the network. Credit unions enjoy strong member loyalty, retention is influenced by their ability to deliver products and services at competitive prices and service levels vis-à-vis other financial services providers. Non-financial companies can also offer members and clients a range of competing service and product options.

Through 2017, Central 1 continued to review its operations and the second tier to determine if there are any opportunities to provide greater value to both members and other clients, to benefit the financial well-being of all Canadians. The result is a renewed focus on the success of Canadian credit unions and their members and a reaffirmation of our commitment to the cooperative values and principles. We know that expanding our services to other financial institutions will further power the progress of credit unions.

Corporate-Specific Factors

In addition to the industry and network-specific factors outlined above, the *Bank Act* provides for the establishment of federal credit unions. A credit union that elects to become a federal credit union would cease to be regulated provincially.

Central 1 has earned a reputation for innovation, with deep expertise in providing services and products that create a competitive edge for our members and enable them to reach their greatest potential. Demand for Central 1's products and services are therefore correlated with the success of member credit unions and their customers. For example, demand for products and services provided by Central 1's WFS business line are correlated with demand for lending and deposits at the

Jump to table of contents

individual credit union level. Technology needs within the network are also driven by member and client needs, which in turn are impacted by regulatory change and potentially disruptive new entrants into the market.

Central 1 has been designated by FICOM as a domestic systemically important financial institution (D-SIFI) within the Canadian credit union network. D-SIFIs are financial institutions whose failure could cause significant disruption to the wider financial network and economic activity.

In connection with the designation of Central 1 as a D-SIFI, FICOM has provided Central 1 with additional requirements related to the management of its activities. These requirements reflect the important role Central 1 plays in the stability of the credit union network. FICOM's intent with its requirements is to ensure that Central 1 is sufficiently capitalized, including under stressed conditions, and to ensure that Central 1's risk profile and corresponding need for capital support remain within the risk appetite and tolerance level of its members.

FICOM's requirements for investments in the MLP are contained in the Cash and Liquid Assets section and its borrowing multiple requirements are described in the Capital Management and Capital Resources section.

Central 1's own credit risk on deposits also affects its financial results. To the extent that Central 1's own credit risk changes, the fair value of financial liabilities designated as trading, such as deposits, would be impacted.

Other Factors

Other factors which could affect actual results include changes in accounting standards, including their effect on Central 1's accounting policies, estimates and judgements. Changes in income tax regulations will also affect Central 1's actual results. In addition, Central 1 may be adversely impacted by the failure of third parties to comply with their obligations, such as obligations related to the handling of personal information or failure to prevent fraud.

Central 1's future performance is also dependent on its ability to attract, develop and retain key management personnel.

Cautionary Note Regarding Forward-Looking Statements

From time to time, Central 1 makes written forward-looking statements, including in this MD&A, in other filings with Canadian regulators, and in other communications. In addition, representatives of Central 1 may make forward-looking statements orally to analysts, investors, the media and others. All such statements may be considered to be forward-looking statements under applicable Canadian securities legislation.

Within this document, forward-looking statements include, but are not limited to, statements relating to Central 1's financial performance objectives, vision and strategic goals, the economic, market and regulatory review and outlook for the Canadian economy and the provincial economies in which Central 1's member credit unions operate. The forward-looking information provided herein is presented for the purpose of assisting readers in understanding Central 1's financial position and results of operations as at and for the periods ended on the dates presented. Forward-looking statements are typically identified by words such as "believe", "expect", "anticipate", "estimate", "plan", "will", "may", "should", "could", or "would" and similar expressions.

Forward-looking statements, by their nature, require Central 1 to make assumptions and are subject to inherent risks and uncertainties, which give rise to the possibility that predictions, forecasts or conclusions will not prove to be accurate, that assumptions may not be correct and that financial objectives, vision and strategic goals will not be achieved. Central 1 cautions readers to not place undue reliance on these statements as a number of risk factors could cause actual results to differ materially from the expectations expressed in the forward-looking statements. These factors – many of which are beyond Central 1's control and the effects of which can be difficult to predict – include business and operations, compliance, credit and counterparty, insurance, liquidity, market, and operational risks.

Readers are cautioned that the foregoing list is not intended to be exhaustive and other factors may adversely impact Central 1's results. Central 1 does not undertake to update forward-looking statements except as required by law.

Jump to table of contents

Economic Developments and Outlook

The following summaries of the economic environment, the state of financial markets and performance by both provincial networks in 2017 offer context for interpreting Central 1's year-over-year results and insight into its future.

The Economic Environment

The world economy outperformed most analysts' expectations in 2017. In January 2017, the International Monetary Fund (IMF) projected global economic growth of 3.4 per cent in 2017. In January 2018, the IMF estimated the global economy grew by 3.7 per cent in 2017.

Canada's economy grew by an estimated 3.0 per cent in 2017, according to the BOC, up sharply from 1.4 per cent in 2016. Growth in 2017 was led by household consumer spending, private sector residential investment spending, international trade, private sector non-residential investment spending and government investment and spending. Growth was supported by still-accommodative monetary policy and financial conditions, stronger U.S. growth and commodity prices, and government spending. Total employment grew 1.9 per cent in 2017 and the unemployment rate fell to 6.3 per cent. Consumer price inflation was 1.6 per cent. The average BOC bank rate and chartered bank prime lending rate in 2017 increased 21 basis points (bps) year-over-year as the BOC raised its benchmark interest rate 50 bps. The average 10-year GOC benchmark bond yield in 2017 increased 53 bps year-over-year.

The BOC forecasts Canadian economic growth at 2.2 per cent in 2018, led by household consumer spending. Business fixed investment spending and government investment and spending will also contribute to growth, with business investment contributing more this year than last year. Residential investment spending will contribute only slightly to growth, while the contribution from international trade will be range-bound. Central 1 Economics forecasts employment growth of 1.4 per cent in 2018 with the unemployment rate declining to 6.1 per cent. Consumer price inflation is forecast at 2.0 per cent. The average three-month treasury bill yield is forecast to rise 21 bps year-over-year while the average long-term GOC bond yield rises 35 bps.

British Columbia

B.C.'s economy expanded at a robust pace of 3.7 per cent in 2017 according to Central 1 estimates. That was up 0.2 per cent from 2016 and well above average growth of 2.8 per cent observed since 2000. Growth was heavily concentrated in household consumer spending and, to a small extent, residential investment spending. Government spending and investment, business investment and net exports were range-bound. Labour income led robust growth in domestic income, with smaller gains in proprietary rental income, taxes less subsidies, and corporate profits.

The labour market in B.C. improved in 2017 with total employment rising 3.7 per cent, the highest growth rate since 1994. Both full- and part-time employment increased, as did private sector, public sector and self-employment. The unemployment rate averaged 5.1 per cent, down from 6.0 per cent in 2016. Aggregate labour income grew by an estimated 6.7 per cent, above average growth of 4.2 per cent since 2000.

The housing market in B.C. remained active in 2017 yet cooled somewhat in Vancouver and Victoria from the torrid pace of 2016 in response to various policy changes designed mainly to dampen speculation. Housing construction starts increased 4.3 per cent from 2016 while housing sales decreased 7.5 per cent. The average sale price increased 2.7 per cent.

Central 1 Economics forecasts growth in B.C.'s economy at 3.0 per cent in 2018, largely due to higher household consumer spending. Business investment in non-residential buildings and intellectual property will contribute more to economic growth while net exports will be a slight drag on growth. Employment is forecast to rise 2.0 per cent while the unemployment rate declines to 4.5 per cent. Domestic income growth is forecast at 5.7 per cent, led by labour income, proprietary rental income and taxes less subsidies.

Ontario

Ontario's economy expanded at a moderate pace of 2.8 per cent in 2017 according to Central 1 estimates, up from 2.6 per cent in 2016 and above average growth of 2.1 per cent observed since 2000. Growth was led by household consumer spending with lesser contributions from private residential investment spending and government spending and investment. Business investment was range-bound while net exports was a drag on growth. Labour income and corporate profits led above average growth in domestic income, with smaller gains in taxes less subsidies and proprietary income.

The labour market in Ontario improved in 2017 with total employment rising 1.8 per cent, up from 1.1 per cent in 2016 and above average growth of 1.3 per cent since 2000. Both full- and part-time employment increased, as did private sector, public sector and self-employment. The unemployment rate declined to 6.0 per cent from 6.5 per cent as labour force growth failed to keep pace with employment growth. Aggregate labour income grew by an estimated 3.9 per cent, equal to the average growth rate since 2000.

Jump to table of contents

Housing lifted Ontario's economy in 2017 despite lower existing home sales, with most regions following the provincial trends. Housing construction starts are estimated at 80,800 units, up 7.7 per cent from 2016. Annual housing sales declined 9.5 per cent to 220,150 units in response to various policy changes designed mainly to dampen speculation. The average sale price increased 9.7 per cent.

Central 1 Economics forecasts growth in Ontario's economy at 2.4 per cent in 2018, largely due to higher household consumer spending. Government spending and investment and business investment will contribute to economic growth while net exports will remain a drag on growth. Employment is forecasted to rise 1.3 per cent while the unemployment rate declines to 5.9 per cent. Domestic income growth is forecasted at 4.3 per cent, largely due to higher labour income. Proprietary income also contributes to growth while corporate profits are a slight drag on growth.

Financial Markets

The BOC raised rates twice during 2017 with another hike on January 17, 2018. Markets are forecasting two to three further BOC rate hikes this year. In 2017, the GOC curve experienced a steepening of shorter rates and a flattening of the curve beyond two years. Spreads between GOC two-year versus five-year terms peaked above 40 bps during the year and then declined to close the year below 20 bps. The five-year versus 10-year terms also continued to decline. Credit spreads continued to narrow on a year-over-year and monthly basis in 2017.

Network Performance

British Columbia

The following table provides a five-year summary of the British Columbia Credit Union Network.

Figure 1 - Five-Year Summary: British Columbia Credit Union Network

As at December 31[1] (Millions of dollars)	2017	2016	2015	2014	2013
Cash and Central 1 operating account	**$ 641.0**	$ 788.3	$ 854.3	$ 766.3	$ 601.4
Investments					
Liquid	**9,709.4**	9,718.0	8,543.9	6,653.2	6,323.7
Other	**268.3**	266.4	240.3	222.2	205.3
Loans[2]	**65,226.0**	59,907.7	55,570.1	52,785.4	50,835.0
Other	**1,198.0**	1,180.0	1,141.5	1,031.1	947.8
Total assets	**$ 77,042.7**	$ 71,860.4	$ 66,350.1	$ 61,458.2	$ 58,913.2
Borrowed funds	**$ 4,838.3**	$ 3,997.8	$ 3,390.8	2,101.4	$ 2,260.2
Members' deposits	**66,317.6**	62,478.6	57,758.5	54,412.7	51,938.0
Non-equity shares	**56.1**	55.8	55.5	57.3	61.8
Retained earnings and equity shares	**4,590.1**	4,260.9	4,038.1	3,903.0	3,699.8
Payables and other	**1,240.6**	1,067.3	1,107.2	983.8	953.4
Total liabilities and equity	**$ 77,042.7**	$ 71,860.4	$ 66,350.1	$ 61,458.2	$ 58,913.2

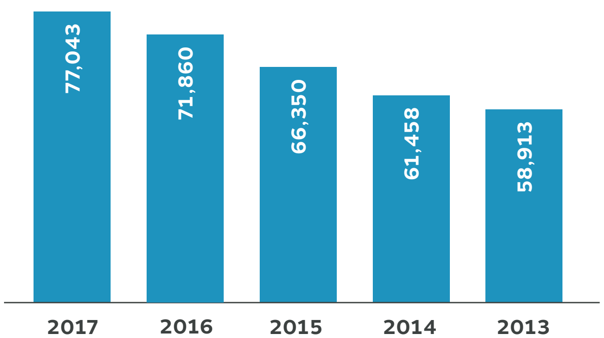
For the years ended December 31[1] (Millions of dollars)	2017	2016	2015	2014	2013
Financial margin	**$ 1,455.1**	$ 1,324.0	$ 1,247.0	$ 1,247.2	$ 1,216.6
Non-financial income	**321.8**	291.5	295.6	277.9	270.6
Net income from equity investments	**58.9**	24.5	19.2	21.8	16.6
	1,835.8	1,640.0	1,561.8	1,546.9	1,503.8
Non-financial expense	**1,382.0**	1,302.3	1,235.7	1,203.0	1,162.0
Net loan loss expense	**36.0**	34.8	35.0	46.3	33.1
Income taxes	**73.4**	39.9	37.0	44.9	55.5
Net income[3]	**$ 344.4**	$ 263.0	$ 254.1	$ 252.7	$ 253.2
Return on equity	**7.8 %**	6.3 %	6.1 %	6.4 %	6.9 %

Jump to table of contents

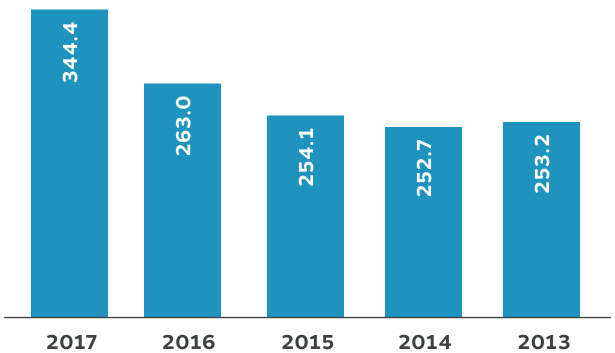
	2017	2016	2015	2014	2013
Statistical					
Number of credit unions	**42**	42	42	43	43
Number of branches[4]	**379**	374	374	365	371
Number of ATMs	**571**	561	567	565	565
Number of members *(thousands)*	**1,965**	1,909	1,920	1,904	1,878

Note: All figures in the table are unaudited. 2017 data is preliminary. 2016 data is revised.
[1] Statements for three credit unions with September 30th year-end are adjusted to twelve months ending December 31st.
[2] Figures are net of allowance for doubtful loans, but include accrued interest.
[3] Excludes equity dividends & patronage refunds, charitable donations, capital gains (losses) & extraordinary items.
[4] Excludes credit union insurance subsidiaries branches.

Total Assets – British Columbia Credit Union Network
(Millions of dollars)



Net Income – British Columbia Credit Union Network
(Millions of dollars)



The B.C. credit union network continued to grow in 2017. Network net income totaled $344.4 million, up from $263.0 million in 2016. Lending grew 8.9 per cent year-over-year, leading to higher financial margin. Return on average equity was 7.8 per cent, up from 6.3 per cent in 2016. Earnings growth was assisted by higher interest rates and wider interest rate spread between assets and liabilities.

Financial margin increased $131.1 million or 9.9 per cent as the balance sheet grew 7.2 per cent and the net interest margin widened by five bps driven by the BOC rate hikes during 2017. Non-financial income increased $30.3 million or 10.4 per cent, led by wealth management, trust and deposit services, and $34.4 million increase in income from equity investments. Non-financial expenses increased $79.7 million or 6.1 per cent, with majority of the increase driven by higher salaries and benefits, followed by higher data processing and information technology expenses. Net loan loss expense increased by $1.2 million or 3.4 per cent.

Assets of the B.C. network totaled $77.0 billion at the end of 2017, up $5.2 billion or 7.2 per cent from a year earlier. Asset growth was largely from increases in low ratio personal residential mortgages, while insured personal residential mortgages declined. Liability and equity growth were led by chequing deposits, term deposits and borrowings.

The 90-day delinquency rate at year-end stood at 0.16 per cent of the loan portfolio, down nine bps from a year earlier. Net loan loss expense for the year was 0.05 per cent of average assets, unchanged from a year earlier. Reserves held against loan losses totaled 0.28 per cent of the portfolio at year-end, down one bp from a year earlier.

Jump to table of contents

The network's liquidity ratio decreased in 2017 while the regulatory capital ratio was down slightly, with both ratios remaining well above the minimum requirements for individual credit unions. The liquidity ratio stood at 14.5 per cent at year-end, down from 15.7 per cent a year earlier. The risk-weighted capital adequacy ratio finished the year at 14.4 per cent, down from 14.7 per cent a year earlier.

B.C. credit union membership stood at approximately 2.0 million at the end of 2017, a year-over-year increase of 2.9 per cent. Province-wide staffing was little changed at 8,454 full-time equivalent employees at year end. B.C. had 42 local credit unions at year-end, unchanged from a year earlier. The number of branches in B.C. increased from 374 to 379, and the network's ATMs increased to 571 from 561.

Ontario

The following table provides a five-year summary of the Ontario Credit Union Network.

Figure 2 - Five-Year Summary: Ontario Credit Union Network

As at December 31 (Millions of dollars)	2017	2016	2015	2014	2013
Cash and Central 1 operating account					
Investments					
Liquid (including cash)	**$ 4,964.7**	$ 4,920.8	$ 4,329.4	$ 3,650.5	$ 3,509.2
Other	**694.1**	650.1	567.9	462.7	622.2
Loans[1]	**43,286.6**	38,596.3	34,327.9	31,388.9	28,316.2
Other	**797.8**	754.6	714.0	654.2	578.7
Total assets	**$ 49,743.2**	$ 44,921.8	$ 39,939.2	$ 36,156.3	$ 33,026.3
Borrowed funds	**$ 5,756.4**	$ 4,966.6	$ 3,943.2	$ 3,119.3	$ 2,374.1
Members' deposits	**39,984.4**	36,087.9	32,464.9	30,028.5	27,986.3
Retained earnings and equity shares	**1,913.8**	1,768.9	1,666.2	1,470.2	1,358.9
Payables and other	**2,088.6**	2,098.4	1,864.9	1,538.3	1,307.0
Total liabilities	**$ 49,743.2**	$ 44,921.8	$ 39,939.2	$ 36,156.3	$ 33,026.3

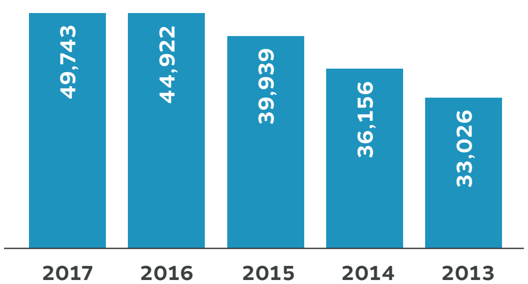
For the years ended December 31 (Millions of dollars)	2017	2016	2015	2014	2013
Financial margin	**$ 946.0**	$ 844.8	$ 798.3	$ 792.3	$ 746.5
Non-financial income	**239.1**	234.6	206.9	179.1	178.6
	1,185.1	1,079.4	1,005.2	971.4	925.1
Non-financial expense	**948.7**	885.0	846.3	794.3	730.1
Net loan loss expense	**17.3**	30.5	26.1	31.1	29.1
Income taxes	**34.6**	21.1	20.5	20.5	16.5
Net income[2]	**$ 184.5**	$ 142.8	$ 112.3	$ 125.5	$ 149.4
Return on equity	**5.8 %**	5.0 %	4.4 %	5.4 %	6.9 %

Jump to table of contents

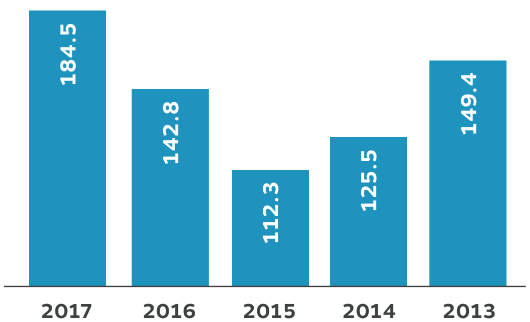
	2017	2016	2015	2014	2013
Statistical					
Number of credit unions	**67**	72	79	84	90
Number of branches	**536**	528	525	516	502
Number of ATMs	**579**	564	567	575	588
Number of members *(thousands)*	**1,422**	1,407	1,384	1,333	1,326

** Results for prior years are restated to conform to current year's presentation*
[1] Figures are net of allowance for doubtful loans
[2] After taxes, before dividends, patronage refunds, extraordinary items and other comprehensive income.
Note: All figures in the table are unaudited.

Total Assets – Ontario Credit Union Network
(Millions of dollars)



Net Income – Ontario Credit Union Network
(Millions of dollars)



Central 1's Ontario credit union network saw assets and profits grow in 2017. Network net income totaled $184.5 million, up from $142.8 million in 2016. Lending grew 12.2 per cent year-over-year. Return on average equity was 5.8 per cent, up from 5.0 per cent in 2016. Higher financial margin, led by balance sheet growth, outweighed higher non-financial expense, led by salaries and benefits reflective of increased staffing.

Asset growth for the Ontario network remained strong in 2017, with assets totaling $49.7 billion at year end, up 10.7 per cent year-over-year. Loan growth was driven by residential mortgages and commercial loans and mortgages. Network deposits totaled $40.0 billion at year-end, up 10.8 per cent from a year earlier. Deposit growth was largely in non-registered term and demand products. Network borrowings totaled $5.8 billion at year end, up 15.9 per cent year-over-year. Credit union capital totaled $3.4 billion at year-end, up 14.1 per cent year-over-year.

The network's credit risk measures improved in 2017. The overall 90-day delinquency rate declined from 0.36 per cent to 0.3 per cent at year-end, while total loan loss reserves ended 2017 at 0.21 per cent of the portfolio, down five bps year-over-year. The rate of loan loss expense was four bps in 2017, down four bps from a year earlier.

The network's liquidity ratio ended 2017 at 10.7 per cent, down from 11.8 per cent at the end of 2016. Class 2 credit unions, those with commercial lending authorizations, represent 99.0 per cent of the network's assets, finished the year with a risk-weighted capital ratio of 13.1 per cent, little changed from 13.0 per cent a year earlier.

Ontario network membership increased 1.1 per cent in 2017 form a year earlier. Staffing increased 4.7 per cent year-over-year. Amalgamations and purchases continued within the Ontario credit union network. There were 67 credit unions in Ontario affiliated with Central 1 at year-end, down from 72 credit unions a year earlier. The number of branches totaled 536 at the end of 2017, up from 528 a year earlier, while the network's ATMs increased to 579 at the end of 2017 from 564 a year earlier.

Jump to table of contents

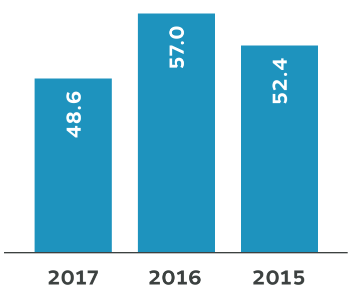
Overall Performance

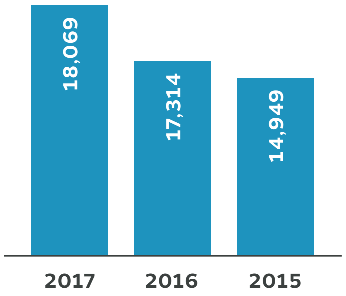
The following table summarizes Central 1's Financial Overview as at December 31, 2017 with comparatives.

Figure 3 – Financial Overview

December 31	2017	2016	2015
Operating results *(millions of dollars, unless otherwise indicated)*			
Net financial income	**$ 73.4**	$ 67.5	$ 50.1
Net financial and other income	**$ 223.5**	$ 207.9	$ 190.9
Operating income (loss)	**$ (14.6)**	$ (1.1)	$ 11.2
Profit for the year	**$ 48.6**	$ 57.0	$ 52.4
Productivity ratio	**73.6 %**	68.1 %	$ 67.9 %
Productivity ratio - non-financial	**109.7 %**	100.8 %	$ 92.1 %
Return on average assets	**0.3 %**	0.4 %	$ 0.4 %
Return on average equity	**4.4 %**	5.6 %	$ 5.5 %
Earnings per share *(cents)*			
Basic	**11.4**	14.9	15.2
Diluted	**11.4**	14.9	15.2
Dividends per share *(cents)*			
Class A	**4.3**	3.6	4.2
Class B & C	**1.7**	1.1	1.0
Weighted average shares outstanding	**$ 424.9**	$ 382.0	$ 345.0
Average assets	**$ 17,851.2**	$ 15,739.6	$ 14,042.1

December 31	2017	2016	2015
Balance sheet *(millions of dollars)*			
Total assets	**$ 18,068.9**	$ 17,314.0	$ 14,949.0
Long-term liabilities	**$ 8,458.4**	$ 7,737.9	$ 5,880.1
Regulatory ratios			
Tier 1 capital ratio	**35.7 %**	34.2 %	31.2 %
Provincial capital ratio	**53.6 %**	51.6 %	40.6 %
Borrowing multiple (times)	**12.4:1**	11.9:1	13.2:1
Share information *(thousands of dollars, unless otherwise indicated)*			
Outstanding $1 par value shares			
Class A – *credit unions*	**$ 428,101**	$ 416,952	$ 370,952
Class B – *cooperatives*	**$ 5**	$ 5	$ 5
Class C – *others*	**$ 7**	$ 7	$ 7
Outstanding $0.01 par value shares with redemption value of $100			
Class E – *credit unions*	**$ 30**	$ 32	$ 32





Profit for the year decreased by $8.4 million or 14.7 per cent from 2016 to $48.6 million in 2017. In 2017 Central 1 invested a total of $20.5 million in strategic initiatives, most notably its UX Platform, external IFRS 9 Loan Loss model, and the Transformation Office. Central 1's investments in these initiatives is essential to ensuring that Central 1 can provide its members with the products and services that will enable them to remain competitive in the future. These increased costs were partially offset by a $5.9 million increase in net financial income reflecting the increased size of the balance sheet and lending activities.

Compared to 2016, return on average assets (ROA) decreased 10 bps and return on average equity (ROE) decreased 120 bps. Central 1's total assets increased 4.4 per cent and average assets increased 13.4 per cent from 2016 due to increased mandatory deposits from credit unions and external borrowings. The decreased profit combined with higher level of average assets and average equity contributed to the lower ROA and ROE. Central 1's capital levels are driven largely by the amount of deposits and external borrowings on its balance sheet.

Central 1's overall productivity ratio, defined as the ratio of operating expenses to the sum of net financial income and other income, increased from 68.1 per cent in 2016 to 73.6 per cent in 2017. The increase was directly attributable to increased costs to support strategic initiatives. Central 1's non-financial productivity ratio, which excludes the variability within net financial income, increased from 100.8 per cent in 2016 to 109.7 per cent in 2017.

As a wholesale provider of services to its credit union members, Central 1 prices many of its services on a cost-recovery basis, rather than at levels that would enhance profit and improve ROE or ROA. Under normal circumstances, this would keep Central 1's productivity ratio higher than would be the case if profit margins were built into product prices.

The following table summarizes Central 1's Financial Objectives as at December 31, 2017 with comparatives.

Figure 4 - Financial Objectives

	2017	2016	2015	Regulatory Requirement
Exceed return on average equity target				
Actual return	**4.4 %**	5.6 %	5.5 %	
Target return	**3.2 %**	3.0 %	3.7 %	
Maintain regulatory capital in excess of 15% of risk weighted assets at the year-end	**53.6 %**	51.6 %	40.6 %	> 10 %

Central 1 exceeded all of its financial objectives for 2017. Central 1's first objective is to earn a ROE equal to or greater than the target return. Central 1 must also ensure that it meets its regulatory capital requirements. The target ratio of regulatory capital, which should be at least equal to 15.0 per cent of risk weighted assets at the year-end as required by provincial regulations, was exceeded in 2017.

Jump to table of contents

Selected Annual Information

Statement of Financial Position

Cash and Liquid Assets

The following table summarizes Central 1's Cash and Liquid Assets for the MLP and WFS business lines as at December 31, 2017 with comparatives.

Figure 5 – Cash and Liquid Assets

December 31, 2017 (Millions of dollars)	MLP Liquid Assets	WFS Liquid Assets	Securities Received as Collateral	Total Liquid Assets	Encumbered Liquid Assets	Unencumbered Liquid Assets
Cash	$ 19.3	$ 531.2	$ –	$ 531.2	$ –	$ 531.2
Federal and provincial government issued and guaranteed securities	7,625.2	3,396.9	603.2	4,000.1	1,634.1	2,366.0
Corporate and financial institution securities AA or greater	354.4	1,084.6	–	1,084.6	21.1	1,063.5
U.S. dollar denominated corporate and financial institution securities AA or greater	37.6	148.9	–	148.9	–	148.9
Insured mortgages securitized as National Housing Act Mortgage-Backed Securities	–	176.8	–	176.8	–	176.8
Other assets	558.3	1,570.4	–	1,570.4	82.3	1,488.1
Total	**$ 8,594.8**	**$ 6,908.8**	**$ 603.2**	**$ 7,512.0**	**$ 1,737.5**	**$ 5,774.5**

December 31, 2016 (Millions of dollars)	MLP Liquid Assets	WFS Liquid Assets	Securities Received as Collateral	Total Liquid Assets	Encumbered Liquid Assets	Unencumbered Liquid Assets
Cash	$ 127.7	$ 359.4	$ –	$ 359.4	$ –	$ 359.4
Federal and provincial government issued and guaranteed securities	6,872.2	3,588.4	298.0	3,886.4	1,480.0	2,406.4
Corporate and financial institution securities AA or greater	1,046.3	2,093.5	–	2,093.5	42.5	2,051.0
U.S. dollar denominated corporate and financial institution securities AA or greater	102.8	418.5	–	418.5	–	418.5
Insured mortgages securitized as National Housing Act Mortgage-Backed Securities	–	258.1	–	258.1	–	258.1
Other assets	–	374.7	–	374.7	95.6	279.1
Total	$ 8,149.0	$ 7,092.6	$ 298.0	$ 7,390.6	$ 1,618.1	$ 5,772.5

December 31, 2015 (Millions of dollars)	MLP Liquid Assets	WFS Liquid Assets	Securities Received as Collateral	Total Liquid Assets	Encumbered Liquid Assets	Unencumbered Liquid Assets
Cash	$ 283.7	$ –	$ –	$ –	$ –	$ –
Federal and provincial government issued and guaranteed securities	6,135.6	2,270.8	55.9	2,326.7	1,279.2	1,047.5
Corporate and financial institution securities AA or greater	708.8	2,088.6	100.8	2,189.4	107.3	2,082.1
U.S. dollar denominated corporate and financial institution securities AA or greater	268.6	389.6	–	389.6	–	389.6
Insured mortgages securitized as National Housing Act Mortgage-Backed Securities	–	207.9	–	207.9	–	207.9
Other assets	–	541.0	–	541.0	–	541.0
Total	$ 7,396.7	$ 5,497.9	$ 156.7	$ 5,654.6	$ 1,386.5	$ 4,268.1

Jump to table of contents

In addition to managing the MLP on behalf of the network, Central 1 manages its own liquidity within WFS. Consistent with Central 1's designation as a D-SIFI, all Canadian dollar denominated securities in the MLP are eligible for collateral under the BOC's Standing Liquidity Facility.

The liquidity management framework for WFS is designed to support the liquidity requirements of the network under non-stressed conditions, to ensure that credit unions have access to reliable and cost-effective sources of liquidity, as well as Central 1's potential cash and collateral obligations, including collateral pledged to the BOC's Large Value Transfer System. Central 1 maintains a portfolio of high quality liquid assets (HQLA) in WFS to support these objectives.

Cash and liquid assets increased $0.4 billion in MLP driven by higher mandatory deposits, and decreased $0.2 billion in WFS year-over-year driven by lower non-mandatory deposits outstanding. Cash and liquid assets in MLP represented 47.6 per cent of Central 1's total assets, up from 47.1 per cent in 2016. Cash and liquid assets in WFS represented 38.2 per cent of Central 1's total assets, down from 41.0 per cent in 2016.

Loans

The following table summarizes Central 1's Loans as at December 31, 2017 with comparatives.

Figure 6 - Loans

December 31 (Millions of dollars)	2017	2016	2015
Credit unions loans	**$ 782.3**	$ 329.5	$ 784.1
Syndicated commercial loans	**622.1**	611.2	518.7
Non syndicated commercial loans	**12.9**	13.4	16.0
Other loans	**7.9**	8.8	9.4
Residential mortgages	**139.9**	161.6	98.0
	782.8	795.0	642.1
Securities acquired under reverse repurchase agreements	**591.9**	316.4	48.9
	$ 2,157.0	$ 1,440.9	$ 1,475.1

** Total loan balances are before the allowance for credit losses and exclude accrued interest, premium and fair value hedge adjustment.*

Central 1 provides clearing lines of credit and short- and medium-term loans to its members. All lending activities are closely integrated and coordinated with Central 1's liquidity management. Clearing lines of credit, available in two currencies, are used to cover cash requirements arising from the settlement of payment transactions. Short- and medium-term loans are used by members for cash management purposes, balance sheet funding and asset acquisitions.

Central 1's Commercial Lending Group participates in loan syndications with members. Central 1 also periodically acquires pools of residential mortgages from its members to provide them with liquidity. Central 1 may resell these pools to other credit unions or securitize them. Most pools acquired by Central 1 are held for short-term periods, pending for resale to other credit unions or securitization.

Total loans increased $716.1 million compared to the prior year, driven by higher credit unions loans and securities acquired under reverse repurchase agreements, which are generally used to support Central 1's credit union members' participation in the Canada Mortgage Bond (CMB) Program. These increases were partially offset by lower residential mortgages. Commercial loans represented 29.4 per cent of Central 1's total loan portfolio, down from 43.3 per cent in the prior year.

Jump to table of contents

Funding

The following table summarizes Central 1’s Sources of Funding as at December 31, 2017 with comparatives.

Figure 7 - Sources of Funding

December 31 (Billions of dollars)	2017	2016	2015
Deposits and trading liabilities by type			
Mandatory deposits	$ 8.1	$ 7.6	$ 6.9
Non-mandatory deposits	3.1	3.5	3.3
Deposits from member credit unions	11.2	11.1	10.2
Deposits from non-credit unions	0.8	0.8	0.6
	12.0	11.9	10.8
Debt securities issued			
Commercial paper issued	0.9	0.7	0.5
Medium-term notes issued	1.3	0.8	0.6
Subordinated liabilities	0.4	0.4	0.2
	2.6	1.9	1.3
Obligations under the CMB Program	1.2	1.2	1.0
Securities under repurchase agreements	0.5	0.3	0.2
	$ 16.3	$ 15.3	$ 13.3

Central 1’s primary funding source is deposits from credit unions, the majority of which are required by regulation or by contractual agreement. Additionally, credit unions deposit excess liquidity with Central 1, which constitutes the largest funding source for WFS. Supplementary to this core deposit base are Central 1’s commercial paper and medium-term note programs. Central 1 also uses asset securitization programs as an alternative source of funding and asset/liability management (ALM) purposes.

Deposits from Central 1’s member credit unions increased $0.1 billion from the prior year. Mandatory deposits from credit unions increased $0.5 billion, reflective of the growth within the B.C. and Ontario credit union networks. Non-mandatory deposits from credit unions decreased $0.4 billion, due to decreased demand in discretionary deposits. Deposits from member credit unions represented 68.7 per cent of Central 1’s total funding portfolio at year-end, down from 72.5 per cent in the prior year.

Total debt securities outstanding increased $0.7 billion compared to the prior year. Debt securities represented 16.0 per cent of Central 1’s total funding portfolio at year end, up from 12.4 per cent in the prior year. Of the total amount outstanding, $1.3 billion was borrowed under Central 1’s medium-term note facility, $0.4 billion was borrowed through subordinated debt issuance and the remainder was borrowed through Central 1’s commercial paper facility. The increase in debt securities was the main cause of the overall growth on Central 1’s balance sheet.

Direct securitization transactions are accounted for on-balance sheet while indirect securitizations are off-balance sheet. Total obligations under the CMB Program were $1.2 billion, remained in line with the prior year. Details of the balances can be found in Notes 6 and 16 of the Consolidated Financial Statements.

Equity

Central 1 distributes the net earnings of the MLP to its Class A members as dividends and requires that its Class A members purchase additional Class A shares to capitalize the growth of the MLP. The increase in share capital in the MLP and the earnings retained by Central 1’s other business lines account for most of the increase in equity year-over-year.

Central 1’s total equity increased $34.2 million during 2017 to $1,119.1 million, compared to an increase in equity of $95.9 million during the prior year. FICOM’s amendment on Central 1’s regulatory requirements for borrowing multiples on August 16, 2017 allowed Central 1 to return its capital to Class A members in a form of a share redemption and dividend payment. On September 29, 2017, Central 1 redeemed $30.0 million of Class A shares and paid $5.0 million dividends to Class A members. On October 27, 2017, Central 1 reacquired $15.0 million of Class E shares.

Central 1's Consolidated Statements of Changes in Equity provides a summary of items that increase or decrease the total equity and Note 21 of the Consolidated Financial Statements provides details on the changes in share capital.

Statement of Profit or Loss

Net Financial Income

Net financial income of $73.4 million increased $5.9 million compared to the prior year. The following table shows the yearly average balances of Central 1's interest earning assets and interest-bearing liabilities, its relative contribution or charge to interest margin, together with related yields and costs.

Figure 8 - Comparative Interest Income and Expense

December 31 (Millions of dollars)	2017 Average Balance	2017 Interest	2017 Average Rate	2016 Average Balance	2016 Interest	2016 Average Rate	2015 Average Balance	2015 Interest	2015 Average Rate
Assets									
Cash and securities	$ 14,702.3	$ 208.0	1.4 %	$ 13,252.0	$ 171.0	1.3 %	$ 12,237.5	$ 155.2	1.3 %
Deposits with regulated financial institutions	6.0	0.2	3.3 %	80.9	0.1	0.1 %	5.9	0.1	1.7 %
Reinvestment assets under CMB Program	463.2	8.2	1.8 %	256.1	5.9	2.3 %	109.8	1.9	1.7 %
Loans	1,928.6	37.5	1.9 %	1,482.0	29.5	2.0 %	1,027.8	21.0	2.0 %
Total interest earning assets	17,100.1	253.9	1.5 %	15,071.0	206.5	1.4 %	13,381.0	178.2	1.3 %
Other assets	751.1	–	0.0 %	668.6	–	0.0 %	661.1	–	0.0 %
Total assets	$ 17,851.2	$ 253.9	1.4 %	$ 15,739.6	$ 206.5	1.3 %	$ 14,042.1	$ 178.2	1.3 %
Liabilities and Equity									
Deposits									
Credit union mandatory deposits	$ 7,750.6	$ 91.5	1.2 %	$ 7,169.7	$ 79.7	1.1 %	$ 6,688.8	$ 83.9	1.3 %
Credit union current accounts	1,050.4	7.7	0.7 %	1,071.0	4.9	0.5 %	1,014.8	4.9	0.5 %
Credit union other	2,170.0	35.1	1.6 %	2,172.9	30.1	1.4 %	1,406.5	18.1	1.3 %
Non credit union	814.7	3.7	0.5 %	690.2	3.1	0.4 %	658.3	7.5	1.1 %
Debt securities issued	1,723.0	26.7	1.5 %	1,242.2	14.4	1.2 %	1,319.8	17.0	1.3 %
Obligations under the CMB Program	1,238.3	18.7	1.5 %	1,107.6	17.9	1.6 %	807.5	14.1	1.7 %
Securities under repurchase agreements	600.7	4.8	0.8 %	259.1	1.2	0.5 %	215.1	1.3	0.6 %
Subordinated liabilities	422.1	12.5	3.0 %	261.0	7.6	2.9 %	218.0	6.3	2.9 %
Total	15,769.8	200.7	1.3 %	13,973.7	158.9	1.1 %	12,328.8	153.1	1.2 %
Other liabilities	969.7	–	0.0 %	742.7	–	0.0 %	764.2	–	0.0 %
Equity	1,111.7	–	0.0 %	1,023.2	–	0.0 %	949.1	–	0.0 %
Total liabilities and equity	$ 17,851.2	$ 200.7	1.1 %	$ 15,739.6	$ 158.9	1.0 %	$ 14,042.1	$ 153.1	1.1 %
Interest margin		$ 53.2	0.3 %		$ 47.6	0.3 %		$ 25.1	0.2 %
Realized and unrealized gains on financial instruments		20.2	0.1 %		19.9	0.1 %		25.0	0.2 %
Net financial income		$ 73.4	0.4 %		$ 67.5	0.4 %		$ 50.1	0.4 %

Interest margin increased $5.6 million compared to the prior year, primarily driven by the growth in average net assets. The BOC interest rate hikes had a positive impact on interest margin as the weighted average yield on assets increase relative to the weighted average cost of liabilities. This is primarily due to the difference in timing of fixed rate liability maturities compared to the maturities within the investment portfolio.

Central 1's funding mix has shifted year-over-year with a higher proportion of debt securities issued. The new issuances of $900.0 million in total for medium-term notes in 2017 combined with the $300.0 million matured in May 2017 have contributed to a higher outstanding balance of long term external borrowings in 2017. This increase results in higher interest expense.

Notes 22 and 23 of the Consolidated Financial Statements contain details of gain (loss) on disposal of financial instruments and change in fair value of financial instruments reported during the year.

Operating Income (Loss)

The following table summarizes Central 1's Operating Income (Loss) for the year ended December 31, 2017 with comparatives.

Figure 9 - Operating Income (Loss)

Years ended December 31 (Millions of dollars)	2017	2016	2015
Other income			
Mandatory Liquidity Pool	$ (0.4)	$ –	$ –
Wholesale Financial Services			
Lending fees	6.4	5.6	4.7
Securitization fees	7.4	6.9	5.0
Foreign exchange income	5.9	6.1	5.9
Other	7.4	7.6	8.0
Digital & Payment Services			
Payment processing and other fees	53.7	53.0	50.6
Digital banking fees	31.8	30.5	28.9
Dues Funded Activities	11.8	12.0	13.4
Other			
Equity interest in affiliates	14.4	8.0	6.7
Income from investees	3.7	4.9	4.1
Litigation settlement	1.1	-	7.7
Other	6.7	5.9	5.7
Total other income	149.9	140.5	140.7
Operating expenses			
Salaries and employee benefits	76.1	74.2	69.5
Premises and equipment	9.1	7.3	7.1
Other administrative expenses			
Management information systems	13.9	9.5	6.9
Flow through membership dues	6.3	5.5	5.0
Professional fees	22.7	10.5	5.4
Other	36.4	34.6	35.6
Total operating expenses	164.5	141.6	129.5
Operating income (loss)	$ (14.6)	$ (1.1)	$ 11.2

Central 1 reported an operating loss of $14.6 million, compared to an operating loss of $1.1 million in 2016. Excluding the one-time litigation settlement, other income would have increased $8.3 million from the prior year. Of this increase, income from Central 1's investees and affiliates accounted for $5.2 million due to an increase in the related investments in affiliates accounted for using the equity method of accounting. The remaining increase was contributed by the increased electronic payments *Interac*® e-Transfer volumes and digital banking fees within Digital & Payment Services together with higher securitization and standby lending fee revenues within WFS.

Operating expenses increased $22.9 million primarily due to increased professional fees and other expenditures to support strategic initiatives, including the $6.4 million incurred to develop the UX Platform and an increase of $2.3 million on the external IFRS 9 Loan Loss model. The external IFRS 9 Loan Loss model is a national platform that provides expected credit loss calculations for credit union members and an analytical layer offering multi-tenant, scalability and security features critical to a national platform. During 2017, Central 1 also incurred $10.9 million in other strategic initiatives of which $2.2 million was incurred for the Transformation Office.

Income Taxes

Central 1's combined federal and provincial statutory tax rate is 26.1 per cent. Central 1's effective tax rate for the year was 17.5 per cent, up from 14.0 per cent in 2016. The increase is primarily the result of tax credits that were realized in 2016 and none in 2017. This was partially offset with a lower B.C. tax rate due to changes in the B.C. provincial budgets in 2017. The B.C. Provincial Government's September 2017 Budget (the Budget), enacted in October 2017, included re-establishing the preferential tax treatment of the full credit union deduction. The Budget also kept the previous decrease to the small business tax rate from 2.5 per cent to 2.0 per cent effective April 1, 2017. Credit unions in B.C. applying the preferential tax treatment effectively pay B.C. provincial tax at the small business rate. The effective B.C. provincial small business tax rate for 2017 was pro-rated to 2.12 per cent.

Results by Segment

Central 1's operations and activities are organized around three key business segments: MLP, WFS, and Digital & Payment Services. Central 1 also offers a variety of additional services that are funded by membership dues. All other activities or transactions, such as the costs of implementing strategic initiatives and exploring strategic alternatives to enhance the ability to support credit unions in the future, are reported in "Other". The costs of Corporate Support functions are also included in Other and are attributed to business lines as appropriate.

Periodically, certain business lines and units are transferred among business segments to closely align Central 1's organizational structure with its strategic priorities. In addition, revenue and expense allocations are updated to more accurately align with current experience. Results for prior periods are restated to conform to the current period presentation.

The following table summarizes Central 1's Results by Segment for the year ended December 31, 2017 with comparatives.

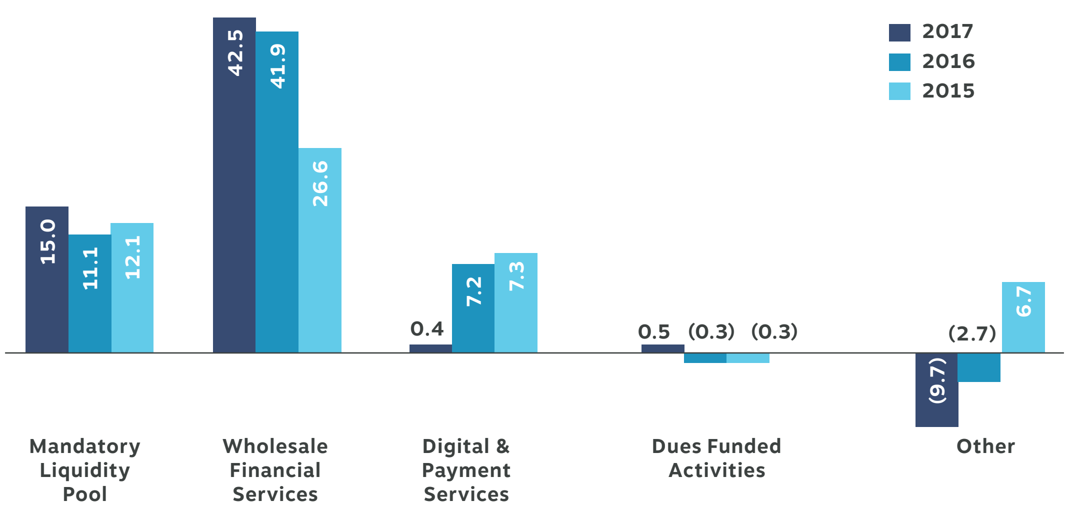
Figure 10 - Results by Segment

For the year ended December 31, 2017 (Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including provision for credit losses	$ 26,555	$ 51,536	$ (292)	$ –	$ (4,234)	$ 73,565
Other income	(381)	26,980	85,493	11,787	26,010	149,889
Net financial and other income	26,174	78,516	85,201	11,787	21,776	223,454
Operating expenses	8,045	25,971	84,763	11,240	34,470	164,489
Profit (loss) before income taxes	18,129	52,545	438	547	(12,694)	58,965
Income taxes (recoveries)	3,154	10,006	71	88	(2,998)	10,321
Profit (loss) for the period	**$ 14,975**	**$ 42,539**	**$ 367**	**$ 459**	**$ (9,696)**	**$ 48,644**

For the year ended December 31, 2016 (Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including provision for credit losses	$ 21,159	$ 50,719	$ (255)	$ –	$ (4,180)	$ 67,443
Other income	(32)	26,184	83,511	12,010	18,826	140,499
Net financial and other income	21,127	76,903	83,256	12,010	14,646	207,942
Operating expenses	7,547	25,586	74,452	12,396	21,616	141,597
Profit (loss) before income taxes	13,580	51,317	8,804	(386)	(6,970)	66,345
Income taxes (recoveries)	2,507	9,465	1,625	(71)	(4,221)	9,305
Profit (loss) for the period	$ 11,073	$ 41,852	$ 7,179	$ (315)	$ (2,749)	$ 57,040

For the year ended December 31, 2015 (Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including provision for credit losses	$ 21,405	$ 33,311	$ (242)	$ –	$ (4,320)	$ 50,154
Other income	8	23,587	79,450	13,414	24,247	140,706
Net financial and other income	21,413	56,898	79,208	13,414	19,927	190,860
Operating expenses	6,985	25,098	70,320	13,778	13,366	129,547
Profit (loss) before income taxes	14,428	31,800	8,888	(364)	6,561	61,313
Income taxes (recoveries)	2,365	5,212	1,563	(60)	(117)	8,963
Profit (loss) for the period	$ 12,063	$ 26,588	$ 7,325	$ (304)	$ 6,678	$ 52,350

Profit (Loss) for the Period
(Millions of dollars)



Mandatory Liquidity Pool
MLP reported a profit of $15.0 million, an increase of $3.9 million compared to the prior year. Interest margin increased by $5.2 million reflecting the increased size of the investment pool. Net realized and unrealized gains increased $0.2 million due to the mark-to-market gains on deposits resulting from rising interest rates partially offset by the mark-to-market losses on securities mitigated by narrowing of credit spreads in 2017. The increase was partially offset by higher operating expenses due to increased management information systems expenses and lower foreign exchange income.

Wholesale Financial Services
WFS reported a profit of $42.5 million, an increase of $0.6 million compared to the prior year. Interest margin increased by $0.5 million due to a combination of factors. Increased credit union lending activities contributed to the improved interest income, which was partially offset by higher interest expense due to increased external borrowings. Net realized and unrealized gains were largely in line with the prior year.

WFS' other income increased $0.8 million compared to the prior year due to higher fee revenue from securitization and standby lending facilities, partially offset by lower commercial lending and foreign exchange income. Operating expenses increased $0.4 million compared to the prior year due to increased staff salaries and management information system costs.

Digital & Payment Services
Digital & Payment Services' profit decreased by $6.8 million from last year, largely driven by a decreased profit within the digital banking area partially offset by an increased profit within payments operations. During the year, Central 1 incurred $6.4 million in the development of the UX Platform, which was partially offset by a $1.3 million increase in digital banking fees. While paper payments volumes have declined over time, the lower costs related to image capture and project node together with increased *Interac*® volumes resulted in increased profits within Payments operations.

Dues Funded Activities
Dues Funded Activities reported a profit of $0.5 million, compared to a loss of $0.3 million in 2016. The objective of these activities is to provide services to members on a cost-recovery basis. This area performed better than anticipated due to improvements in operating efficiency. These improvements will result in a reduced level of dues funding in 2018.

Other
The Other operating segment reported a loss of $9.7 million, compared to a loss of $2.7 million in 2016. Operating expenses within this segment increased $12.9 million from a year ago mainly due to increased costs incurred to support Central 1's strategic initiatives. The $2.3 million increased spending on the development of the external IFRS 9 Loan Loss model together with increased staff complement to support corporate and strategic projects also partly contributed to the increase in the operating expenses. These increases were partially offset by the $1.1 million final litigation settlement and increased income from investees and affiliates.

Summary of Quarterly Results

Quarterly Results

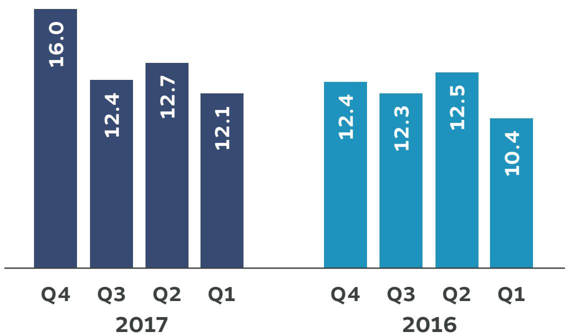
The following table summarizes Central 1's Quarterly Earnings for fiscal 2017 and 2016.

Figure 11 - Quarterly Earnings

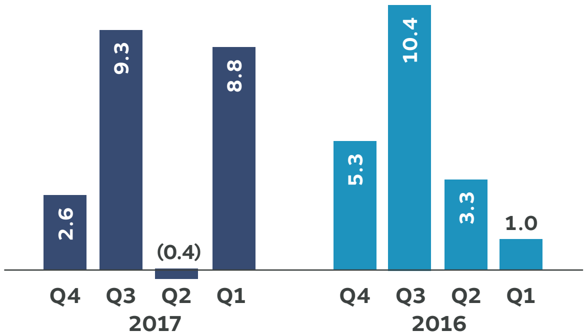
(Thousands of dollars, except as indicated)	2017 Q4	2017 Q3	2017 Q2	2017 Q1	2016 Q4	2016 Q3	2016 Q2	2016 Q1
Total interest income	**$ 73,208**	$ 62,781	$ 60,513	$ 57,366	$ 56,143	$ 52,296	$ 49,975	$ 48,059
Total interest expense	**57,171**	50,407	47,807	45,294	43,784	39,958	37,477	37,646
Interest margin	**16,037**	12,374	12,706	12,072	12,359	12,338	12,498	10,413
Realized and unrealized gains (losses)	**2,579**	9,296	(434)	8,815	5,286	10,395	3,261	979
Recovery of (provision for) credit losses	**(1)**	8	140	(27)	(6)	22	(70)	(32)
	18,615	21,678	12,412	20,860	17,639	22,755	15,689	11,360
Other income	**38,620**	37,656	38,575	35,038	35,431	34,461	38,333	32,274
Operating expenses	**(46,892)**	(40,454)	(38,892)	(38,251)	(36,408)	(32,868)	(38,061)	(34,260)
Operating income (loss)	**(8,272)**	(2,798)	(317)	(3,213)	(977)	1,593	272	(1,986)
Profit before income taxes	**10,343**	18,880	12,095	17,647	16,662	24,348	15,961	9,374
Income taxes	**(2,463)**	(3,182)	(1,643)	(3,033)	(2,942)	(2,889)	(2,592)	(882)
Profit for the period	**$ 7,880**	$ 15,698	$ 10,452	$ 14,614	$ 13,720	$ 21,459	$ 13,369	$ 8,492
Weighted average shares outstanding *(millions)*	**417.1**	440.3	425.2	417.0	396.1	385.0	375.8	371.0
Earnings per share								
Basic *(cents)*	**1.9**	3.6	2.5	3.5	3.5	5.6	3.6	2.3
Diluted *(cents)*	**1.9**	3.6	2.5	3.5	3.5	5.6	3.6	2.3

**Earnings per share calculated for a central credit union must be taken in the context that member shares may not be traded or transferred.*

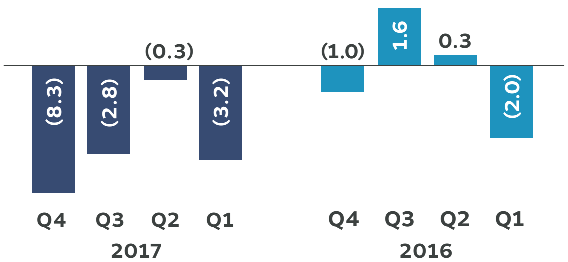
Interest Margin
(Millions of dollars)



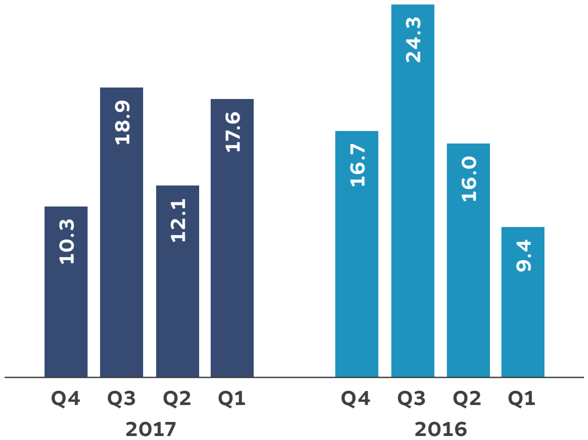
Realized and Unrealized Gains (Losses)
(Millions of dollars)



Operating Income (Loss)
(Millions of dollars)



Profit Before Income Taxes
(Millions of dollars)



Central 1 experienced significant growth in its interest margin during the fourth quarter of 2017, compared to the previous quarters in the past two years. The $16.0 million interest margin represents an increase of $3.6 million or 30.0 per cent compared to the same period in 2016. The BOC interest rate hikes during 2017 contributed to the widening of Central 1's net interest spread, combined with the increase in the average net asset resulted in a significant boost in the interest margin during the fourth quarter of 2017. This is primarily due to the difference in timing of fixed rate liability maturities compared to the maturities within the investment portfolio.

Net realized and unrealized gains (losses) have a significant impact on profit or loss and their timing and magnitude are not predictable.

Q4 2017 vs Q4 2016

Net Financial Income

Net financial income increased $1.0 million compared to the fourth quarter of 2016. The increase was driven by an increase in interest margin of $3.7 million due to the widened spread between interest earning assets and interest-bearing liabilities in the fourth quarter of 2017. The increases in lending activities and average assets balance also contributed to higher interest income compared to the fourth quarter of prior year. This increase was partially offset by the increased outstanding medium-term notes and commercial paper in 2017. Net realized and unrealized gains decreased by $2.7 million mainly due to losses on disposal of available-for-sale assets in the fourth quarter of 2017.

Operating Income (Loss)

The following table summarizes Central 1's Operating Income (Loss) for the three months ended December 31, 2017 with comparatives.

Figure 12 - Operating Income (Loss)

For the three months ended December 31 (Millions of dollars)	2017	2016	2015
Other income			
Mandatory Liquidity Pool	$ –	$ 0.1	$ 0.1
Wholesale Financial Services			
Lending fees	1.8	1.7	1.3
Securitization fees	1.9	1.9	1.4
Foreign exchange income	1.8	1.8	1.8
Other	1.9	2.0	2.0
Digital & Payment Services			
Payment processing and other fees	13.4	13.4	12.7
Digital banking fees	8.8	8.1	7.4
Dues Funded Activities	2.9	3.2	3.9
Other			
Equity interest in affiliates	4.2	1.9	2.8
Income from investees	0.1	0.6	0.7
Litigation settlement	–	–	–
Other	1.8	0.7	0.7
Total other income	38.6	35.4	34.8
Operating expenses			
Salaries and employee benefits	18.5	18.5	18.3
Premises and equipment	2.9	2.2	2.1
Other administrative expenses			
Management information systems	3.3	2.5	1.9
Flow through membership dues	1.7	1.3	1.4
Professional fees	11.3	3.8	1.6
Other	9.2	8.1	7.9
Total operating expenses	46.9	36.4	33.2
Operating income (loss)	$ (8.3)	$ (1.0)	$ 1.6

Central 1 reported an operating loss of $8.3 million for the fourth quarter of 2017, compared to an operating loss of $1.0 million for the same period in 2016.

Jump to table of contents

Other income during the fourth quarter increased by $3.2 million primarily driven by increased digital banking fees revenue together with higher income from affiliates accounted for under the equity method of accounting.

Operating expenses increased $10.5 million from a year ago primarily due to higher costs incurred to support Central 1's strategic initiatives including the UX Platform and Transformation Office.

Results by Segment

The following table summarizes Central 1's Results by Segment for the three months ended December 31, 2017 with comparatives.

Figure 13 - Results by Segment

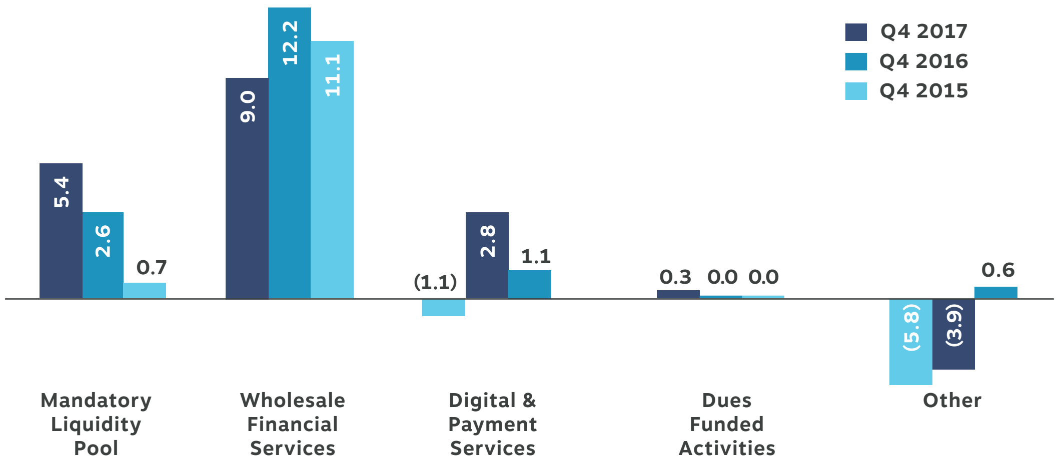
For the three months ended December 31, 2017 (Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including provision for credit losses	$ 8,235	$ 11,525	$ (87)	$ –	$ (1,058)	$ 18,615
Other income	44	7,368	22,180	2,880	6,148	38,620
Net financial and other income	8,279	18,893	22,093	2,880	5,090	57,235
Operating expenses	2,014	6,346	23,372	2,563	12,597	46,892
Profit (loss) before income taxes	6,265	12,547	(1,279)	317	(7,507)	10,343
Income taxes (recoveries)	898	3,523	(217)	(18)	(1,723)	2,463
Profit (loss) for the period	**$ 5,367**	**$ 9,024**	**$ (1,062)**	**$ 335**	**$ (5,784)**	**$ 7,880**

For the three months ended December 31, 2016 (Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including provision for credit losses	$ 4,925	$ 13,822	$ (71)	$ –	$ (1,037)	$ 17,639
Other income	107	7,449	21,476	3,155	3,244	35,431
Net financial and other income	5,032	21,271	21,405	3,155	2,207	53,070
Operating expenses	1,827	6,207	18,023	3,187	7,164	36,408
Profit (loss) before income taxes	3,205	15,064	3,382	(32)	(4,957)	16,662
Income taxes (recoveries)	592	2,844	624	(77)	(1,041)	2,942
Profit (loss) for the period	$ 2,613	$ 12,220	$ 2,758	$ 45	$ (3,916)	$ 13,720

For the three months ended December 31, 2015 (Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including provision for credit losses	$ 2,380	$ 12,996	$ (50)	$ –	$ (1,064)	$ 14,262
Other income	90	6,470	20,063	3,882	4,327	34,832
Net financial and other income	2,470	19,466	20,013	3,882	3,263	49,094
Operating expenses	1,686	6,222	18,434	3,641	3,298	33,281
Profit (loss) before income taxes	784	13,244	1,579	241	(35)	15,813
Income taxes (recoveries)	129	2,152	430	211	(604)	2,318
Profit (loss) for the period	$ 655	$ 11,092	$ 1,149	$ 30	$ 569	$ 13,495

Jump to table of contents

Profit (Loss) for the Period
(Millions of dollars)



Mandatory Liquidity Pool

MLP reported a profit of $5.4 million, an increase of $2.8 million compared to the fourth quarter of 2016. Net financial income increased by $3.3 million. Net realized and unrealized gains decreased $0.5 million, mainly due to higher unrealized losses from deposits partially offset by gains in securities. Interest margin increased $3.8 million, driven by the combination of an 8.9 per cent increase in interest earning assets and the widened spread between securities and deposits interest rates. Operating expenses were largely in line with the fourth quarter of the prior year.

Wholesale Financial Services

WFS reported a profit of $9.0 million, a decrease of $3.2 million compared to the fourth quarter of 2016. Net financial income decreased $2.3 million. Net realized and unrealized losses decreased $2.2 million mainly due to higher net losses on disposal of available-for-sale assets in the fourth quarter of 2017. Interest margin and other income were largely in line with the fourth quarter of the prior year. Operating expenses were largely in line with the fourth quarter of the prior year.

Digital & Payment Services

Digital & Payment Services' profit decreased $3.9 million from the fourth quarter of 2016. Digital Banking reported a higher loss over the same period last year attributed to increased professional fees and infrastructure expenses arising from the development of the UX Platform, partially offset by increased digital banking fees.

Dues Funded Activities

Dues Funded Activities reported a profit of $0.3 million, compared with a breakeven result from the same period in 2016. The objective of these activities is to provide services to members on a cost-recovery basis. This area performed better than anticipated due to improvements in operating efficiency. These improvements will result in a reduced level of dues funding in 2018.

Other

The Other operating segment reported a loss of $5.8 million, compared with a loss of $3.9 million for the same period in 2016. The operating expenses increased $5.4 million mostly related to cost incurred to support Central 1's strategic initiatives including Transformation Office. This increase was partially offset by the increased income from affiliates accounted for using the equity method of accounting.

Jump to table of contents

2016 Financial Performance Review

The preceding discussions in the MD&A focused on Central 1's performance for the year ended December 31, 2017. This section compares the performance for the years ended December 31, 2016 and 2015.

Overall Performance

Profit for the year increased by $4.6 million or 8.8 per cent from 2015 to $57.0 million in 2016. Net financial income increased by $17.4 million in 2016, which was partially offset by a $12.3 million decrease in operating income due to an increase in Central 1's staff complement in Corporate Support functions as well as increased professional fees and other expenditures to support strategic initiatives.

ROA remained consistent with the prior year, while ROE of 5.6 per cent in 2016 increased 10.0 bps from 2015. Central 1's capital levels are driven in large part by the amount of deposits in the MLP as credit unions are required to contribute capital in proportion to the growth of mandatory deposits. Central 1's average equity increased by 7.8 per cent with the result that the increase in profits in 2016 was largely offset by increased equity in deriving Central 1's ROE.

Results by Segment

Mandatory Liquidity Pool

MLP reported a profit of $11.1 million, a decrease of $1.0 million compared to the prior year. Interest margin increased by $0.6 million reflecting the increased size of the investment pool, while net realized and unrealized gains decreased $0.9 million due to lower net gains on disposal of available-for-sale assets. Operating expenses increased $0.6 million primarily due to increased costs of maintaining Central 1's management information systems. Central 1 completed the second phase of a multi-phase treasury management system upgrade during the first quarter of 2016 with the associated operating costs being allocated to Central 1's MLP and WFS business lines.

Wholesale Financial Services

WFS reported a profit of $41.9 million, an increase of $15.3 million compared to the prior year. Interest margin increased by $21.7 million due to a combination of factors. Increased levels of liquidity in the credit union network led to significant growth in non-mandatory deposits resulting in higher average assets and a lower weighted cost of funds. Increased securitization and lending activities also contributed to the improvement over 2015. Net realized and unrealized gains decreased $4.1 million due to lower net gains on disposal of available-for-sale assets.

WFS' other income increased $2.6 million compared to the prior year due to higher fee revenue from securitization, standby lending facilities, commercial lending and foreign exchange income. Operating expenses increased $0.5 million compared to the prior year due to increased staff salaries and management information system expenses.

Digital & Payment Services

Digital & Payment Services profit declined by $0.1 million compared to 2015 led by lower profit within digital banking area, partially offset by a small increase of profit within Payment operations. The increased investment in infrastructure to support future growth outweighed the increased digital banking fees. While paper payment volumes have declined over time, price increases resulted in paper profits increasing by $0.3 million in 2016. Meanwhile, electronic payment volumes have seen an increasing trend which resulted in a $0.4 million increase in profits in 2016.

Dues Funded Activities

Dues Funded Activities reported a loss of $0.3 million, a slight decrease from 2016. The decrease in dues revenue was offset by lower operating expenses.

Other

The Other operating segment reported a loss of $2.7 million, compared to a profit of $6.7 million in 2015. Central 1 recorded a credit to income of $7.7 million in 2015 on a settlement of a long-standing legal claim. Excluding this credit after tax, Central 1 would have recorded a breakeven in this area in 2015. The resulting variance reflects the impact of several one-time restructuring charges totaling $1.9 million.

Income from investees and affiliates increased by $3.4 million over 2015, in part due to a one-time credit to income on the restructuring of Credit Union Central of Canada (now Canadian Credit Union Association) of $1.4 million recorded in 2016. Operating expenses within this segment increased by $8.3 million due largely to costs incurred to explore strategic alternatives to enhance Central 1's ability to support its members in the future. The costs of some Corporate Support functions also increased in 2016, but most of that increase was attributed to business lines.

Jump to table of contents

Off-Balance Sheet Arrangements

In the normal course of business, Central 1 enters into off-balance sheet arrangements, which fall into the following main categories: derivative financial instruments, guarantees and commitments, and assets under administration.

Derivative Financial Instruments

The following table summarizes the notional off-balance sheet derivative financial instruments as at December 31, 2017, with comparatives.

Figure 14 - Derivative Financial Instruments

Notional Amount December 31 (Millions of dollars)	2017	2016	2015
Interest rate contracts			
Bond forwards	**$ 96.7**	$ 79.5	$ 83.6
Futures contracts	**65.0**	432.8	205.0
Swap contracts	**30,292.7**	29,679.2	26,090.3
Options purchased	**10.0**	–	–
Options written	**10.0**	–	–
	30,474.4	30,191.5	26,378.9
Foreign exchange contracts			
Foreign exchange forward contracts	**247.4**	152.4	269.4
Other derivative contracts			
Equity index-linked options	**231.7**	253.7	278.9
	$ 30,953.5	$ 30,597.6	$ 26,927.2

**The table discloses derivative notional amounts while the Consolidated Statements of Financial Position records derivatives at fair value.*

Central 1 acts as a swap intermediary between the Canada Housing Trust and member credit unions and additionally provides derivative capabilities to member credit unions to be used in the ALM of their respective balance sheets. These activities represented $9.6 billion and $17.0 billion, respectively, of the total derivative notional balances as at December 31, 2017 (December 31, 2016 - $9.8 billion and $16.2 billion; December 31, 2015 - $7.2 billion and $16.6 billion).

Derivatives are primarily used in the ALM activities at Central 1. In addition, Central 1 facilitates the sale of derivative products to member credit unions to be used in the ALM of their respective balance sheets.

Derivatives are recorded in the Consolidated Statements of Financial Position at fair value. The notional amounts are not recorded on the Consolidated Statements of Financial Position as they do not represent actual amounts exchanged. Counterparty credit risk arising from derivative contracts is managed within the context of Central 1's overall credit risk policies and through the existence of Credit Support Annex (CSA) agreements in place with all of its non-credit union derivatives counterparties. Under a CSA, net fair value positions are collateralized with high quality liquid securities. Central 1's credit exposure to its credit union counterparties is secured by the general security arrangements it has in place with each credit union.

The fair value of derivative positions is presented in Note 7 to the Consolidated Financial Statements.

Jump to table of contents

Guarantees and Commitments

The following table presents the maximum amount of credit that Central 1 could be required to extend if commitments were to be fully utilized, and the maximum amount of guarantees that could be in effect if the maximum authorized amount were transacted.

Figure 15 - Guarantees and Commitments

December 31 (Millions of dollars)		2017		2016		2015
Commitments to extend credit	**$**	**4,327.9**	$	4,447.3	$	3,857.1
Guarantees						
Financial Guarantees	**$**	**367.5**	$	390.0	$	347.0
Performance Guarantees	**$**	**810.0**	$	440.0	$	340.0
Standby letters of credit	**$**	**187.9**	$	173.5	$	145.4
Mortgage purchase commitments	**$**	**–**	$	–	$	6.1
Future prepayment swap reinvestment commitment	**$**	**770.3**	$	431.5	$	–

Commitments to extend credit decreased $272.5 million from a year ago. Guarantees increased $347.5 million due to higher volumes, while standby letters of credit increased $14.4 million. Future prepayment swap reinvestment commitment increased $338.8 million.

In the normal course of business, Central 1 enters into various off-balance sheet credit instruments to meet the financing, credit and liquidity requirements of its member credit unions. These are in the form of commitments to extend credit, standby commitments, and performance guarantees.

Commitments to extend credit and standby commitments may expose Central 1 to liquidity and credit risk, and are managed in accordance with the liquidity and funding risk policy and the credit and counterparty risk policy.

Performance guarantees are provided to enable member credit unions to enter transactions with counterparties without the need to have that counterparty individually assess the credit worthiness of each individual institution, and are also managed in accordance with risk policies.

Note 29 of the Consolidated Financial Statements provides further details of guarantees and commitments.

Assets under Administration

The following table summarizes Assets under Administration (AUA) as at December 31, 2017 with comparatives.

Figure 16 - Assets under Administration

December 31 (Millions of dollars)		2017		2016		2015
Registered Retirement Savings Plans	**$**	**1,534.2**	$	1,558.0	$	1,581.9
Tax-Free Savings Accounts		**829.1**		729.2		630.1
Registered Retirement Income Funds/Life Income Funds		**396.3**		369.6		362.9
Registered Education Savings Plans		**224.0**		210.7		187.0
Registered Disability Savings Plans		**20.7**		15.8		11.1
	$	**3,004.3**	$	2,883.3	$	2,773.0

Jump to table of contents

AUA mainly include government approved registered plans for tax deferral purposes, which are administered by Central 1 or one of its wholly owned subsidiaries. Central 1 provides trust and administrative services on AUA for the members of the B.C. credit union network, and the subsidiary provides the same services for the members of the Ontario credit union network. These assets are owned by members of Central 1's member credit unions.

As at December 31, 2017, AUA totaled $3.0 billion, up $121.0 million or 4.2 per cent from a year ago, mainly due to an overall increase in the Tax-Free Savings Accounts business from both Ontario and B.C. credit unions. The Registered Retirement Income Funds/Life Income Funds and the Registered Education Savings Plans also increased slightly from a year ago, partially offset by a small decrease in the Registered Retirement Savings Plans.

Capital Management and Capital Resources

Central 1 manages capital to maintain strong capital limits in support of the risks and activities of the organization while generating an appropriate rate of return for its members. In addition to the regulatory requirements, Central 1 considers the expectation of credit rating agencies, credit union network growth and internal capital ratios. The longer term strategic goal is to optimize the capital usage and structure through the use of an economic capital model to provide a better return for the capital invested by the members.

Capital Management Framework

Central 1's capital management framework provides the policies and processes for defining, measuring, and allocating capital across the organization. It defines the roles and responsibilities in assessing capital adequacy, dividends and management of regulatory capital requirements.

A key component of Central 1's capital management is the annual capital planning process that involves teams from all areas of the organization. Capital planning has two key integrated components, the annual budget process which established operating targets for the organization and the Internal Capital Adequacy Assessment Process (ICAAP) in determining the required amount of capital to cover material risks to which the organization is exposed. The capital planning process includes forecasting growth in assets, earnings and capital in light of projected market conditions. These components are updated and monitored regularly during the year.

Central 1's share capital, with the exception of nominal amounts, is entirely held by its Class A members, which is comprised of B.C. credit unions and its member credit unions in Ontario. Central 1's policy requires an annual rebalancing of Class A share capital subscriptions so that member credit unions maintain Class A share capital in proportion to their assets.

Central 1's rules permit it to unconditionally require its Class A members to increase their investment in its share capital. Class A share calls are routinely scheduled each May and November to support the MLP. Under the terms of the Capital Policy, Central 1's Class A members are required to subscribe to additional Class A shares on a semi-annual basis to ensure that Central 1's MLP borrowing multiple meets regulatory requirements. As Class A members contribute the funding and capital, net earnings in the MLP is to be distributed to Central 1's Class A members as dividends on their Class A shares.

On April 28, 2017 Central 1's members approved changes to Central 1's capital structure and received regulatory approval by FICOM on December 5, 2017. The changes include the creation of a new class of shares, Class F shares, which will be the primary form of capital in the MLP. Credit unions will be required to subscribe to Class F shares based on the growth in deposits they place in the MLP rather than their share of credit union network assets.

On transition, credit unions' investment in Class A shares will be transferred to Class F shares which will then be rebalanced. Credit unions that hold a larger portion of mandatory deposits than Class A shares prior to transition will be required to contribute additional Class F shares during the rebalancing phase. Credit unions that hold a higher portion of Class A shares than their proportion of mandatory deposits will have a portion of their Class F shares redeemed. All credit unions will be required to subscribe to Class A shares in proportion to their share of network assets. The aggregate level of Class A shares will be based on Central 1's estimate of regulatory capital required to support strategic and operational initiatives over Central 1's planning cycle which is currently $50.0 million. As a result of the FICOM approval received on December 5, 2017, Central 1 plans to reacquire 750 thousand of Class E shares with an aggregate value of $75.0 million, which would reduce Central 1's regulatory capital. The series of transactions is anticipated to be completed by March 31, 2018.

Regulatory Capital

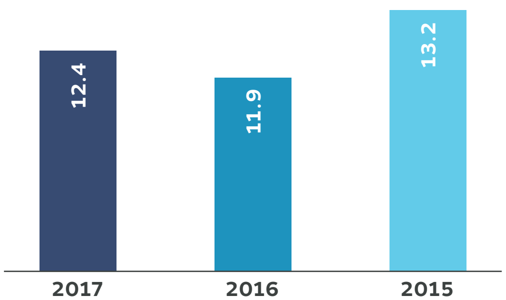
As at December 31, 2017, Central 1's Tier 1 regulatory capital was $1,081.3 million and total capital before deductions was $1,507.0 million. In determining regulatory capital, adjustments are required to amounts reflected in Central 1's Consolidated Statements of Financial Position. Deductions from capital are required for certain investments, including Central 1's substantial investments in affiliated cooperative organizations. The computation of the provincial capital base is broadly similar to the federal regulatory capital used for borrowing multiple purposes.

The following table summarizes Central 1's Capital Position as at December 31, 2017 with comparatives.

Figure 17 - Capital Position

December 31 (Millions of dollars)	2017	2016	2015
Share capital	$ **428.1**	$ 417.0	$ 371.0
Contributed surplus	**72.9**	87.9	87.9
Retained earnings	**585.0**	552.8	507.0
Less: accumulated net after tax gain in investment property	**(4.7)**	(4.7)	(4.6)
Tier 1 capital	**1,081.3**	1,053.0	961.3
Subordinated liabilities	**421.0**	421.0	218.0
Add: accumulated net after tax gain in investment property	**4.7**	4.7	4.6
Tier 2 capital	**425.7**	425.7	222.6
Total capital	**1,507.0**	1,478.7	1,183.9
Statutory capital adjustments	**(178.3)**	(171.2)	(162.2)
Capital base (federal)	$ **1,328.7**	$ 1,307.5	$ 1,021.7
Borrowing Multiple - consolidated	**12.4:1**	11.9:1	13.2:1
Borrowing Multiple - Mandatory Liquidity Pool	**15.7:1**	15.3:1	15.3:1
Borrowing Multiple - Wholesale Financial Services	**11.9:1**	10.5:1	12.9:1

Borrowing Multiple (Consolidated)



A three-year comparison of Central 1's capital adequacy, measured under both provincial and federal regulations, is provided above. Central 1 was in compliance with all regulatory capital requirements during these years.

Effective August 16, 2017, FICOM amended the borrowing multiple requirements to no more than 17.0:1 for the MLP segment and no more than 15.0:1 for the WFS segment. Following this amendment, Central 1 amended its capital limits which allowed Central 1 to return $50.0 million in capital to its Class A members. On September 29, 2017, Central 1 redeemed $30.0 million of Class A shares and paid $5.0 million dividends to Class A shareholders. On October 27, 2017, Central 1 reacquired $15.0 million of Class E shares.

Jump to table of contents

At December 31, 2017, Central 1's consolidated borrowing multiple was 12.4:1 compared to 11.9:1 at December 31, 2016. Central 1 manages the MLP's borrowing multiple through semi-annual capital calls from its membership and manages the WFS' borrowing multiple through growth in retained earnings and subordinated debt.

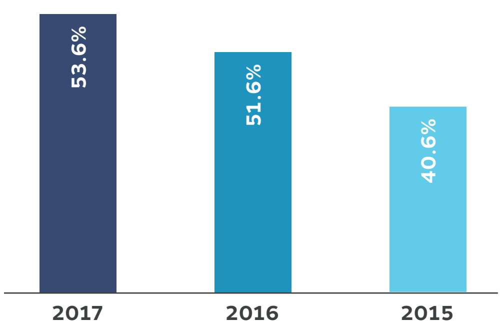
Note 34 to Central 1's Consolidated Financial Statements provides further details of capital management.

The following table summarizes Central 1's Risk Weighted Assets as at December 31, 2017 with comparatives.

Figure 18 - Risk Weighted Assets

December 31 (Millions of dollars)	Risk Weight	2017 Gross Assets	2017 Risk Weighted	2016 Gross Assets	2016 Risk Weighted	2015 Gross Assets	2015 Risk Weighted
On-balance sheet							
Cash	0-20 %	$ **550.8**	$ **110.1**	$ 487.1	$ 97.4	$ 106.8	$ 16.5
Securities	0-100 %	**14,953.2**	**1,017.7**	14,754.4	1,089.8	12,610.9	1,068.7
Deposits with regulated FIs	20-100 %	**6.0**	**1.2**	5.9	1.2	6.1	1.2
Loans	20-100 %	**2,162.1**	**791.0**	1,453.8	689.8	1,490.8	710.2
Other	0-100 %	**396.9**	**65.4**	612.8	287.3	734.4	344.1
		18,069.0	**1,985.4**	17,314.0	2,165.5	14,949.0	2,140.7
Off-balance sheet							
Derivatives (credit equivalent amounts)	0-100 %	**251.0**	**50.2**	238.4	47.7	263.2	52.7
Credit commitments	0-50 %	**5,935.1**	**292.2**	4,405.6	209.6	3,786.9	207.4
Guarantees and letters of credit	10-50 %	**553.6**	**110.7**	372.8	74.5	398.2	79.6
		6,739.7	**453.1**	5,016.8	331.8	4,448.3	339.7
Total risk weighted assets		$ **24,808.7**	$ **2,438.5**	$ 22,330.8	$ 2,497.3	$ 19,397.3	$ 2,480.4
Capital base (provincial)			$ **1,306.2**		$ 1,288.7		$ 1,007.0
Provincial capital ratio			**53.6%**		51.6%		40.6%

Provincial Capital Ratio



The provincial capital ratio has increased from 51.6 per cent in 2016 to 53.6 per cent due to a slight increase in capital and decrease in risk weighted assets.

Jump to table of contents

Risk Discussion

Central 1's business operations, industry and environment expose Central 1 to a wide variety of risks, some of which are well known and readily managed and others, such as industry or environment driven risks, that are outside of our immediate control and influence. Central 1's risk management is focused on effectively managing those risks it can control and creating organizational readiness and resilience for those risks it has limited ability to manage. Risk management prioritizes awareness of all the risks it faces and, once identified, measuring or assessing and then monitoring its risks. Central 1 also ensures it has the financial strength through its profitability and capital adequacy to support its businesses and its resultant risks.

Central 1 employs a multifaceted risk management framework designed in keeping with the organization's business operations and role in the credit union network, its operational capabilities and its designation by FICOM as a D-SIFI. Our risk management framework provides independent risk oversight across for Central 1 and its capabilities consider risk across the credit union network.

The risk management framework is founded on several key principles:

1. Central 1 takes business-related risks necessary to execute its strategy:
    - recognizes and accepts that there are risks inherent in providing core services to its members
    - ensures that business strategies generate a level of value commensurate with its respective risk profile
    - does not take speculative risks
2. Central 1 only takes risks that it understands and can manage:
    - clearly identifies, openly discusses, and explicitly accepts the risks inherent in its businesses
    - uses the most appropriate tools, methodologies, and governance structures to manage its risks
    - establishes clear boundaries around its risk profile and continuously supports them with adequate levels of capital and liquidity
3. Central 1 takes and manages risk in a way that maximizes good outcomes for the credit union network:
    - tailors its risk management approach to facilitate innovation and to allow members' needs to be met swiftly and nimbly
    - as a D-SIFI, Central 1 considers, manages, and places risk in the best interests of the credit union network
    - does not take risks that expose the financial strength or the reputation of the network to critical or incapacitating harm

Business and Operations Risks

As noted in the Business Profile, Central 1's business involves centralized liquidity, funding, treasury and portfolio management services, forward thinking technology and payment settlement services and other innovative services and solutions aimed at providing a competitive edge to member credit unions and other corporate clients. These business activities involve inherent risks arising from day-to-day activities and systemic and strategic risks arising from the highly competitive and constantly evolving financial sector. These risks are identified in this section and further discussed in the following sections.

Systemic risk is the risk that the financial system as a whole may not withstand the effects of a crisis resulting from extraordinary economic, political, social or financial circumstances. This risk is inherent for a large, highly interconnected and mutually dependent system such as the financial sector. This risk could result in financial, reputation or other losses and is the risk that Central 1 is least able to materially affect or influence.

Strategic risk is the potential for gaining or losing value related to making and executing strategic business decisions in response to changes of the business environment. Central 1 has control over its strategic decisions and decision processes, but does not always have clear insight into competitive pressures and/

or emerging industry and competitive threats. Central 1 is also part of a network of credit unions and support organizations and its strategy needs to be created and managed within this dynamic network.

Compliance risk is the potential for legal or regulatory sanctions, material financial loss or damage to Central 1's reputation resulting from failure to comply with applicable laws, regulations, rules, related self-regulatory organization standards and/or codes of conduct applicable to its activities. Central 1's objective is to adhere to all legislative and regulatory requirements and actively monitor the ongoing changes arising in these areas. Central 1 actively manages its risk arising from existing and clearly signaled legislative and regulatory requirements, but cannot as readily manage requirements under emerging legislation and regulation given time frames for implementation and compliance.

Operational risk is the potential for loss of value caused by people, processes, systems, or external events. An ongoing but evolving concern for Central 1 is cyber security, which focuses on the protection of the confidentiality, integrity and availability of information systems from both internal and external forces. Central 1 has implemented strong monitoring and control frameworks around the internal elements of this risk and has implemented business continuity and recovery plans based on potential external events.

Credit risk is the potential for incurring financial loss/opportunity cost resulting from the default or failure of a borrower, endorser, guarantor or issuer to repay their financial obligation as they come due. Central 1's capabilities in the measurement of credit risk are strong and include due diligence, expected loss calculation, risk rating models and strict limit monitoring.

Counterparty risk is the potential for financial loss resulting from the inability of a counterparty in a value-exchange transaction (e.g., interest rate swap, foreign exchange deal) to fulfill its obligations. Central 1 has developed potential future exposure modeling to complement existing capabilities around counterparty risk.

Insurance risk is the potential for financial loss or loss to Central 1's reputation resulting from an inability to fully meet the obligations arising from offering insurance. This can result from higher than expected claims frequency, claim amounts and administration costs. Central 1 is exposed to insurance risk through the activities of its subsidiary, CUPP Services Ltd. Central 1 manages its exposure to insurance risk by imposing underwriting limits and robust monitoring.

Liquidity risk is the potential for financial loss resulting from the inability to meet cash flow obligations in a timely manner due to an inability to generate sufficient cash from assets or funding sources. Central 1 also provides liquidity support to the credit union network in B.C. and Ontario and considers the liquidity and funding risks for each of its member credit unions as part of Central 1's risk.

Market risk is the potential for financial gain or loss resulting from favorable or unfavorable movements in interest rates, exchange rates and asset prices/yields. Central 1 uses Value-at-Risk (VaR), duration and stress scenarios among other risk measures to monitor and report on market risk.

These risks are not managed as standalone elements but within ongoing business and operations management. In addition, the Risk Group monitors all risk activities and exposures, including risk transfers, migrations and transformations, as well as risk diversification and amplification.

Risk Management Framework

The risk management framework consists of a strong governance framework including Board and management risk committees, risk policies, management standards and procedures, clear authorities and responsibilities, effective control and oversight functions with clear and independent reporting lines and risk education on key topics.

The Board and its Committees

Board of Directors		
Risk Review and Investment & Loan Committee	Audit and Finance Committee	Technology Committee

The Board reviews and approves material business strategies and activities. Subject to Central 1's Constitution and Rules (Rules) and applicable legislation, the Board may delegate certain duties to committees of the Board. The Board has delegated to the Risk Review and Investment & Loan Committee (RRILC) the responsibility for overseeing the risk-taking operations and risk management functions of Central 1 and ensuring appropriate risk governance processes are executed effectively and that investment, lending and other business operations of Central 1 are undertaken in a prudent and risk-informed manner. The Board has the overall responsibility for Central 1's business conduct. It is responsible for supervising the management of the affairs and business of Central 1 in accordance with Central 1's Rules and applicable legislation and regulations.

The RRILC reviews the risk, investment and lending activities of Central 1, the associated corporate policies and any significant and emerging events and related action plans, and recommends any improvements or changes to the Board as

Jump to table of contents

deemed necessary or desirable. The RRILC also monitors and oversees compliance with anti-money laundering and counter terrorism financing (AML/CTF) legislation and related policies.

The Audit and Finance Committee (AFC) has responsibility for oversight over the financial reporting process. The AFC's purpose is to review:

1. The integrity of Central 1's financial statements;
2. The external auditors' qualifications and independence;
3. The performance of Central 1's internal audit function and external auditors;
4. The adequacy and effectiveness of internal controls; and
5. Central 1's compliance with legal and regulatory requirements affecting financial reporting.

The AFC derives its authority from the Board and Article 14A, Rule 6 of Central 1's Rules. For the purposes of performing its duties, the AFC has the right to inspect the books and records of Central 1 and its subsidiaries, and to discuss with management, the officers, and external and internal auditors such information and matters pertaining to the financial reporting of Central 1, as it deems necessary.

The Chairs of the AFC and the RRILC are members of both committees as mandated by the committees' terms of reference.

The Technology Committee has oversight over all information technology and major project risks at Central 1.

Management and its Risk Committees

The President and Chief Executive Officer (CEO) provides overall leadership and vision in developing, together with Central 1's Board, Central 1's strategic direction, vision, mission, goals and the business plans necessary to realize Central 1's goals. The incumbent is accountable to Central 1's Class A members, through the Board, for providing value generating services to its members, earning a sustainable economic return and for creating an organization focused on strengthening its members and the credit union network. The President and CEO is responsible for the overall Central 1 risk profile and creating a culture of ethical business conduct and prudent risk management.

Central 1's business lines are overseen by key members of Central 1's executive management. The Chief Investment Officer (CIO) is responsible for the management of Central 1's MLP and WFS, including a variety of investment and funding programs to meet the differing needs of Central 1's members and clients, and the Chief Technology and Payments Officer (currently vacant and managed by an Interim Vice President, Digital and Payment Services) is responsible for the management of the Digital & Payment Services to members credit unions and other corporate clients.

The Chief Risk Officer (CRO) is responsible for:

- Overseeing Central 1's independent Risk Group
- Monitoring and reporting on adherence to and consistency of strategic initiatives with the Board-approved risk appetite framework, risk tolerances, and risk profile
- Implementing and maintaining a sound enterprise-wide, integrated risk governance framework
- Overseeing and managing AML/CTF control activity in all relevant business areas of Central 1 for the purposes of establishing a reasonable threshold level of control consistency

The CRO develops, implements and oversees a comprehensive process for assessing, identifying, monitoring and effectively managing pertinent business risks that could interfere with Central 1's core purpose and ability to grow and develop its business lines for the benefit of the credit union network.

The CRO reports to the President and CEO and has direct access to the RRILC.

The Chief Financial Officer (CFO) is responsible for all aspects of Central 1's financial management, accounting and compliance with financial reporting requirements. Operating areas include external financial reporting and regulatory filings, financial planning and budgeting, internal management accounting, and treasury back-office operations. The CFO plays a key role in the overall risk management framework.

Jump to table of contents

The CFO reports to the President and CEO and has direct access to the Chairperson of the AFC.

Internal Audit's objective is to enhance and protect organizational value by providing risk-based and objective assurance, advice and insight. Central 1's internal audit function is independent of management and the Risk Group. Internal Audit develops audit plans for approval by and reports independently to the AFC of Central 1's Board on the design and effectiveness of policies, procedures and internal controls.

Corporate Policy Coverage
Central 1's risk policy framework outlines the roles and responsibilities of the business and operations functions, Risk Group and corporate support groups in the effective creation, approval, maintenance and communication of corporate risk policies as well as management risk standards.

Risk policies that cover risk identification, measurement, management and reporting are set by the Risk Group and are considered minimum requirements for the business and operations functions and the other support and control functions. These policies communicate Central 1's risk appetite, limits and parameters within which business groups and employees can operate. All risk policies are subject to a rigorous approval process which, depending on the type and significance of the policy, can involve different management risk committees, the RRILC and, for all Corporate Policies, the Board.

Central 1's risk policy framework includes the organization's Risk Appetite Framework and Risk Appetite Statement (RAS), which defines the types and amounts of risk that Central 1 is willing to take in pursuit of its strategic objectives. The RAS covers all of Central 1's main risk categories, including Compliance Risk, Credit Risk, Counterparty Risk, Liquidity Risk, Market Risk, Operational Risk and Strategic Risk.

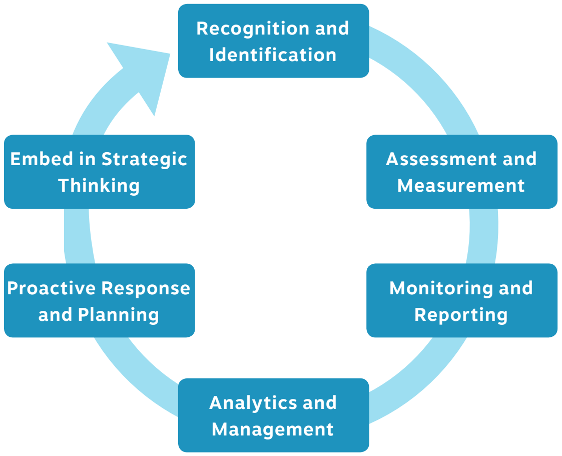
The policy framework provides clear authorities and responsibilities for all functions and creates effective control and oversight functions with clear and independent reporting lines. Central 1 operates a dual stream adjudication process, whereby all risk exposures are recommended by the business and concurred with by the Risk Group. This ensures that any potential risk exposure both supports business objectives and is independently reviewed.

Central 1's risk policy framework establishes definitions for the common risk terms used by line management, risk oversight functions and support functions at Central 1 including:

- Risk and risk management
- Risk categories, sub-categories, and risk drivers
- Common risk terms
- Risk impacts
- Risk misnomers

Central 1 undertakes rigorous risk education on several key topics. All Central 1 staff are required to complete information security training as part of the employee onboarding process. All staff involved with funds flows, whether deposit, loan or payments flows, must complete annual AML/CTF training. Central 1 has a business continuity plan (BCP) and all employees with planning and/or resolution responsibilities must complete annual BCP training.

Risk Management Process
Central 1's Corporate Risk Management Policy outlines the organization's risk process and this is summarized below. The process is based on six related and reinforcing steps, as follows:



Recognition and Identification involves the detection and description of risks that could compromise the ability of Central 1 to achieve its business objectives, and the disciplined analysis of those risks in order to determine their potential to affect, individually or collectively, business objectives.

Assessment and Measurement starts with an evaluation of identified risks to determine their potential to affect, individually or collectively, business objectives. Appropriate methodologies and models to determine the quantum or magnitude of a particular risk are developed and then implemented to measure that risk. Wherever possible, such measurement is expressed in terms of potential impact on earnings, value, and/or capital. All Central 1 exposures are measured for both normal market conditions and stressed conditions. Stress testing is a core element in Central 1's approach to risk measurement and management.

Jump to table of contents

Monitoring and Reporting involves the qualitative and quantitative measurement of Central 1's risk profile against approved limits, the tracking of identified risk issues, the reporting of risk at varying levels of aggregation to Central 1's management, RRILC, and the Board, and the escalation of risk exposures to the appropriate level of the organization for discussion and action. Monitoring and reporting must be time-effective to inform and support effective management action, with the appropriate frequency determined by the nature of both the business activity and the risk being measured.

Analytics and Management is the transformation of measured risk data into business-actionable risk information through the application of quantitative modelling and methodologies, as well as skilled judgment and qualitative interpretation. It includes trend identification and analysis, detection of correlations and amplifications, recognition of concentrations, and assessment of the organization's capabilities. While necessarily based on past risk data, analytics and management looks forward to predict possible future states and inform future management actions.

Proactive Response and Planning entails management action informed by business-actionable risk information. It includes both reactive measures to ensure Central 1's risk profile stays within the organization's risk appetite, and identifying forward-looking, longer term tactical plans aimed at maximizing value for Central 1, again while staying within the organization's risk appetite. Management options include avoiding risk, reducing risk, accepting or maintaining risk, or increasing risk. Central 1's contingency and crisis management plans fit within this process element.

Embed in Strategic Thinking involves incorporating consideration of Central 1's actual and desired risk profile within the organization's strategic planning process. It includes making strategic choices at the business and enterprise levels based on an assessment of options that is informed by risk information. Central 1 considers the risk implications in all of its strategic and day-to-day tactical decisions.

Risk Oversight and Management

Central 1's approach to managing and mitigating specific types of risk is as follows:

Strategic Risk

Central 1 believes that pressures on all financial institutions including credit unions, from, among other things, tight margins and financial technology disruption characterize the current environment. Central 1 needs to be prepared to respond to the resulting changes and opportunities. Central 1 relies on the underlying network's direction, ongoing member and client engagement and a continuous strategic planning process to pursue a strategy that prepares it for the risks inherent in the environment and to deliver value for credit unions and clients.

Compliance Risk

Central 1 is exposed to compliance risk in all areas of the organization, ranging from legislative and regulatory requirements enforced as a result of the products and services offered by the various business lines, and through the oversight and regulatory reporting obligations placed upon corporate control and support functions. Compliance risk is managed by a framework that is in place to ensure that Central 1 continues to meet the requirements of:

- The law, to uphold its reputation and that of the credit union network
- Government regulators, to be allowed to continue to do business
- Financial network counterparties, to be able to provide products and services to the credit union network
- Internal policies, management standards, and procedures, to help ensure a strong and efficient governance structure

Central 1's compliance risk framework includes policies, management standards, and operational procedures, as well as risk assessments, monitoring and reporting processes, and relevant training. Specifically:

- The onus is placed on each business line or functional area to manage the compliance risk arising from its day-to-day operations. At this level, risk management is accomplished through a combination of ongoing training and development and documentation of operational procedures, as well as regular risk assessments that are reported as necessary to compliance.
- Compliance provides guidance to the business line or functional area, and assesses, monitors, and regularly reports upon the compliance levels within Central 1 to the CRO and, through the CRO, to the RRILC of the Board.

Counterparty Risk

Within the Treasury and Digital & Payment Services operations, Central 1 incurs counterparty risk through entering into contracts with counterparties in return for a bilateral value-exchange of services. The counterparty risk is managed within the same adjudication process as credit risk. Counterparty risk is currently assessed as low given the quality of counterparties being government entities, credit unions and banks with high external credit ratings AA-low to AAA DBRS.

Credit Risk

Within the Treasury and Digital & Payment Services operations, Central 1 incurs credit risk through loans, payment services and the purchasing of credit instruments.

Central 1's policies establish the parameters within which the organization manages its credit risk. These policies are implemented through a number of key business procedures. Together, the policies and procedures form a framework that includes:

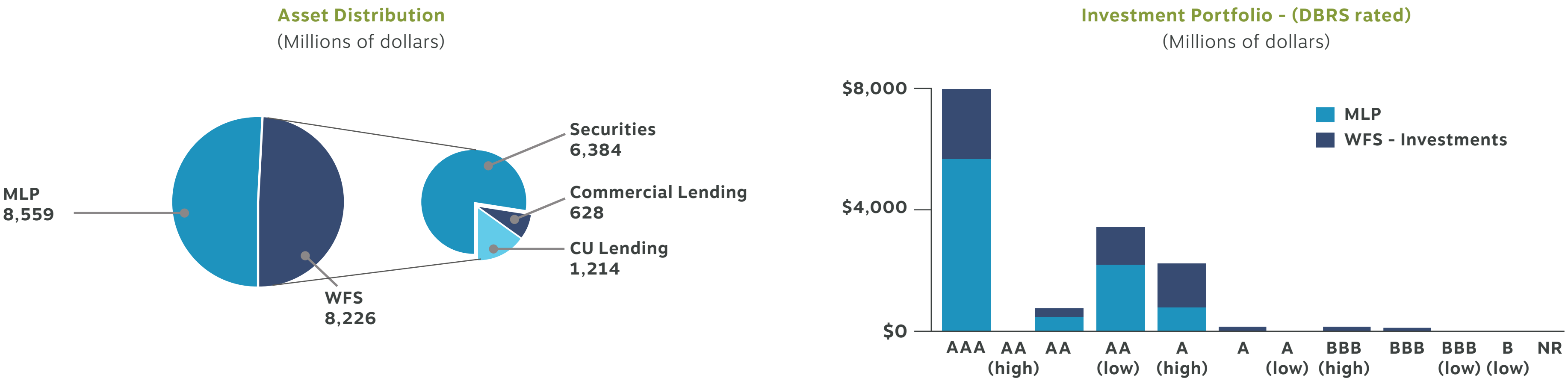
- Application of safe and sound, stringent lending and/or funding criteria to all credit exposures prior to their acquisition
- Clearly defined management and policy limits on the amount, types, and concentrations of credit risk
- Regular evaluation and assessment of existing credit risk exposures and allowances
- Continuous monitoring of credit exposures so as to promptly identify deteriorating situations and take appropriate action

All potential and existing borrowers are evaluated by skilled lenders and are adjudicated by independent, highly trained credit officers. Annually, the status of each borrower and transaction is reviewed in the same manner as a new proposal.

The exposures are concentrated in low-risk investment securities with very limited exposure to underperforming loans in the lending portfolios.

The following figure illustrates Central 1's credit exposure and risk profile based on outstanding balances in the investment portfolios held in the MLP and WFS. WFS holds $0.3 billion in A rated and below exposures.

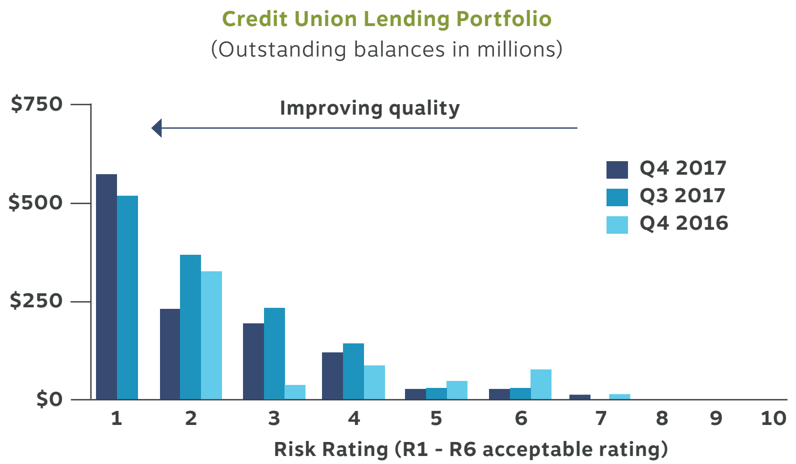
Figure 19 - Credit Exposure by Portfolio and Rating

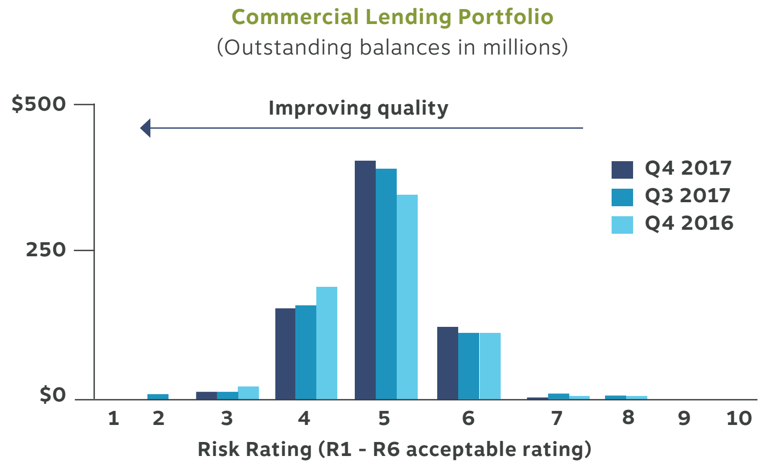


Credit risk associated with Central 1's credit union lending portfolio has been assessed by management as low. The risk associated with the commercial loan syndication program is currently assessed by management as low.

The following figure provides the year-end exposure in the Commercial Lending and Credit Union Lending Portfolios.

Figure 20 – Portfolio Exposures by Risk Rating



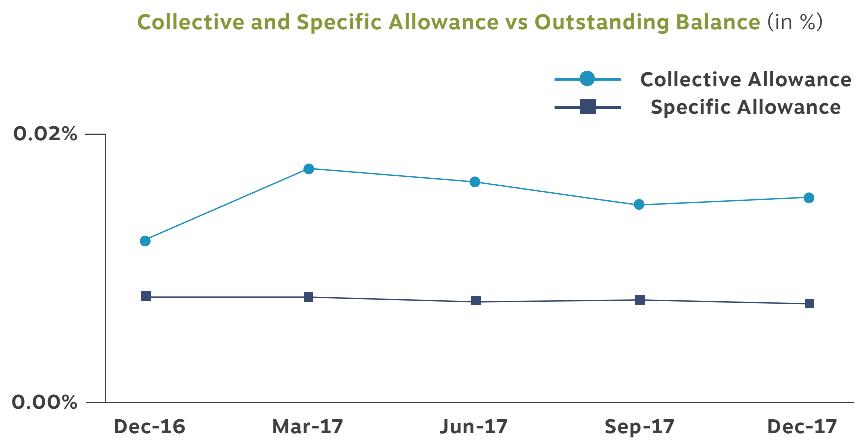


Credit Quality Performance - Commercial Lending Portfolio

No loans in the Commercial Lending Portfolio were written off in 2017. Currently there are no impaired loans in the portfolio. Watch List accounts represent 0.5 per cent of the outstanding portfolio balance as at December 31, 2017.

The following figure provides a summary of Allowances for Credit Losses for Commercial Lending.

Figure 21 – Allowances for Credit Losses – Commercial Lending



Jump to table of contents

Credit Quality Performance - Credit Union Lending Portfolio
No loans in the Credit Union Lending Portfolio were written off in 2017. Currently, there are no impaired loan facilities in the Credit Union Lending Portfolio. While there are no impaired facilities in the portfolio, a number of credit unions have been placed on the Watch List. As at December 31, 2017 there were six Ontario and three B.C. credit unions classified as Watch List, with the total balance of $7.7 million representing 0.63 per cent of the outstanding portfolio balance. The security provided for the Watch List facilities is substantial and no losses are expected.

Credit Quality Performance - Investments Portfolio
Central 1 has an impaired investment related to an Asset-Backed Commercial Paper exposure. Central 1 continues to receive cash flows on the underlying assets. Specific allowances for the impaired investment as at December 31, 2017 were $0.4 million.

As part of its ongoing risk management activities, Central 1 performs ongoing stress tests to measure the resiliency of its credit portfolios against a range of severe scenarios. The stress tests provide comfort that Central 1 continues to maintain adequate capital to withstand a range of severe economic scenarios.

Insurance Risk

Central 1 is exposed to insurance risk through the activities of its subsidiary, CUPP Services Ltd. Central 1 manages its exposure to insurance risk by imposing underwriting limits and undertaking robust monitoring.

Liquidity Risk

Liquidity risk is the potential inability to meet cash flow obligations in a timely manner, because Central 1 is either unable to sell securities at a desired market price or unable to secure the funds needed to meet its obligations when due. Liquidity events can be caused by an internal mismatch between the cash flows of Central 1's assets and liabilities, external idiosyncratic or systemic market and credit events or unexpected changes in the liquidity needs of Central 1's members. Sound liquidity management by Central 1 ensures the safety of credit union members' deposits and the health of credit union network.

Central 1's mandate includes the management of credit union members' access to liquidity in B.C. and Ontario. Credit unions are required to hold (by regulation in B.C. and by contractual agreement in Ontario) their core liquidity reserves in the MLP. Board, management and regulatory guidelines ensure that deposits are supported by highly liquid assets. These assets are held to provide liquidity to credit unions in the event of a liquidity crisis.

Central 1's WFS business line provides capital markets products and services to Class A, B and C members. Product offerings include current accounts, term deposits, credit union lending, commercial lending, access to securitization vehicles, foreign exchange services, and derivatives. WFS is funded through members' discretionary deposits and capital markets under Central 1's commercial paper and medium-term note programs.

Central 1 provides payment clearing and settlement services to Class A, B and C members. Central 1 manages the Group Clearer function on behalf of the credit union network nationally (excluding Quebec) and is a direct clearer through the Payments Canada network. Central 1 provides access to global correspondent banks for the credit union network to settle foreign currency payments. These activities directly expose Central 1 to credit and liquidity risk from other direct participants in the payments network. The credit and liquidity risk of these core banking functions are managed within WFS.

Central 1 has established a comprehensive liquidity risk framework that is comprised of:

- A robust risk governance framework
- Investment strategies focused on maintaining sufficient unencumbered highly liquid assets to meet cash flow requirements in normal and stressed conditions
- Access to diversified funding sources – member deposits and capital markets
- Monitoring of credit union network liquidity, performance and financial health
- An enterprise Contingency Funding Plan (CFP)
- Frequent measurement of portfolio liquidity

Investment Strategies
Central 1 invests in a sufficient quantity of highly liquid assets to ensure that it can meet the deposit withdrawal and borrowing requirements of its member in normal and stressed market environments. Central 1 views the following assets as highly liquid and includes them in management's assessment of portfolio liquidity:

1. GOC securities, GOC guaranteed securities (including NHA MBS and CMB), Canadian provincial and municipal governments securities and other high quality government assets meeting OSFI's definition of HQLA.
2. Other securities eligible to be pledged to the BOC in the form of financial institution and investment grade corporate debt (collectively other BOC Standing Liquidity Fund (SLF) eligible assets).
3. USD denominated variants of the securities identified in groups (1) and (2) above.

MLP deposits are backed entirely by assets in one of the three categories above. USD denominated debt is matched against the USD denominated deposits to ensure that exposure to foreign currency market risk is mitigated. MLP assets are not currently used to meet derivative and clearing and settlement collateral requirements; consequently, the portfolio is 100 per cent unencumbered.

WFS liquidity management is more complex than for MLP and, consequently, it is subject to a more rigorous measurement and monitoring regime. A portion of WFS liabilities is invested in HQLA as defined above, sufficient to ensure the portfolio's liquidity objectives are met. These liabilities are also invested in credit union and commercial loans and residential mortgages. As part of its normal business operations, Central 1 makes commitments to grant loans to credit unions and commercial borrowers, enters into derivatives and securities lending transactions, and is a participant in the national clearing and settlements network. Central 1 encumbers a portion of WFS' highly liquid assets to support these activities. Asset encumbrances are closely monitored, limited to 20.0 per cent of the portfolio and excluded from liquidity measures as they are not available to support payment obligations.

Diversification of Funding

Central 1's liquidity management framework is designed to ensure that reliable and cost-effective funding sources are available to satisfy current and prospective commitments of Central 1 and its member credit unions. Diversification of funding sources provides flexibility and minimizes concentration risk. It is a crucial component of Central 1's overall liquidity management strategy.

The MLP is funded primarily through Class A member statutory (for B.C.) or contractual (for Ontario) deposits.

WFS is funded through a combination of Class A, B and C member deposits and capital markets borrowing. Central 1 regularly issues commercial paper and medium-term notes in the capital markets. Central 1 also issues subordinated debt. Regular participation in these markets and the maintenance of a strong external credit rating is critical for ensuring that capital markets access is maintained. Central 1 funds a portion of its purchases of residential mortgages and credit union NHA MBS through the NHA MBS and CMB mortgage securitization programs.

Credit Union Network Health Analysis

Central 1's liquidity is directly affected by the liquidity of the B.C. and Ontario credit union networks and the liquidity of its Class B and C members. Central 1 closely monitors credit unions' financial positions for any indication of negative liquidity trends. Utilization of lending facilities, liquidity ratios, deposit levels, economic conditions, and use of capital market and other funding sources are among the items regularly monitored.

Contingency Funding Plan

Central 1 provides financial stewardship of the liquidity deposits of the B.C. and Ontario credit union networks. Accordingly, it is imperative that Central 1 maintain members' trust and confidence by ensuring the existence of an appropriate plan to provide the credit union network with access to funding during a liquidity crisis.

Given that a Central 1 liquidity crisis would likely be the result of a liquidity event that flows through the credit union network, Central 1 continually monitors the network and its environment for indicators of impending stress. Although there is a low probability of a significant liquidity crisis occurring, Central 1 monitors the risk and has implemented a CFP should such a crisis occur.

Risk Monitoring

Central 1 monitors its asset and liability positions, encumbrances, commitments, cash flows and funding to better understand its liquidity capacity and its sensitivity to changing market conditions. Central 1 includes the following types of assets in its liquidity measures (including Liquidity Coverage Ratios) as highly liquid assets:

- **HQLA 1.** Assets issued by the GOC, provincial governments and securities secured by GOC as defined by OSFI
- **HQLA 2.** Investment grade corporate, covered debt and residential mortgage-backed securities (RMBS) as defined by OSFI
- **Other SLF Eligible.** Securities eligible to be pledged to the BOC in the form of financial institution and investment grade corporate debt (collectively other BOC SLF eligible assets) not included in HQLA 1 or 2; and USD denominated variants of the securities identified in groups above (per agreement with FICOM)

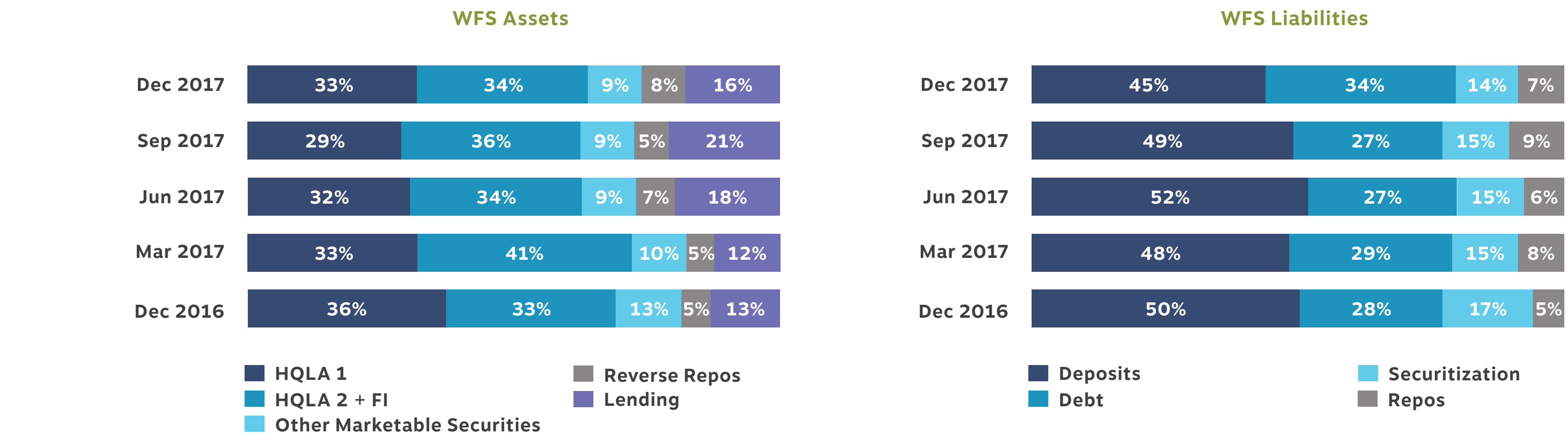
In the MLP investment strategy, limits and regulations ensure that MLP deposits are entirely covered by HQLA 1, HQLA 2 and Other SLF Eligible assets. Note that the nominal amount of other assets relates to tax and other accounting based non-marketable assets. Since the entire portfolio is highly liquid and eligible to be pledged to the BOC SLF, management is confident that the portfolio can be converted to cash through sale, repurchase agreement or pledging to the BOC to meet member needs in a liquidity stress event.

The majority of assets in the WFS is highly liquid and can be readily sold or pledged to the BOC to generate cash to support member deposit withdrawals or the drawdown of committed loan facilities in both normal and stressed markets. While WFS holds other less liquid assets, the quantity of highly liquid assets is greater than the level of funding provided by member deposits.

Jump to table of contents

The following figure illustrates the relationship between assets and liabilities.

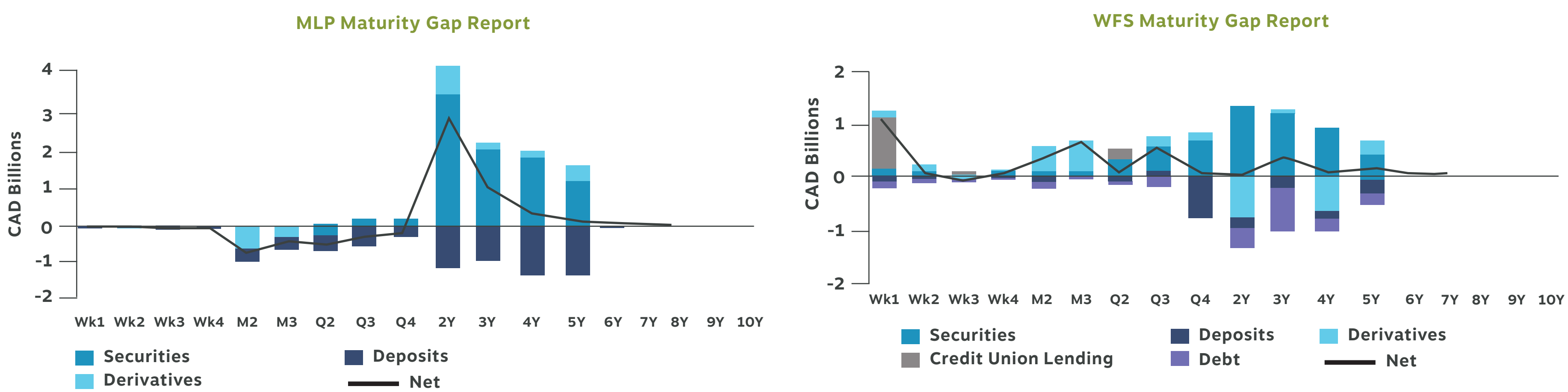
Figure 22 – Asset and Liability Allocations



The Maturity Gap provides a picture of the mismatch between the contractual maturity of Central 1's asset and liabilities. These gaps, even under normal market conditions, must be closed by Central 1 receiving additional funding or liquidating assets. Under normal market conditions, the MLP maturity gaps are generally funded by members rolling over or renewing their mandatory or contractual deposits as, typically, credit union deposits are growing. The maturity gaps reported for WFS are within normal levels.

The following figure shows the Maturity Gap for MLP and WFS.

Figure 23 - Asset and Liability Allocations



The Liquidity Coverage Ratio (LCR) measures whether Central 1 has sufficient unencumbered highly liquid assets to cover its cash flow obligations over a 30-day horizon under a stressed deposit withdrawal scenario. For the MLP, management currently assumes a 100 per cent drawdown of member deposits. For WFS, the standard OSFI deposit drawdown assumptions are used. Targets for MLP and WFS are set at 100 per cent for the LCR.

The following table shows that the LCR remains stable for both MLP and WFS on a quarter-over-quarter basis, and above the 100 per cent target set for the WFS. LCR for WFS was 174.7 per cent while MLP was 105.7 per cent for the quarter ended December 31, 2017. The ratios for both WFS and MLP show a satisfying level of liquid assets are maintained for adequate coverage of the short-term cash outflows.

Figure 24 – Liquidity Coverage Ratio

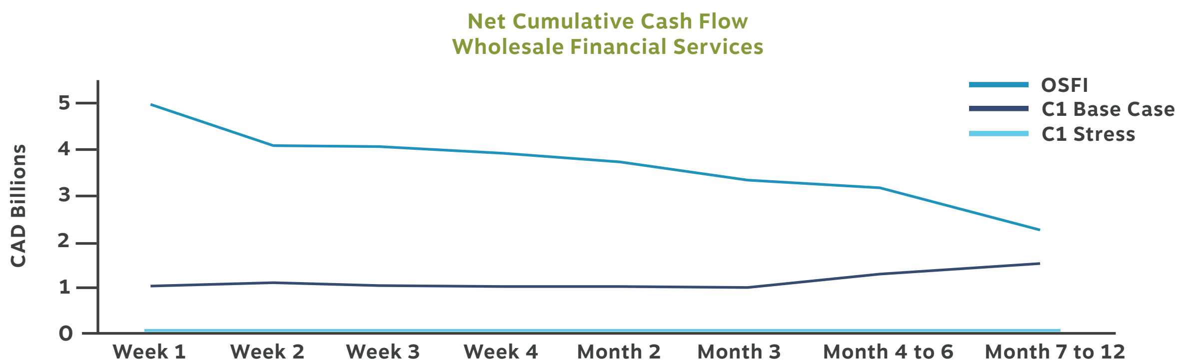
Liquidity coverage ratio	Dec 2017	Average	Max	Min	Dec 2016
Mandatory Liquidity Pool	105.7%	105.3%	106.9%	103.0%	104.5%
Wholesale Financial Services	174.7%	180.7%	230.2%	134.6%	169.8%

Net Cumulative Cash Flow (NCCF) measures whether assets are of sufficient quality and quantity to support a prolonged drawdown of deposits and drawdown of committed lending facilities with limited access to capital market funding. Central 1 assesses NCCF measures under three scenarios:

- **OSFI Scenario.** OSFI guidelines for the NCCF test presumes that all assets are liquidated in week one and tests whether the cash generated is sufficient to fund obligations for 12 months
- **Central 1's Base Case Scenario.** The base case assumes no deposit withdrawal and the renewal of all maturing loans and debt issuances.
- **Central 1's Severe Stress Scenario.** The stress scenario assumes that the largest B.C. and Ontario credit unions withdraw all deposits and draw down on committed loan facilities. The scenario assumes no access to capital markets and that funding is obtained by gradual liquidation of assets.

The following figure illustrates WFS' ability to meet deposits withdrawals under three scenarios. A non-negative cash flow in each period indicates a positive outcome of the test.

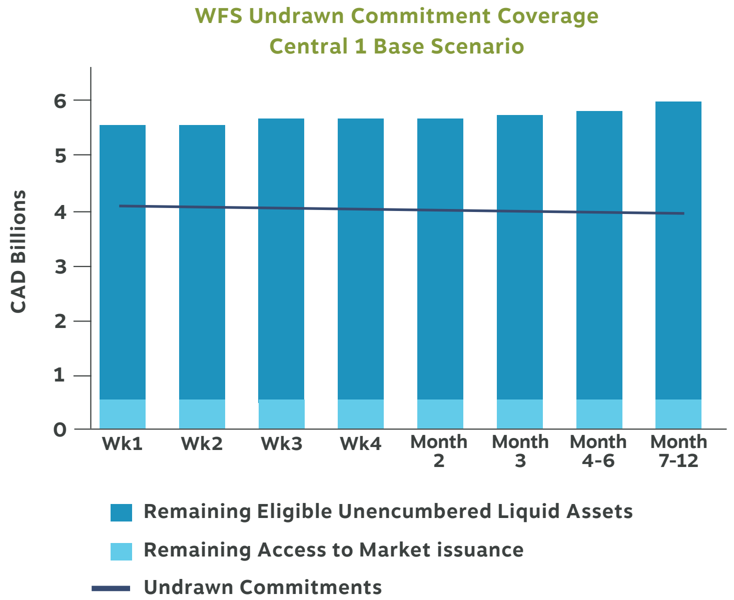
Figure 25 - Net Cumulative Cashflow

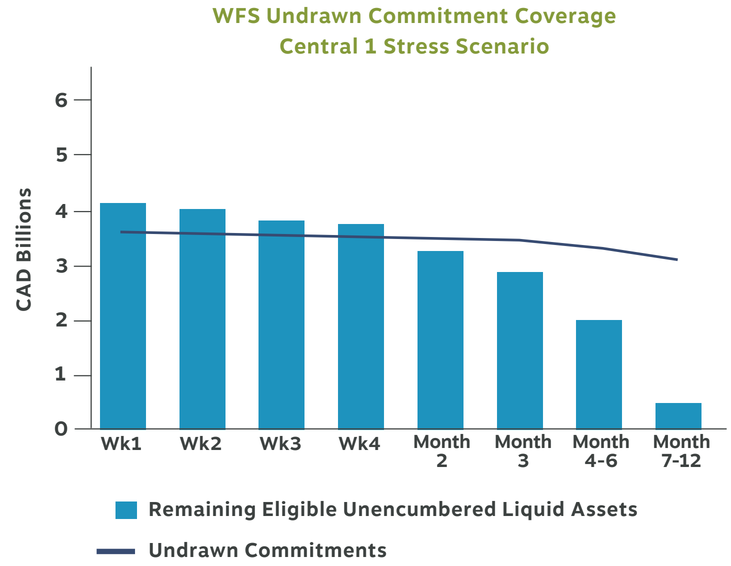


The following figure illustrates WFS portfolios' ability to cover undrawn lending commitments under the base case (business as usual) and a severe stress scenario. Under the base scenario, undrawn lending commitments can be met with the sale of assets. In the severe stress scenario, lending commitments can be covered from asset sales through month three, but access to capital markets would be required to cover 100 per cent of undrawn commitments in months four through 12.

Jump to table of contents

Figure 26 – Undrawn Commitment Coverage





FICOM performed a Supervisory Review of Central 1's Liquidity Management in 2016. Amongst a few recommendations, Central 1 has augmented its existing stress tests to include the following scenarios:

- Default of the largest non-credit union system and non-governmental counterparty
- Drawdown of committed facilities and deposits of the largest and three largest credit unions

The stress testing assesses the adequate stock of unencumbered liquid assets to meet Central 1's liquidity needs for 30 calendar days under different liquidity stress scenarios (LCR Based). Central 1 has met the expectations of these stress test consistently throughout 2017.

Market Risk

The level of market risk to which Central 1 is exposed varies depending on market conditions, future price and market movements and the composition of Central 1's investment, lending and derivative portfolios.

Central 1 manages its exposure to market risk through a range of governance and management processes. Central 1's policies detail the measurement of market risk and establish exposure limits in keeping with Central 1's overall risk appetite. Central 1 independently monitors exposure against limits, investigates any breaches and reports them at the appropriate level for review and action. This management framework is complemented by a series of rigorous stress test scenarios that are run on a regular basis.

Central 1 will not incur market risk for speculative purposes or in pursuit of returns beyond those required to reasonably fulfill its primary mandate of safeguarding network liquidity.

Value-at-Risk

Central 1 regularly monitors its exposure to market risk. Central 1 has established separate market risk appetite limits for the MLP and WFS. The current limits approved by the Board are set at 10 bps or 0.10 percent of MLP asset market value and 11 bps or 0.11 percent of WFS asset market value. As of quarter end, the limits were $8.4 million for MLP and $9.0 million for WFS. Central 1 complied with MLP and WFS limits during fourth quarter.

Note 31 to the Consolidated Financial Statements provides additional information on the fair value of financial assets and liabilities compared to their carrying value.

The following tables summarizes Central 1's VaR for MLP and WFS.

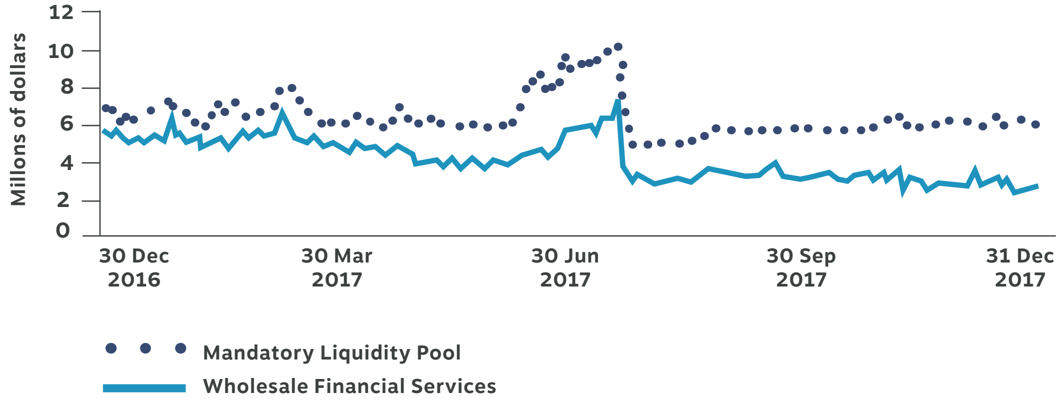
Figure 27 - VaR by Risk Type

	Mandatory Liquidity Pool					
				2017		
Millions of dollars	Q4 2017	Q3 2017	Q4 2016	Average	High	Low
Interest Rate VaR	$ 5.1	$ 4.5	$ 7.0	$ 6.2	$ 10.3	$ 3.7
Credit Spread VaR	4.8	5.0	3.1	3.9	5.1	2.0
Foreign Exchange VaR	0.1	0.1	0.8	0.1	0.8	0.0
Diversification[1]	(4.2)	(3.9)	(4.6)	nm	nm	nm
Total VaR	$ 5.8	$ 5.7	$ 6.3	$ 6.2	$ 10.0	$ 4.7

	Wholesale Financial Services					
				2017		
Millions of dollars	Q4 2017	Q3 2017	Q4 2016	Average	High	Low
Interest Rate VaR	$ 1.6	$ 1.9	$ 5.5	$ 3.2	$ 5.9	$ 1.5
Credit Spread VaR	1.3	1.3	1.8	1.5	2.1	1.1
Foreign Exchange VaR	2.1	2.2	2.9	2.0	3.4	0.8
Diversification[1]	(2.4)	(2.2)	(4.5)	nm	nm	nm
Total VaR	$ 2.6	$ 3.2	$ 5.7	$ 4.0	$ 7.1	$ 2.3

[1]Total VaR is less than the sum of Risk Factors' VaR as a result of diversification and offsetting risk factors.
nm - Not meaningful to calculation

Figure 28 - Daily 99% VaR by Business Line



There was a breach on the market risk limit in MLP on July 19, 2017. Specifically, the reported exposure of $9.96 million exceeded the previous VaR limit of $9.86 million. This was deemed to be a technical breach and modified VaR calculations and limits were introduced on July 20, 2017 to address the issues. The new VaR methodology more accurately represents risk exposure.

Stress Testing

VaR Stress Testing allows us to test the performance of the portfolio in different market environments. Stress tests are measured using a 10-day 99 per cent VaR.

Stress tests are conducted over three historical periods:

- Pre-Lehman Crisis (October 2006 through December 2007) – widening in short-term spreads and increased volatility in the USD-CAD spot rate
- Lehman Crisis (January 2008 through May 2009) – widening of short-term, corporate, MBS and other yields with high volatility in the USD-CAD rate
- European Crisis (November 2010 through December 2013) – rising short-term spreads and USD-CAD rate volatility

The MLP portfolio is most exposed to market events similar to the Lehman Crisis. This crisis is characterized by the widening of spreads between corporate and government bonds, high volatility in the USD-CAD spot rate and negative real Fed funds rate.

The WFS portfolio is most exposed to market events similar to the Pre-Lehman Crisis. This period is characterized by moderate increases in corporate and bank spreads, declining sovereign and swap rates, and an appreciating Canadian dollar.

The following figure illustrates the stress tests as at December 31, 2017.

Figure 29 - VaR Stress Test

December 31, 2017 (Millions of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services
10 Day VaR	$ 11.2	$ 7.1
Pre-Lehman Crisis (Oct 2006 - Dec 2007)	$ 13.0	$ 11.7
Lehman Crisis (Jan 2008 - May 2009)	$ 25.7	$ 10.9
European Crisis (Nov 2010 - Dec 2013)	$ 21.1	$ 14.8

Direction and Sources of Interest Rate Risk

Central 1 uses a number of secondary market risk measures to help understand the direction and sources of interest rate risk in the MLP and WFS portfolios. DV01 measures the sensitivity of the portfolio to one bp increase in interest rates.

Foreign Exchange Rate Exposure

Central 1 has assets and liabilities denominated in several major currencies and buys foreign currencies from, and sells these currencies to its member credit unions. The risk associated with changing foreign currency values is managed by applying limits on the amounts (short or long positions) that can be maintained in the various currencies, utilizing derivative exchange contracts to lessen the impact of on-balance sheet positions and through VaR management limits. Exposure is concentrated in USD and only a relatively small amount is held in other major currencies.

The following table provides the Foreign Exchange Position as at December 31, 2017.

Figure 30 - Foreign Exchange Position

Currency (Millions of dollars)	Balance Sheet in Native Currency	Off-Balance Sheet Items - FX Forwards	Net Position in Native Currency	BOC Closing Rate	CAD Equivalent
USD	$ (116.8)	$ 133.9	$ 17.1	$ 1.2538	$ 21.4

Note 33 to the Consolidated Financial Statements provides additional information regarding Central 1’s foreign currency exposure.

Operational Risk

Operational risk is measured by referring to organizational and industry loss events combined with estimates of frequency from the historical record and key risk drivers. While the financial impact associated with operational risk can be significant, it is equally important to recognize the less identifiable and quantifiable non-financial impacts. Real or perceived changes in an institution’s credibility can damage its reputation, image, and stakeholder confidence, thereby negatively affecting the institution’s results in the future.

Given the high volume of transactions Central 1 processes on behalf of its members and external organizations, shortcomings in its internal processes could lead to financial and reputational damage. Furthermore, although Central 1 has contingency and business continuity plans, natural disasters, power or telecommunications disruptions, acts of terrorism, physical or electronic break-ins or other events could adversely impact Central 1’s ability to provide services to its members, damage Central 1’s reputation or otherwise adversely impact Central 1’s ability to conduct business.

Central 1 manages this type of risk through implementing policies and associated procedures that are fundamental to its operating infrastructure. Elements include:

- Developing and maintaining a comprehensive system of internal controls encompassing segregation of functional activities, managerial reporting and delegation of authority
- Continuous monitoring, evaluation, and improvement of Central 1's operational practices
- Selection and training of highly qualified staff, supported by policies that provide for skills upgrading, clear authorization levels and adherence to an employee code of conduct
- Maintaining a comprehensive portfolio of insurance to reduce the impact of any potential losses
- Contingency business resumption plans for activation in response to systems failure or catastrophic events, including off-site data storage and back-up processing capabilities for all critical operations

As well as having the above measures in place, Central 1's policies provide for regular, ongoing review of its practices and procedures by internal audit teams, technology systems security personnel and management personnel. External resources, when required, also supplement the internal reviews. In addition, both provincial and federal regulatory agencies undertake periodic reviews of Central 1's operations and contingency plans.

Central 1 continues to experience increasing exposure to technological risk and has implemented real-time intrusion detection monitoring of its remote banking applications and uses an external agency to continuously monitor security performance. Central 1 continues to invest in the infrastructure to successfully defend against a variety of cyber-attacks on behalf of member credit unions, reducing their exposure and the risk of significant negative effects.

Reputation

Central 1 recognizes that its reputation is among its most important assets, and considers reputational impact in all of its business and planning practices. Integrity and ethical conduct are core values for Central 1, and these are fostered at the most fundamental levels of the organization through the adherence of each employee and contractor to Central 1's Code of Conduct. In addition to the key principles listed in the Corporate Risk Management Policy (the Policy), the following specific principles govern Central 1's management of its reputation:

- Central 1 will maintain the highest degree of integrity and ethical conduct at all times. Everything Central 1 does and every decision it makes will be guided by principles of honesty, integrity, respect and ethical standards.
- Central 1 will avoid activities that may harm either Central 1's reputation or the reputation of the credit union network.
- Central 1 will consider the reputational impact on Central 1 of all business activities that it undertakes.

Emerging Risks

Emerging risks are risks that are newly developing or rapidly changing. They are difficult to quantify and may have a major impact on Central 1. They are investigated because of the substantial potential impact on Central 1's business.

Central 1 identifies and assesses emerging risks in various ways, including at the strategic planning and business unit levels. These include risk oversight committee discussions and regular risk reviews to identify, assess and ensure that management is forward-looking in its treatment of emerging risks. Emerging risks are quantified using established techniques where possible or qualitatively assessed on the basis of impact and likelihood.

Accounting and Control Matters

Central 1's 2017 annual Consolidated Financial Statements have been prepared using the same accounting policies as set out in Note 3 to those statements.

Critical Accounting Policies and Estimates

In preparing the Consolidated Financial Statements in accordance with IFRS, management must exercise judgements and make estimates and assumptions that affect the application of accounting policies and the carrying amounts of assets and liabilities, net income and related disclosures. The most significant areas for which management must make subjective or complex estimates and judgements include financial instruments measured at fair value, allowance for credit losses, income taxes and pension and post-retirement benefits. Actual results could differ materially from those estimates. Note 4 to Central 1's 2017 annual Consolidated Financial Statements provides additional details regarding estimates and judgements used by management in preparing these statements.

Future Changes in Accounting Policies

IFRS 9 – Financial Instruments

In July 2014, International Accounting Standards Board (IASB) issued the complete version of IFRS 9, *Financial Instruments*, which will replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 is effective for Central 1 for the annual periods beginning on January 1, 2018 and is to be applied retrospectively with some exemptions. As permitted, Central 1 will not restate the comparative

Jump to table of contents

period financial statements, but instead recognize the transition impact through adjustments to the opening balances of retained earnings and accumulated other comprehensive income as at January 1, 2018.

Implementation approach
Central 1's implementation approach is based on five work streams including Scoping, Analysis, Development, Testing, and Go-live. Central 1's IFRS 9 project has focused on developing accounting policies, assessing business models for the classification and measurement of financial instruments, and developing and validating impairment models to support the IFRS 9 impairment conclusions.

Classification and measurement
Under IFRS 9, financial assets will be classified as amortized cost, fair value through profit or loss (FVTPL), or fair value through other comprehensive income (FVOCI) based on the business model for managing assets and the contractual cash flow characteristics of the financial asset.

Upon transition, the business model assessment will be based on the facts and circumstances as at January 1, 2018. Debt instruments that have contractual cash flows representing solely payments of principal and interest (SPPI) and are managed within a business model that is held-to-collect, are classified as amortized cost. Debt instruments that meet the SPPI test and are managed within a business model that is held-to-collect and for sale, are classified as FVOCI with changes in fair value recognized in other comprehensive income (OCI) until the asset is derecognized, upon which the cumulative gain or loss previously recognized in OCI is reclassified to profit or loss. All other debt instruments will be classified and measured as FVTPL.

Equity instruments would generally be measured at FVTPL unless an irrevocable election is made to classify these instruments at FVOCI which will result in change in fair value recognized in other comprehensive income (OCI) with no subsequent impact to profit or loss upon the sale of the instruments.

The classification and measurement of financial liabilities remain essentially unchanged under IFRS 9 except for financial liabilities designated as FVTPL. Once the designation is made, changes in the fair value attributable to an entity's own credit risk should generally be recognized in other comprehensive income without subsequent reclassification in profit or loss.

Impairment
IFRS 9 introduces a new expected credit loss (ECL) model applicable for all debt instruments financial assets classified as amortized cost or FVOCI, as well as certain off-balance sheet loan commitments and financial guarantees. Compared to the current incurred loss model under IAS 39, Financial Instruments: Recognition and Measurement, the new ECL will result in an allowance for credit losses being recorded regardless of whether there has been an actual loss event. For financial assets that are credit impaired or have experienced a significant increase in credit risk, the loss allowance is recognized based on expected credit losses that result from possible default events over the expected lifetime (lifetime ECL). The loss allowance for all other financial assets are recognized based on the expected credit losses that result from possible default events within twelve months of the reporting date (twelve months ECL).

The definition of credit impaired is similar to an incurred credit loss under IAS 39. The determination of ECL requires consideration of past events, current conditions and forward-looking information.

Hedge accounting
IFRS 9 also introduces new hedge accounting rules that align hedge accounting more closely with risk management and expands the scope of hedged items and risks eligible for hedge accounting. IFRS 9 includes an accounting policy choice which permits the application of existing rules under IAS 39 for hedge accounting. Central 1 has elected to retain the hedge accounting requirements under IAS 39. However, Central 1 will implement the revised hedge accounting disclosures that are required by the IFRS 9 related amendments to IFRS 7, *Financial Instruments: Disclosures*, in its 2018 consolidated financial statements.

Transition
Based on December 31, 2017 data and current implementation status, Central 1 expects the adoption of IFRS 9 will lead to a reclassification impact in equity between retained earnings and accumulated other comprehensive income as at January 1, 2018 due to the classification and measurement requirements and the own credit risk assessment. The estimate of the impact of applying the new impairment model for financial assets is not significant. Central 1 will continue to validate and refine its impairment models and the process controls related to classification and measurement as required under IFRS 9.

IFRS 15 - Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15, Revenue from Contracts with Customers, which will replace the current revenue recognition standards IAS 18, Revenue, and related interpretations. In April 2016, the IASB issued amendments to IFRS 15, clarifying some requirements and providing additional transition relief at the date of initial application. The standard introduces a single comprehensive model to account for revenue arising from contracts with customers and applies to all contracts with customers, except for contracts that are within the scope of other IFRS standards such as leases, insurance contracts and financial instruments.

Jump to table of contents

Therefore, the adoption of IFRS 15 will not impact certain revenue streams of Central 1, including interest income, interest expense, gain (loss) on disposal of financial instruments and change in fair value of financial instruments.

IFRS 15 is effective for Central 1 for the annual periods beginning on or after January 1, 2018. As permitted, Central 1 will not restate the comparative period financial statements, but instead recognize the transition impact through an adjustment to the opening balance of retained earnings as at January 1, 2018. Central 1 has established a project to determine the impact of IFRS 15. Central 1's implementation approach consists of performing a detailed assessment of the significant revenue contracts through applying a five-step model which includes:

- Identifying the contract,
- Identifying the performance obligations within the contract,
- Determining the transaction price,
- Allocating the price to the performance obligations in the contract, and
- Recognizing revenue.

Central 1 is continuing to review its revenue contracts that fall within the scope of IFRS 15 and to assess the impact on its Consolidated Financial Statements, including the additional disclosure requirements. Based on December 31, 2017 data and current implementation status, the standard is not expected to have a material impact on the Consolidated Financial Statements.

IFRS 16 - Leases

In January 2016, the IASB issued IFRS 16, *Leases*, which will replace IAS 17, *Leases*, and related interpretations. IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard, and lessors continue to classify leases as finance or operating leases.

IFRS 16 has a mandatory effective date for annual periods beginning on or after January 1, 2019. The standard may be adopted retrospectively by applying the new lease definition to all contracts, or as of the application date by adjusting the retained earnings at that date and applying the new definition only to new contracts. Central 1 is not able to determine the impact of IFRS 16 on Central 1's Consolidated Financial Statements at this time.

Controls and Procedures

Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported on a timely basis to senior management, so that appropriate decisions can be made regarding public disclosure. As at the end of the year covered by this MD&A, management evaluated Central 1's disclosure controls and procedures as required by Canadian securities laws.

Based on that evaluation, management has concluded that the disclosure controls and procedures were effective in providing reasonable assurance that information required to be disclosed in Central 1's filings, as such term is defined under the Canadian Securities Administrators' National Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings, is recorded, processed, summarized and reported within the time periods specified by those laws, and that material information is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosure.

Internal Controls and Procedures

Central 1 evaluated the design of its internal controls and procedures over financial reporting as defined under National Instrument 52-109 for the year ended December 31, 2017. Based on that evaluation, management has concluded that the design of its internal monitoring controls and procedures over financial reporting was effective.

Transactions with Related Parties

In the normal course of business, Central 1 grants loans to its key management personnel under the same terms as those offered to any other employees. Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of Central 1, which include Central 1's Executive Management and Vice-Presidents. As of December 31, 2017, these loans totaled $364 thousand.

Details of Central 1's investments in subsidiaries, affiliates and the compensation of key management personnel and the Board are disclosed in Note 35 of the Consolidated Financial Statements as at December 31, 2017.

Credit Ratings

Central 1's debt securities are rated by DBRS and S&P.

Figure 31 – Credit Ratings

	DBRS	S&P
Instrument rating		
Senior debt	A (high)	A–
Subordinated debt	A	BBB+
Short-term debt	R-1 (middle)	A–2
Issuer rating		
Rating outlook	Stable	Stable

Five Year Summary – Consolidated Statements of Financial Position

(Thousands of dollars)	2017	2016	2015	2014	2013
Assets					
Cash	**$ 550,763**	$ 487,128	$ 106,834	$ 145,203	74,153
Deposits with regulated financial institutions	**5,975**	5,885	6,104	6,198	7,132
Trading assets	**8,889,745**	8,772,130	6,765,557	5,778,553	4,376,856
Reinvestment assets under the Canada Mortgage Bond Program	**545,247**	360,570	165,146	65,518	306,914
Derivative assets	**101,839**	81,807	116,631	42,162	29,383
Loans	**2,162,059**	1,453,802	1,490,839	1,047,637	1,157,972
Investment securities	**5,518,174**	5,621,749	5,680,158	5,475,562	5,553,354
Secured loans to members	**–**	–	–	–	229,620
Current tax assets	**7,027**	8,020	397	3,175	4,338
Property and equipment	**21,122**	18,022	18,807	18,388	16,111
Intangible assets	**34,665**	25,147	19,897	13,246	12,198
Deferred tax assets	**14,615**	5,171	11,924	10,342	6,371
Investments in affiliates	**143,642**	130,700	125,767	122,390	120,107
Settlements in-transit	**44,134**	327,062	427,167	308,449	280,976
Other assets	**29,893**	16,826	13,790	16,057	18,957
Total Assets	**$ 18,068,900**	$ 17,314,019	$ 14,949,018	$ 13,052,880	$ 12,194,442
Liabilities					
Deposits designated as trading	**8,561,503**	8,659,505	7,546,745	5,483,413	3,332,189
Obligations related to securities sold short	**95,503**	74,100	29,415	181,534	66,704
Derivative liabilities	**83,933**	85,660	130,805	104,174	150,645
Debt securities issued	**2,178,650**	1,490,730	1,075,344	1,568,840	1,097,509
Deposits	**3,436,892**	3,250,470	3,250,036	3,448,098	5,167,617
Obligations under the Canada Mortgage Bond Program	**1,190,108**	1,236,058	989,611	595,151	831,762
Subordinated liabilities	**421,765**	421,406	218,247	217,581	169,139
Provisions	**1,854**	1,688	1,882	2,958	3,991
Securities under repurchase agreements	**500,472**	298,416	221,211	105,698	106,706
Deferred tax liabilities	**23,000**	9,146	7,407	5,971	4,699
Settlements in-transit	**389,814**	643,602	432,913	344,569	329,398
Other liabilities	**66,285**	58,363	56,382	70,050	57,745
Total Liabilities	**16,949,779**	16,229,144	13,959,998	12,128,037	11,318,104
Equity					
Share capital	**428,143**	416,996	370,996	333,118	307,185
Contributed surplus	**72,897**	87,901	87,901	87,901	87,901
Retained earnings	**584,971**	552,782	506,979	467,072	433,171
Accumulated other comprehensive income	**19,072**	13,119	9,231	23,099	35,078
Reserves	**3,950**	4,034	3,954	3,751	3,130
Total equity attributable to members of Central 1	**1,109,033**	1,074,832	979,061	914,941	866,465
Non-controlling interest	**10,088**	10,043	9,959	9,902	9,873
	1,119,121	1,084,875	989,020	924,843	876,338
Total Liabilities and Equity	**$ 18,068,900**	$ 17,314,019	$ 14,949,018	$ 13,052,880	$ 12,194,442

Jump to table of contents

Five Year Summary – Consolidated Statements of Profit

(Thousands of dollars)	2017	2016	2015	2014	2013
Interest income					
Securities	**$ 208,050**	$ 170,947	$ 155,253	$ 162,635	$ 159,427
Deposits with regulated financial institutions	**164**	100	115	130	295
Loans	**37,487**	29,530	20,955	24,730	29,917
Reinvestment assets under the Canadian Mortgage Bond Program	**8,167**	5,896	1,880	6,076	43,817
	253,868	206,473	178,203	193,571	233,456
Interest expense					
Debt securities issued	**31,490**	15,594	18,301	22,752	18,159
Deposits	**138,038**	117,848	114,429	119,355	122,729
Obligations under the Canadian Mortgage Bond Program	**18,681**	17,859	14,065	14,950	52,726
Subordinated liabilities	**12,470**	7,564	6,260	8,610	6,542
	200,679	158,865	153,055	165,667	200,156
Interest margin	**53,189**	47,608	25,148	27,904	33,300
Gains (loss) on disposal of financial instruments	**(34,630)**	8,174	2,111	7,227	26,152
Change in fair value of financial instruments	**54,886**	11,747	22,809	37,224	29,290
Net financial income	**73,445**	67,529	50,068	72,355	88,742
Provision for (recovery) for credit losses	**(120)**	86	(86)	(15)	(1,203)
	73,565	67,443	50,154	72,370	89,945
Other income	**149,889**	140,499	140,706	119,745	115,829
Net financial and other income	**223,454**	207,942	190,860	192,115	205,774
Operating expenses					
Salaries and employee benefits	**76,156**	74,175	69,527	70,126	64,729
Premises and equipment	**9,073**	7,300	7,048	8,830	8,624
Other administrative expenses	**79,260**	60,122	52,972	50,525	53,423
	164,489	141,597	129,547	129,481	126,776
Profit before income taxes	**58,965**	66,345	61,313	62,634	78,998
Income taxes	**10,321**	9,305	8,963	9,044	10,548
Profit for the year	**$ 48,644**	$ 57,040	$ 52,350	$ 53,590	$ 68,450

Jump to table of contents

Statistical (Millions of dollars, unless otherwise indicated)	2017	2016	2015	2014	2013
Average Assets	**$ 17,851.2**	$ 15,739.6	$ 14,042.1	$ 12,947.6	$ 13,180.0
Average cash, securities and deposits with regulated financial institutions	**14,708.3**	13,332.9	12,243.4	10,843.1	9,907.5
Average loans	**1,928.6**	1,482.0	1,027.8	1,062.3	1,310.4
Average debt securities issued	**1,723.0**	1,242.2	1,319.8	1,337.7	1,021.3
Average subordinated liabilities	**422.1**	261.0	218.0	280.1	168.9
As a Percent of Average Assets					
Average cash & securities and deposits with regulated FI's	**82.4 %**	84.7 %	87.2 %	83.7 %	75.2 %
Average loans	**10.8 %**	9.4 %	7.3 %	8.2 %	9.9 %
Average debt securities issued	**9.7 %**	7.9 %	9.4 %	10.3 %	7.7 %
Average subordinated liabilities	**2.4 %**	1.7 %	1.6 %	2.2 %	1.3 %
Yields / Costs					
Cash, securities and deposits with regulated financial institutions	**1.4 %**	1.3 %	1.3 %	1.5 %	1.6 %
Loans	**1.9 %**	2.0 %	2.0 %	2.3 %	2.3 %
Debt securities issued	**1.7 %**	1.2 %	1.3 %	1.6 %	1.6 %
Returns on Average					
Assets	**0.3 %**	0.4 %	0.4 %	0.4 %	0.5 %
Share capital	**11.4 %**	14.9 %	15.2 %	17.0 %	23.3 %
Equity	**4.4 %**	5.6 %	5.5 %	5.9 %	8.2 %
Returns on Average					
Assets (before taxes and dividends)	**0.3 %**	0.4 %	0.4 %	0.5 %	0.6 %
Share capital (before taxes and dividends)	**13.9 %**	17.4 %	17.8 %	19.9 %	26.9 %
Equity (before taxes and dividends)	**5.3 %**	6.5 %	6.5 %	6.9 %	9.5 %
Dividends as % year-end capital	**5.4 %**	3.3 %	3.9 %	6.7 %	4.6 %
Debt/equity ratio	**15.1**	15.0	14.1	13.1	12.9
Dividends per share - Class A (cents)	**4.3**	3.6	4.2	7.1	4.8
Dividends per share - Class B and C (cents)	**1.7**	1.1	1.0	1.4	1.4
Average deposits	**$ 11,785.7**	$ 11,103.8	$ 9,768.4	$ 8,770.2	$ 8,682.1
Average debt securities issued	**1,723.0**	1,242.2	1,319.7	1,356.3	1,021.3
Average repurchase agreements	**600.7**	259.1	215.1	126.8	143.9
Average share capital	**424.9**	382.0	345.0	314.7	294.2
Average equity	**1,111.7**	1,023.2	949.1	901.9	835.7
Dividends	**23.1**	13.6	14.4	22.4	14.0

Jump to table of contents

Glossary of Financial Terms

Asset-Backed Commercial Paper is a short-term investment with a maturity that is typically less than 180 days. The commercial paper is backed by physical assets such as trade receivables and is generally used for short-term financing needs.

Basis Point (bps) is one one-hundredth of a percentage point.

Borrowing Multiple is the ratio of Central 1's total borrowings to regulatory capital.

Capital Base includes Tier 1 and Tier 2 capital, net of certain deductions.

Capital Ratio is the ratio of risk-adjusted assets to capital as defined by provincial legislation. The provincial legislation closely approximates that applied to other financial institutions by the Office of the Superintendent of Financial Institutions.

Commitments to extend credit are amounts in undrawn credit facilities and unutilized lending arrangements that have been authorized to Central 1's members.

Credit Spread is the difference between the yield of a given debt security and the yield of a risk-free government bond with similar maturity.

Derivatives are contracts which require little or no initial investment and where payments between parties are "derived" from movements in interest or foreign exchange rates, indices, equities or commodity prices. Derivatives allow for the transfer, modification or reduction of current or expected risks from changes in rates and prices.

Earnings Per Share (EPS) is calculated by dividing profit by the average number of member common shares outstanding.

Fair Value is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Group Clearer is the arrangement whereby Central 1 is appointed as the group clearing member of the Payments Canada that, on its own behalf and on behalf of the clearing Centrals, exchanges payment items and effects clearing and settlement into the Payments Canada system.

Hedging is a risk management technique used to neutralize or manage interest rate, foreign currency, equity, commodity or credit exposures arising from normal business activities.

Interest Margin is the difference between the amounts of interest earned on interest bearing assets less the amounts of interest paid on liabilities that have interest charges associated with them and include both on- and-off-balance sheet financial instruments.

Liquidity is the ability to meet debt obligations, guarantees and commitments as they become due through the use of cash or the conversion of assets that are readily convertible to cash.

Mark-to-Market represents the valuation of securities and derivatives at market rates as of the balance sheet date, where required by accounting rules.

Net Income is a performance measure used to describe the B.C. and Ontario credit union networks. It is the source of retained earnings and is equal to net operating income after income taxes, but before dividends, patronage refunds, charitable donations, capital gains/extraordinary items and other comprehensive income.

Net Financial Income consists of interest and dividend income earned on financial assets, plus realized and unrealized gains or losses on financial instruments, and less interest expense paid on financial liabilities.

Operating Income (Loss) is other income less operating expenses. Central 1 typically records an operating loss as the administration costs of earning financial income are included in this calculation, but the revenue is not.

Productivity Ratio is the ratio of operating expenses to the sum of net financial income and other income.

Productivity Ratio – Non-Financial is the ratio of operating expenses to other income.

Provision for Credit Losses is a charge to income that represents an amount deemed adequate by management to fully provide for impairment in loans and acceptances and other credit instruments, given the composition of the portfolios, the probability of default, the economic environment and the allowance for credit losses already established.

Return on Average Equity is calculated as profit for the year, as a percentage of average member shareholders' equity. Member shareholders' equity consists of share capital, contributed surplus, accumulated other comprehensive income (loss), retained earnings and reserves.

Jump to table of contents

Securities Acquired under Reverse Repurchase Agreements are instruments supported by the pledge of collateral, which arise from transactions that involve the borrowing or purchasing of securities.

Securities Sold under Repurchase Agreements are low-cost, low-risk liabilities, supported by collateral, which arise from transactions that involve the lending or selling of securities.

Swaps are contractual agreements between two parties to exchange a series of cash flows with counterparties generally exchanging fixed and floating rate interest payments based on a notional value.

Swap Spread is the difference between the fixed rate paid on a given swap and the yield of a risk-free government bond with similar maturity.

Consolidated **Financial Statements**

Years ended December 31, 2017, 2016 and 2015

Jump to table of contents

Management's Responsibility for Financial Reporting

The management of Central 1 Credit Union (Central 1) is responsible for the integrity, objectivity, reliability and fair presentation of the accompanying consolidated financial statements. These consolidated financial statements were prepared in accordance with International Financial Reporting Standards, as issued by the International Accounting Standards Board.

These consolidated financial statements contain items that reflect the best estimates and judgments of the expected effects of current events and transactions with appropriate consideration to materiality. The financial information presented elsewhere in this Annual Report is consistent with the information in the consolidated financial statements.

In meeting our responsibility for the integrity, objectivity, and reliability of financial information presented, Central 1 designed and maintained a system of accounting, internal controls and supporting procedures to provide reasonable assurance that financial records are complete, reliable, and accurate and that assets are safeguarded. The procedures include training and selection of qualified staff, and the establishment of an organizational structure that provides a well-defined division of responsibilities and accountability for performance. In addition, the systems include policies and standards of business conduct that are communicated throughout the organization to prevent conflicts of interest and unauthorized disclosure of information.

The Board of Directors, acting through its Audit and Finance Committee (the Committee), oversees management's responsibilities for the financial reporting and internal control systems. The Committee reviews the consolidated financial statements and recommends them to the Board of Directors for approval. Other key responsibilities of the Committee include reviewing the adequacy and effectiveness of internal controls, the performance of Central 1's internal audit function and external auditors, and the compliance with legal and regulatory requirements affecting financial reporting.

The Financial Institutions Commission of British Columbia conduct examinations and inquiries into Central 1's business and affairs as deemed necessary to satisfy themselves that the provisions of the appropriate legislation are being duly observed and that Central 1 is in sound financial condition.

KPMG LLP, the independent auditors appointed by the members, has performed an independent audit on the consolidated financial statements and issued their report, which follows. The auditors have full and complete access to, and meet periodically with, the Committee to discuss their audit and matters arising therefrom.

Mark Blucher
President & Chief Executive Officer

D. Blue
Chief Financial Officer

Independent Auditors' Report

To the Members of Central 1 Credit Union

We have audited the accompanying consolidated financial statements of Central 1 Credit Union, which comprise the consolidated statements of financial position as at December 31, 2017 and December 31, 2016, the consolidated statements of profit, comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

We believe that the audit evidence we have obtained in our audits 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 consolidated financial position of Central 1 Credit Union as at December 31, 2017 and December 31, 2016, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Professional Accountants
February 23, 2018
Vancouver, Canada

Consolidated Statements of Financial Position

As at December 31

(Thousands of dollars)	Notes	December 31, 2017	December 31, 2016	December 31, 2015
Assets				
Cash	(5)	$ 550,763	$ 487,128	$ 106,834
Deposits with regulated financial institutions		5,975	5,885	6,104
Trading assets	(6)	8,889,745	8,772,130	6,765,557
Reinvestment assets under the Canada Mortgage Bond Program	(6)	545,247	360,570	165,146
Derivative assets	(7)	101,839	81,807	116,631
Loans	(8)	2,162,059	1,453,802	1,490,839
Investment securities	(6)	5,518,174	5,621,749	5,680,158
Current tax assets		7,027	8,020	397
Property and equipment	(9)	21,122	18,022	18,807
Intangible assets	(10)	34,665	25,147	19,897
Deferred tax assets	(11)	14,615	5,171	11,924
Investments in affiliates	(12)	143,642	130,700	125,767
Settlements in-transit		44,134	327,062	427,167
Other assets	(13)	29,893	16,826	13,790
		$ 18,068,900	$ 17,314,019	$ 14,949,018
Liabilities				
Deposits designated as trading	(14)	$ 8,561,503	$ 8,659,505	$ 7,546,745
Obligations related to securities sold short	(15)	95,503	74,100	29,415
Derivative liabilities	(7)	83,933	85,660	130,805
Debt securities issued	(16)	2,178,650	1,490,730	1,075,344
Deposits	(14)	3,436,892	3,250,470	3,250,036
Obligations under the Canada Mortgage Bond Program	(16)	1,190,108	1,236,058	989,611
Subordinated liabilities	(17)	421,765	421,406	218,247
Securities under repurchase agreements	(16)	500,472	298,416	221,211
Provisions	(18)	1,854	1,688	1,882
Deferred tax liabilities	(11)	23,000	9,146	7,407
Settlements in-transit		389,814	643,602	432,913
Other liabilities	(20)	66,285	58,363	56,382
		16,949,779	16,229,144	13,959,998
Equity				
Share capital	(21)	428,143	416,996	370,996
Contributed surplus		72,897	87,901	87,901
Retained earnings		584,971	552,782	506,979
Accumulated other comprehensive income		19,072	13,119	9,231
Reserves		3,950	4,034	3,954
Total equity attributable to members of Central 1		1,109,033	1,074,832	979,061
Non-controlling interest		10,088	10,043	9,959
		1,119,121	1,084,875	989,020
		$ 18,068,900	$ 17,314,019	$ 14,949,018
Guarantees, commitments, and contingencies	(29)			
Commitments under leasing agreements	(30)			

See accompanying notes to the consolidated financial statements

Approved by the Directors:

Rick Hoevenaars
Chairperson

Robert Wellstood
Chairperson
Audit and Finance Committee

Jump to table of contents

Consolidated Statements of Profit

For the Years Ended December 31, 2017

(Thousands of dollars)	Notes	December 31, 2017	December 31, 2016	December 31, 2015
Interest income				
Securities		**$ 208,050**	$ 170,947	$ 155,253
Deposits with regulated financial institutions		**164**	100	115
Loans		**37,487**	29,530	20,955
Reinvestment assets under the Canada Mortgage Bond Program		**8,167**	5,896	1,880
		253,868	206,473	178,203
Interest expense				
Debt securities issued		**31,490**	15,594	18,301
Deposits		**138,038**	117,848	114,429
Obligations under the Canada Mortgage Bond Program		**18,681**	17,859	14,065
Subordinated liabilities		**12,470**	7,564	6,260
		200,679	158,865	153,055
Interest margin		**53,189**	47,608	25,148
Gain (loss) on disposal of financial instruments	(22)	**(34,630)**	8,174	2,111
Change in fair value of financial instruments	(23)	**54,886**	11,747	22,809
Net financial income		**73,445**	67,529	50,068
Provision for (recovery of) credit losses	(8)	**(120)**	86	(86)
		73,565	67,443	50,154
Other income	(24)	**149,889**	140,499	140,706
Net financial and other income		**223,454**	207,942	190,860
Operating expenses				
Salaries and employee benefits	(27)	**76,156**	74,175	69,527
Premises and equipment		**9,073**	7,300	7,048
Other administrative expenses	(25)	**79,260**	60,122	52,972
		164,489	141,597	129,547
Profit before income taxes		**58,965**	66,345	61,313
Income taxes	(26)	**10,321**	9,305	8,963
Profit for the year		**$ 48,644**	$ 57,040	$ 52,350

See accompanying notes to the consolidated financial statements

Jump to table of contents

Consolidated Statements of Comprehensive Income

For the Years Ended December 31

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Profit for the year	$ 48,644	$ 57,040	$ 52,350
Other comprehensive income (loss), net of tax			
Items that may be reclassified subsequently to profit or loss			
Fair value reserves (available-for-sale financial assets)			
Net change in fair value of available-for-sale financial assets[1]	13,064	9,082	(4,344)
Reclassification of realized gains on available-for-sale financial assets to profit or loss[2]	(7,218)	(4,706)	(13,912)
Share of the other comprehensive income (loss) of affiliates accounted for using the equity method[3]	(1,246)	337	775
	4,600	4,713	(17,481)
Item that will not be reclassified subsequently to profit or loss			
Net actuarial gain (loss) on employee benefit plans[4]	1,353	(825)	3,613
Other comprehensive income (loss), net of tax	5,953	3,888	(13,868)
Comprehensive income, net of tax	$ 54,597	$ 60,928	$ 38,482
Income tax (recoveries) on items that may be reclassified subsequently to profit or loss			
[1]Net change in fair value of available-for-sale financial assets	$ 2,752	$ 2,055	$ (850)
[2]Reclassification of realized gains on available-for-sale financial assets to profit or loss	$ (1,521)	$ (1,066)	$ (2,728)
[3]Share of the other comprehensive income (loss) of affiliates accounted for using the equity method	$ (15)	$ 14	$ 33
Income tax (recovery) on an item that will not be reclassified subsequently to profit or loss			
[4]Net actuarial gain (loss) on employee benefit plans	$ 535	$ (276)	$ 910

See accompanying notes to the consolidated financial statements

Consolidated Statements of Changes in Equity

For the Year Ended December 31, 2017

(Thousands of dollars)	Share Capital	Contributed Surplus	Retained Earnings	Fair Value and Affiliates Reserves	Employee Benefits Reserve	Other Reserves	Equity Attributable to Members	Non-Controlling Interest	Total Equity
	Attributable to equity members								
Balance at January 1, 2017	$ 416,996	$ 87,901	$ 552,782	$ 16,280	$ (3,161)	$ 4,034	$ 1,074,832	$ 10,043	$ 1,084,875
Total comprehensive income for the year									
Profit for the year			48,599				48,599	45	48,644
Other comprehensive income, net of tax									
Fair value reserve (available-for-sale financial assets)				5,846			5,846		5,846
Share of the other comprehensive loss of affiliates accounted for using the equity method				(1,246)			(1,246)		(1,246)
Employee benefits reserve					1,353		1,353		1,353
Total comprehensive income	–	–	48,599	4,600	1,353	–	54,552	45	54,597
Transactions with owners, recorded directly in equity									
Dividends to members			(23,129)				(23,129)		(23,129)
Related tax savings			4,024				4,024		4,024
Class "E" share reacquisitions	(2)	(15,004)					(15,006)		(15,006)
Related tax savings			2,611				2,611		2,611
Net Classes "A", "B" and "C" shares issued	11,149						11,149		11,149
Transfer from reserves			84			(84)	–		–
Total contributions from and distributions to owners	11,147	(15,004)	(16,410)	–	–	(84)	(20,351)	–	(20,351)
Balance at December 31, 2017	**$ 428,143**	**$ 72,897**	**$ 584,971**	**$ 20,880**	**$ (1,808)**	**$ 3,950**	**$ 1,109,033**	**$ 10,088**	**$ 1,119,121**

Profit attributable to:		**2017**	2016	2015
	Members of Central 1	**$ 48,599**	$ 56,956	$ 52,289
	Non-controlling interest	**45**	84	61
		$ 48,644	$ 57,040	$ 52,350
Total comprehensive income attributable to:				
	Members of Central 1	**$ 54,552**	$ 60,844	$ 38,421
	Non-controlling interest	**45**	84	61
		$ 54,597	$ 60,928	$ 38,482

See accompanying notes to the consolidated financial statements

Jump to table of contents

Consolidated Statements of Changes in Equity

For the Year Ended December 31, 2016

	Attributable to equity members								
(Thousands of dollars)	Share Capital	Contributed Surplus	Retained Earnings	Fair Value and Affiliates Reserves	Employee Benefits Reserve	Other Reserves	Equity Attributable to Members	Non-Controlling Interest	Total Equity
Balance at January 1, 2016	$ 370,996	$ 87,901	$ 506,979	$ 11,567	$ (2,336)	$ 3,954	$ 979,061	$ 9,959	$ 989,020
Total comprehensive income for the year									
Profit for the year			56,956				56,956	84	57,040
Other comprehensive income, net of tax									
Fair value reserve (available-for-sale financial assets)				4,376			4,376		4,376
Share of the other comprehensive income of affiliates accounted for using the equity method				337			337		337
Employee benefits reserve					(825)		(825)		(825)
Total comprehensive income	–	–	56,956	4,713	(825)	–	60,844	84	60,928
Transactions with owners, recorded directly in equity									
Dividends to members			(13,580)				(13,580)		(13,580)
Related tax savings			2,507				2,507		2,507
Net Classes “A”, “B” and “C” shares issued	46,000						46,000		46,000
Transfer to reserves			(80)			80	–		–
Total contributions from and distributions to owners	46,000	–	(11,153)	–	–	80	34,927	–	34,927
Balance at December 31, 2016	**$ 416,996**	**$ 87,901**	**$ 552,782**	**$ 16,280**	**$ (3,161)**	**$ 4,034**	**$ 1,074,832**	**$ 10,043**	**$ 1,084,875**

Jump to table of contents

Consolidated Statements of Changes in Equity

For the Year Ended December 31, 2015

(Thousands of dollars)	Share Capital	Contributed Surplus	Retained Earnings	Fair Value and Affiliates Reserves	Employee Benefits Reserve	Other Reserves	Equity Attributable to Members	Non-Controlling Interest	Total Equity
	Attributable to equity members								
Balance at January 1, 2015	$ 333,118	$ 87,901	$ 467,072	$ 29,048	$ (5,949)	$ 3,751	$ 914,941	$ 9,902	$ 924,843
Total comprehensive income for the year									
Profit for the year			52,289				52,289	61	52,350
Other comprehensive loss, net of tax									
Fair value reserve (available-for-sale financial assets)				(18,256)			(18,256)		(18,256)
Share of the other comprehensive income of affiliates accounted for using the equity method				775			775		775
Employee benefits reserve					3,613		3,613		3,613
Total comprehensive income	–	–	52,289	(17,481)	3,613	–	38,421	61	38,482
Transactions with owners, recorded directly in equity									
Dividends to members			(14,428)				(14,428)		(14,428)
Related tax savings			2,365				2,365		2,365
Class "E" share redemptions			(138)				(138)		(138)
Related tax savings			22				22		22
Net Classes "A", "B" and "C" shares issued	37,878						37,878		37,878
Preferred shares redeemed by subsidiary							–	(4)	(4)
Transfer to reserves			(203)			203	–		–
Total contributions from and distributions to owners	37,878	–	(12,382)	–	–	203	25,699	(4)	25,695
Balance at December 31, 2015	$ 370,996	$ 87,901	$ 506,979	$ 11,567	$ (2,336)	$ 3,954	$ 979,061	$ 9,959	$ 989,020

Consolidated Statements of Cash Flows

For the Years Ended December 31

(Thousands of dollars)	Notes	December 31, 2017	December 31, 2016	December 31, 2015
Cash flows from operating activities				
Profit for the year		**$ 48,644**	$ 57,040	$ 52,350
Adjustments for:				
Depreciation and amortization		**7,411**	5,626	4,632
Interest margin		**(53,189)**	(47,608)	(25,148)
Gain (loss) on disposal of financial instruments		**34,630**	(8,174)	(2,111)
Change in fair value of financial instruments		**(54,886)**	(11,747)	(22,809)
Income tax expense		**10,321**	9,305	8,963
Provision for (recovery of) credit losses		**(120)**	86	(86)
Other items, net		**(21,412)**	(7,408)	(4,217)
		(28,601)	(2,880)	11,574
Change in trading assets		**(194,603)**	(2,031,860)	(938,459)
Change in settlements in-transit		**29,141**	310,794	(30,374)
Change in loans		**(712,772)**	36,685	(442,724)
Change in deposits designated as trading		**(30,411)**	1,148,888	2,044,198
Change in obligations related to securities sold short		**23,315**	46,105	(157,180)
Change in deposits		**184,244**	121	(194,083)
Change in derivative instruments		**(21,055)**	(11,651)	(37,364)
		(750,742)	(503,798)	255,588
Interest received		**248,399**	206,071	173,533
Interest paid		**(191,430)**	(158,816)	(167,638)
Income tax paid		**(90)**	(6,679)	(1,251)
Net cash from (used in) operating activities		**(693,863)**	(463,222)	260,232
Cash flows from investing activities				
Change in deposits with regulated financial institutions		**(31)**	213	83
Change in reinvestment assets under the Canada Morgtage Bond Program		**(188,411)**	(194,709)	(98,576)
Change in investment securities		**120,914**	68,529	(212,636)
Change in property and equipment		**(5,994)**	(1,706)	(1,166)
Change in intangible assets		**(13,928)**	(8,277)	(8,505)
Net cash used in investing activities		**(87,450)**	(135,950)	(320,800)
Cash flows from financing activities				
Change in debt securities issued	(19)	**693,689**	414,959	(492,229)
Change in obligations under the Canada Morgtage Bond Program	(19)	**(28,176)**	252,755	383,471
Change in subordinated liabilities	(19)	**–**	203,000	–
Change in securities under repurchase agreements	(19)	**201,872**	77,180	115,527
Dividends paid	(19)	**(18,580)**	(14,428)	(22,448)
Issuance of shares		**11,147**	46,000	37,878
Change in contributed surplus		**(15,004)**	–	–
Net cash from financing activities		**844,948**	979,466	22,199
Increase (decrease) in cash		**63,635**	380,294	(38,369)
Cash – beginning of year		**487,128**	106,834	145,203
Cash – end of year		**$ 550,763**	$ 487,128	$ 106,834

See accompanying notes to the consolidated financial statements

Jump to table of contents

Table of Contents

Notes to the Consolidated Financial Statements

Years Ended December 31, 2017, 2016 and 2015

1. General information

Central 1 Credit Union (Central 1) is domiciled in Canada with a registered office located at 1441 Creekside Drive, Vancouver, British Columbia V6J 4S7, Canada. Central 1 is governed by the *Credit Union Incorporation Act (British Columbia).* These Consolidated Financial Statements cover Central 1 and its subsidiaries.

Central 1 is the primary liquidity manager, payments processor and trade association for credit unions in British Columbia and its member credit unions in Ontario. The performance of the British Columbia credit union network and that of Central 1's member credit unions in Ontario (collectively referred to herein as the Ontario credit union network) plays an integral part in determining the results of Central 1's operations and its financial position.

2. Basis of presentation

(a) Statement of compliance

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

The policies set out below have been consistently applied to all the periods presented and by all subsidiaries included in the Consolidated Financial Statements.

The Consolidated Financial Statements were authorized for issue by the Board of Directors on February 23, 2018.

(b) Basis of measurement

The Consolidated Financial Statements have been prepared on the historical cost basis except for the following:

- Derivative financial instruments are measured at fair value.
- Financial instruments at fair value through profit or loss (FVTPL) are measured at fair value.
- Available-for-sale financial assets are measured at fair value.
- The assets and liabilities for defined benefit obligations are recognized as the present value of the benefit obligation less the net total of the plan assets, plus unrecognized actuarial gains, less unrecognized actuarial past service costs and unrecognized actuarial losses.
- Recognized financial assets and financial liabilities designated as hedged items in qualifying fair value hedge relationships are adjusted for changes in fair value attributable to the risk being hedged.

(c) Functional and presentation currency

These Consolidated Financial Statements are presented in Canadian dollars, which is Central 1's functional currency.

(d) Use of estimates and judgements

In preparing the Consolidated Financial Statements in accordance with IFRS, management must exercise judgements and make estimates and assumptions that affect the application of accounting policies and the carrying amounts of assets and liabilities, net income and related disclosures. The most significant areas for which management must make subjective or complex estimates and judgements include financial instruments measured at fair value, designating financial instruments in qualifying hedge relationships, allowance for credit losses, income taxes and pension and post-retirement benefits. Description of these estimates and judgements are provided in Note 4. Actual results may differ materially from those estimates.

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

3. Accounting policies

The significant accounting policies used in the preparation of these Consolidated Financial Statements are summarized below.

(a) Basis of consolidation

Subsidiaries

The Consolidated Financial Statements include the assets, liabilities, results of operations and cash flows of Central 1 and its subsidiaries: 0789376 B.C. Ltd., Central Financial Corporation (1989) Ltd., Central 1 Trust Company, C.U. Financial Services Ltd., Central Data Systems Ltd., Credit Union Advantage Insurance Brokerage Ltd., CUPP Services Ltd., Inovera Solutions Inc., Landmark Credit Limited, and Stabilization Fund Corporation. These subsidiaries are entities where Central 1 exercises control through its ownership of the majority of the voting shares.

Management must exercise judgements in determining whether Central 1 must consolidate an entity. An entity is consolidated if Central 1 concludes that it controls the entity. The following circumstances may indicate a relationship in which, in substance, Central 1 controls and therefore consolidates the entity:

- Central 1 has power over the entity whereby Central 1 has the ability to direct the relevant activities (i.e., the activities that affect the entity's returns).
- Central 1 is exposed, or has rights, to variable returns from its involvement with the entity.
- Central 1 has the ability to use its power over the entity to affect the amount of the entity's returns.

The financial statements of subsidiaries are included in the Consolidated Financial Statements from the date that control commences until the date that control ceases. The Consolidated Financial Statements have been prepared using uniform accounting policies across all subsidiaries for like transactions and other events in similar circumstances. All inter-company transactions and balances are eliminated on consolidation.

Non-controlling interest

Credit unions of British Columbia participate in insurance programs offered by CUPP Services Ltd. (CUPP) and hold preferred shares of CUPP. Central 1 owns 100 per cent voting rights of CUPP and six per cent non-voting rights with the non-controlling interest (NCI) owning the remaining 94 per cent non-voting rights. NCI is presented as a separate component of equity in the Consolidated Statements of Financial Position, which represents the equity interests of credit unions of British Columbia, other than Central 1, in CUPP. The net profit attributable to non-controlling interest in CUPP is presented separately in the Consolidated Statements of Changes in Equity.

Affiliates

Affiliates are entities over which Central 1 has significant influence and are accounted for using the equity method of accounting. Significant influence is the power to participate in the financial and operating policy decisions of an entity. Central 1's investments in affiliates are initially accounted for at acquisition cost and subsequently increased or decreased to recognize Central 1's share of the affiliates' profit or loss, other comprehensive income, and the receipt of any dividends.

Further information regarding Central 1's subsidiaries and affiliates is contained in Note 12 and Note 35.

(b) Foreign currency

Transactions in foreign currencies are translated into Canadian dollars at the spot exchange rate at the date of the transaction. Subsequently, monetary assets and liabilities denominated in foreign currencies are retranslated into Canadian dollars at the spot exchange rate at the reporting date. Non-monetary assets and liabilities denominated in foreign currencies that are measured in terms of historical cost are translated into Canadian dollars using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated into Canadian dollars using the spot exchange rate at the date when the fair value was determined.

Foreign currency differences arising on translation are recognized in the Consolidated Statements of Profit. Foreign currency translation gains and losses on available-for-sale investment securities that are denominated in foreign currencies are also included in the Consolidated Statements of Profit.

(c) Financial assets and liabilities

Recognition

Central 1 initially recognizes financial assets on the date on which they are acquired and recognizes financial liabilities on the date on which they are issued. Regular way purchases and sales of financial assets are recognized on the trade date at which Central 1 commits to purchase or sell the assets. A financial asset or liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issuance.

Classification
All financial assets and liabilities must be classified based on their characteristics, management's intention, or management's choice of category in certain circumstances. When initially recognized, all financial assets are classified as FVTPL, available-for-sale, loans and receivables, or held-to-maturity, while all financial liabilities are classified as FVTPL or as other financial liabilities measured at amortized cost.

Classification of Central 1's financial assets and liabilities are described in Notes 3(d) to 3(j) and 3(p).

Fair value measurement
Note 31 contains information on the measurement of financial assets and liabilities recognized in the Consolidated Statements of Financial Position at fair value.

Derecognition
Central 1 derecognizes a financial asset when the contractual rights to the cash flows of the financial asset expire, or when it transfers the right to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. When Central 1 neither transfers nor retains substantially all the risks and rewards of ownership related to a financial asset, it derecognizes the financial asset that it no longer controls. In transactions which Central 1 neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset but it retains control over the asset, Central 1 continues to recognize the asset to the extent of its continuing involvement in that asset, determined by the extent to which it is exposed to changes in the value of the transferred asset. Any rights and obligations retained following the asset transfer are recognized as a separate asset or liability in the Consolidated Statements of Financial Position.

On derecognition of a financial asset, the difference between the carrying value of the asset and the sum of the consideration received and any cumulative gain or loss that has been recognized in other comprehensive income is recognized as profit or loss.

Where Central 1 enters into a transaction whereby it transfers assets but retains all or substantially all the risks and rewards of ownership, the transferred assets are not derecognized. Transfers of assets where Central 1 retains all or substantially all risks and rewards include, for example, securities lending and repurchase transactions.

Central 1 derecognizes a financial liability when its contractual obligations are discharged, cancelled or expired.

Offsetting
Financial assets and liabilities are offset and the net amount is presented in the Consolidated Statements of Financial Position when, and only when, Central 1 has a legal right to set off the recognized amounts and it intends to either settle on a net basis or to realize the asset and settle the liability simultaneously. Where a transfer of a financial asset does not qualify for derecognition, Central 1 does not offset the transferred asset and the associated liability.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions.

Identification and measurement of impairment
At each reporting date, Central 1 assesses whether there is objective evidence that financial assets not carried at FVTPL are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the assets that can be estimated reliably.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by the borrower or indications that a borrower or issuer will enter bankruptcy, and the disappearance of an active market for the security. It may also include other observable data related to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group or economic conditions that correlate with defaults in the group.

Central 1 considers evidence of impairment for loans and investment securities at both a specific asset and collective level. All individually significant loans and investment securities are assessed for specific impairment. All individually significant loans and investment securities not found to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and investment securities that are not individually significant are collectively assessed for impairment by grouping together loans and investment securities with similar characteristics.

In assessing collective impairment, Central 1 uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Jump to table of contents

Impairment losses on assets carried at amortized cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Impairment losses are recognized in the Consolidated Statements of Profit and reflected in an allowance account. Interest on impaired assets continues to be recognized through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Central 1 writes off loans and investment securities when they are determined to be uncollectible. Impairment losses on available-for-sale investment securities are recognized by reclassifying the losses accumulated in the fair value reserve in equity to profit or loss. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss. However, any subsequent recovery in the fair value of an available-for-sale equity security is recognized in other comprehensive income.

Designation at fair value through profit or loss
Central 1 has designated financial certain assets and financial liabilities at FVTPL in the following circumstances:

- The asset or liability is managed, evaluated and reported internally on a fair value basis.
- The designation eliminates or significantly reduces an accounting mismatch that would otherwise arise.
- The asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

(d) Cash

Cash includes unrestricted cash balances held with financial institutions. Cash is carried at amortized cost in the Consolidated Statements of Financial Position.

(e) Deposits with regulated financial institutions

Deposits with regulated financial institutions are classified as loans and receivables and initially measured at fair value plus incremental direct transaction costs. Subsequently, these deposits are measured at amortized cost using the effective interest method. Interest income earned is included in the Consolidated Statements of Profit using the accrual basis of accounting.

(f) Securities

Trading assets at FVTPL
Trading assets are those assets that Central 1 acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed for short-term profit or position-taking.

Trading assets at FVTPL are initially recognized and subsequently also measured at fair value in the Consolidated Statements of Financial Position, with transaction costs recognized directly in the Consolidated Statements of Profit. All changes in fair value and associated interest income as well as realized gains or losses are recognized in the Consolidated Statements of Profit.

Trading assets at FVTPL are not reclassified subsequent to their initial recognition, except that non-derivative trading assets, other than those designated at FVTPL upon initial recognition, may be reclassified out of the FVTPL (i.e. trading) category if they are no longer held for the purpose of being sold or repurchased in the near term and the following conditions are met:

- If the financial asset would have met the definition of loans and receivables, it may be reclassified if Central 1 has the intention and ability to hold the financial asset for the foreseeable future or until maturity.
- If the financial asset would not have met the definition of loans and receivables, it may be reclassified out of the trading category only in rare circumstances.

Investment securities
Investment securities are non-derivative financial assets that are classified as available-for-sale. These securities are initially and subsequently measured at fair value plus incremental direct transaction costs.

Certain equity securities that do not have a quoted market price in an active market and for which a reliable valuation cannot be obtained are carried at cost. The existence of restrictions placed on Central 1's ability to transfer or sell these investments severely limits the size of the available market. In the absence of purchases or sales of these securities between arm's length parties, Central 1 will continue to carry these investments at the value determined by reference to the most recent transaction which meets such criteria.

Interest income is recognized in profit or loss using the effective interest method. Foreign exchange gains or losses on available-for-sale debt security investments are recognized in profit or loss.

Other fair value changes are recognized, net of applicable income taxes, in the Consolidated Statements of Comprehensive Income until the investment is sold or impaired, whereupon the cumulative gains and losses previously recognized in other comprehensive income are reclassified to profit or loss as a reclassification adjustment.

A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it would otherwise have met the definition of loans and receivables and if Central 1 has the intention and ability to hold that financial asset for the foreseeable future or until maturity.

(g) Securitizations under the Canada Mortgage Bond (CMB) Program

Central 1's securitization activity primarily involves indirect securitizations whereby Central 1 facilitates the transfers of National Housing Act Mortgage-Backed Securities (NHA MBS) by its member credit unions by acting as a swap counterparty with Canada Housing Trust (CHT) and through the provision of administrative services. In such instances, indirect securitization transactions are off balance sheet and Central 1 records administration fees as other income when earned but Central 1 does not acquire an interest in the underlying mortgages.

Central 1 also participates in indirect securitization activities whereby Central 1 acts as a swap counterparty with CHT and receives a fee from its member credit unions for managing reinvestment assets.

Central 1 may also participate in direct securitizations by acquiring an interest in third-party MBS or insured mortgage pools from its member credit unions and subsequently transferring the associated MBS securities to CHT under the CMB Program.

Mortgages transferred to CHT continue to be recognized in Central 1's Consolidated Statements of Financial Position as, in the opinion of Central 1's management, these transactions do not result in the transfer of substantially all the risks and rewards of ownership of the underlying assets. Consideration received from CHT as a result of these transactions is recognized in Central 1's Consolidated Statements of Financial Position as secured borrowing.

(h) Derivative instruments

Derivative instruments are measured at fair value in the Consolidated Statements of Financial Position, with changes in fair value recognized in profit or loss.

Derivatives may be embedded in other contractual arrangements (a 'host contract'). Central 1 accounts for an embedded derivative separately from the host contract when the host contract is not itself carried at FVTPL, the terms of the embedded derivative meet the definition of a derivative if they were contained in a separate contract, and the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract. Separate embedded derivatives are accounted for depending on their classification and are presented in the Consolidated Statements of Financial Position together with their host contract.

Derivatives held for risk management purposes and hedge accounting

For risk management purposes, Central 1 designates certain derivatives to hedge fair value risk on select commercial loans and medium-term notes as hedging instruments in qualifying hedging relationships. Central 1 has not entered into any cash flow hedges at this time.

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

- At the inception of the hedge, there is formal designation and documentation of the hedging relationship and Central 1's risk management objective and strategy for undertaking the hedge. That documentation shall include identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk.
- The hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship.
- For cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss.
- The effectiveness of the hedge can be reliably measured (i.e. the fair value or cash flows of the hedged item that are attributable to the hedged risk and the fair value of the hedging instrument can be reliably measured).
- The hedge is assessed on an ongoing basis and determined to have been highly effective throughout the financial reporting periods for which the hedge was designated.

(i) Loans

Loans are financial assets with fixed or determinable payments that are not quoted in an active market and that Central 1 does not intend to sell immediately or in the short term.

With the exception of a single portfolio of commercial loans, which are measured at FVTPL, all loans are classified as loans and receivables and initially measured at fair value plus incremental direct transaction costs on the trade date in the Consolidated Statements of Financial Position. They are subsequently measured at amortized cost using the effective interest method, net of allowances for credit losses and any unearned interest. Interest income is recognized using the effective interest method, loan origination fees and other fees received and paid are recorded in interest income over the term of the loans.

(j) Securities purchased under reverse repurchase agreements and sold under repurchase agreements

Securities purchased under reverse repurchase agreements consist of the purchase of the security with a commitment by Central 1 to resell to the original seller on a specified date at a specified price. Financial assets acquired under reverse repurchase agreements, other than those acquired in securitization transactions, are classified as loans and receivable in the Consolidated Statements of Financial Position. The difference between the cost of the purchase and predetermined proceeds to be received on a resale agreement is recorded in interest income.

A repurchase agreement consists of the sale of a security with a commitment by Central 1 to repurchase the security on a specified date at a specified price. Obligations related to securities sold under repurchase agreements are recorded at amortized cost in the Consolidated Statements of Financial Position. The difference between the proceeds received on the sale of the security and the amount that Central 1 agrees to repay under the repurchase agreement is recorded in interest expense.

(k) Property and equipment

Items of property and equipment, except for land, are measured at cost less accumulated depreciation and accumulated impairment losses. Land is recorded at cost net of any impairment losses. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, and any other costs directly attributable to bringing the assets to a working condition for their intended use. Subsequent expenditure is capitalized only when it is probable that the future economic benefits of the expenditure will flow to Central 1. Ongoing repairs and maintenance are expensed as incurred.

When parts of an item of property and equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment. The gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of the item of property and equipment, and is recognized net within other income in the Consolidated Statements of Profit.

Depreciation is recognized in the Consolidated Statements of Profit on a straight-line basis over the estimated useful life of each part of an item of property and equipment, since this most closely reflects the pattern of consumption of future economic benefits embodied in the asset. Leased assets under finance leases are depreciated over the shorter of the lease term and their useful lives. Land is not depreciated.

The estimated useful lives for the current and comparative periods of significant items of property and equipment are as follows:

Buildings	50 years
Computer hardware	3 to 5 years
Furniture, fixtures and equipment	3 to 10 years
Leaseholds	Lesser of the useful life of the leasehold or the term of the lease

Depreciation methods, useful lives and residual values are reassessed at the end of each reporting period and adjusted if appropriate.

(l) Investment property

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services, or for administrative purposes. When the use of a property changes such that it is reclassified as property and equipment, its carrying value at the date of reclassification becomes its cost for subsequent accounting.

Items of investment property are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. When parts of an item of investment property have different useful lives, they are accounted for as separate items (major components) of investment property.

Jump to table of contents

Depreciation is recognized in the Consolidated Statements of Profit on a straight-line basis over the estimated useful lives of each part of an item of investment property. The estimated useful lives for the current and comparative periods are 50 years.

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

(m) Intangible assets

Software acquired by Central 1 is classified as an intangible asset and is measured at cost less accumulated depreciation and accumulated impairment losses.

Expenditure on internally developed software is recognized as an asset when Central 1 is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and can reliably measure the costs to complete the development. The capitalized costs of internally developed software include all costs directly attributable to developing the software and capitalized borrowing costs. Internally developed software is stated at capitalized cost less accumulated depreciation and impairment.

Subsequent expenditure on software assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Depreciation is recognized in the Consolidated Statements of Profit on a straight-line basis over the estimated useful life of the software, from the date that it is available for use, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. The estimated useful lives for the current and comparative periods are three to ten years.

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

(n) Leases

Central 1 as lessee

Assets held by Central 1 under leases which transfer to Central 1 substantially all of the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments, discounted at the interest rate implicit in the lease, if practicable, or else at Central 1's incremental borrowing rate. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset. Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Other leases are operating leases which are not recognized in the Consolidated Statements of Financial Position. Payments made under operating leases are recognized in the Consolidated Statements of Profit on a straight-line basis over the term of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

Central 1 as lessor

Leasing agreements whereby Central 1 earns rental income on premises classified as investment property are classified as operating leases. Central 1 recognizes rental income on a straight-line basis over the term of the lease. Lease inducements are recognized as an integral part of the total lease income, over the term of the lease.

(o) Impairment of non-financial assets

The carrying amounts of Central 1's non-financial assets, other than investment property and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. In assessing the value in use, the estimated future cash flows associated with the asset are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognized if the carrying amount of the asset exceeds its recoverable amount. An impairment loss recognized in prior periods for an asset is reversed if, and only if, there has been a change in the estimate used to determine the asset's recoverable amount since the last impairment was recognized. In this case, the impairment loss is reversed only to the extent that the carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no previous impairment loss had been recognized.

(p) Financial liabilities at FVTPL and other financial liabilities

Financial liabilities at FVTPL are those liabilities that Central 1 designates upon initial recognition. This designation is permitted when doing so results in more relevant information because either it eliminates or significantly reduces a measurement or recognition inconsistency, or a group of financial assets or financial liabilities or both is managed and its performance is evaluated on a fair value basis and information about the group is provided internally to key management personnel.

Financial liabilities at FVTPL are initially recognized and subsequently also measured at fair value in the Consolidated Statements of Financial Position, with transaction costs recognized directly in the Consolidated Statements of Profit. All changes in fair value and associated interest income as well as realized gains or losses are recognized in the Consolidated Statements of Profit.

Deposits, debt securities issued and subordinated liabilities are classified as other financial liabilities. They are initially measured at fair value plus incremental direct transaction costs and are subsequently measured at their amortized cost using the effective interest method.

(q) Provisions

A provision is recognized if, as a result of a past event, Central 1 has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

The provisions are reviewed at the end of each reporting period.

Central 1, in consultation with its actuaries, maintains a provision for unpaid claims, including adjustment expenses, which is discounted and represents the estimated amounts required to settle all outstanding and unreported claims incurred at the end of the reporting period. The initial estimate of unpaid claims is prepared on an undiscounted basis using assumptions, historical trends, and data available on individual claims to determine an expected Net Loss Ratio. Net Loss Ratio is the ratio of claims incurred during a specified period to the premiums earned during that period. The discounted provision for unpaid claims incorporates assumptions about projected cash flows and provisions for adverse deviations.

Differences between the estimated cost and subsequent settlement of claims are recognized in the Consolidated Statements of Profit in the year in which they are settled or in which the provision for claims outstanding is re-estimated. The provision for unpaid claims is subject to measurement uncertainty.

(r) Insurance contracts

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk is transferred when one party agrees to compensate another party (the policyholder) if a specified uncertain future event (other than a change in a financial variable) adversely affects the policyholder. Any contracts not meeting the definition of an insurance contract are classified as investment contracts or service contracts, as appropriate.

Through its subsidiary CUPP, Central 1 provides insurance related services to its members. CUPP is incorporated under the laws of British Columbia and is subject to the *Insurance (Captive Company) Act of British Columbia*.

CUPP provides the following insurance to its shareholders:

- Professional liability insurance, including directors' and officers', corporate errors and omissions, privacy, and employment practices liability insurance.
- Property and casualty insurance, including property, boiler and machinery, and loan impairment insurance.

Insurance premiums earned are included in other income and accounted for in the period in which the contract is entered into. Premiums are earned as revenue on a time proportionate basis over the term of the insurance coverage.

A provision for unearned premiums is included in other liabilities and represents the portion of premiums written relating to periods of insurance coverage subsequent to the reporting period.

Central 1 is exposed to insurance risk through the activities of CUPP. Insurance risk is the potential for financial loss or loss to Central 1's reputation resulting from inability to fully meet the obligations arising from offering insurance. This can result from higher than expected claims frequency, claim amounts and administration costs. Central 1 monitors its exposure to insurance risk by imposing underwriting limits and robust monitoring.

(s) Financial guarantees

Financial guarantees are contracts that require Central 1 to make specified payments to reimburse the beneficiary for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Liabilities arising from financial guarantees are recognized initially at their fair value, and the initial fair value is amortized over the life of the related guarantee. The liability is subsequently carried at the higher of this amortized amount and the present value of any expected payment when a payment under the guarantee becomes probable.

(t) Income taxes

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

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

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences:

- the initial recognition of an asset or a liability in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss; and
- temporary differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset only if:

- there is a legally enforceable right to offset current tax liabilities against current tax assets;
- they relate to income taxes levied by the same tax authority on the same taxable entity; or
- they relate to income taxes levied by the same tax authority on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized. In determining the amount of current and deferred tax, Central 1 takes into account the impact of uncertain tax positions and makes judgements, estimates and assumptions to assess whether additional taxes and interest may be due.

(u) Post-employment benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior reporting periods. Obligations for defined contribution pension plans are determined by the amounts to be contributed and recognized as expense in profit or loss when they are due in respect of service rendered before the end of the reporting period. Central 1 participates in a multi-employer defined benefit plan in which plan assets and liabilities are pooled and actuary does not determine an individual employer's own unfunded liability. Each member credit union is exposed to the actuarial risks of the other employers with the result that, in management's opinion, there is no reasonable way to allocate any defined benefit obligations. This plan is therefore accounted for on a defined contribution basis.

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. Central 1's net obligation in respect of defined benefits plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets. It is calculated periodically by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for service in the current and prior periods and discounting that benefit to determine its present value using market yields at the end of the reporting period on high-quality corporate bonds.

Central 1 recognizes all actuarial gains and losses arising from changes in actuarial assumptions and experience adjustments immediately in the Consolidated Statements of Comprehensive Income and all expenses related to defined benefit plans immediately in the Consolidated Statements of Profit.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognized in the Consolidated Statements of Profit on a straight-line basis over the average period until the benefits become vested. To the extent that benefits vest immediately, the expense is recognized immediately in the Consolidated Statements of Profit.

Short-term employee benefits

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

A liability is recognized for the amount expected to be paid under short-term incentive plans if Central 1 has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(v) Reserves

Through Stabilization Fund Corporation (SFC), Central 1 maintains the Credit Union Deductible Fund and the Stabilization Fund on behalf of its member credit unions in Ontario.

The Credit Union Deductible Fund, which is funded primarily by assessments to credit unions, represents the excess of revenue over expense related to the

Jump to table of contents

provision of insurance services. The Stabilization Fund represents an endowment in support of loss prevention activities which is restricted to programs that are considered loss preventative in nature.

(w) Revenue recognition

Interest income and expense
Interest income and expense, other than that earned or incurred on trading assets and financial liabilities at FVTPL, are recognized in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, Central 1 estimates future cash flows considering all contractual terms of the financial instrument, but without considering future credit losses. The calculation of the effective interest rate also includes all fees and amounts paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Transaction costs incurred on the acquisition of trading assets or issuance of financial liabilities at FVTPL are recognized in profit or loss at the time of acquisition or issuance. Central 1 records interest income and expense on trading assets and financial liabilities at FVTPL based on the contractual terms of the instrument.

Interest income and expense presented in the Consolidated Statements of Profit include:

- Interest income and expense on financial assets and liabilities measured at amortized cost calculated on an effective interest basis.
- Interest income on available-for-sale investment securities calculated on an effective interest basis.
- Interest income and expense on financial assets and liabilities measured at FVTPL based on the contractual terms of the instrument.

Changes in fair value of financial instruments
Changes in fair value of financial instruments included in the Consolidated Statements of Profit include:

- Fair value changes on derivatives.
- Fair value changes on loans at FVTPL.
- Fair value changes on trading assets and financial liabilities at FVTPL.
- Fair value changes on financial assets and liabilities under the CMB Program.
- Impairment charges on available-for-sale investment securities that have been reclassified from other comprehensive income.
- The effective and ineffective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

Other income
Fees and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Membership dues and provincial advertising assessments are received from Central 1's member credit unions and are recognized in income as earned. Fees earned by Digital & Payment Services, Wholesale Financial Services (WFS) and Other services are recorded in other income when Central 1 has rendered the related services and is entitled to receive income.

Dividends from equity instruments are recognized in the Consolidated Statements of Profit when Central 1's right to receive payment is established.

(x) Operating segments

Central 1's operations and activities are organized around a number of key operating segments in accordance with the aggregation criteria and quantitative thresholds under IFRS 8, *Operating Segments*. Management regularly monitors these segments' operating results for the purpose of making decisions about resource allocation and performance assessment. Segment results include items that are directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items including adjustments and other management reclassification, corporate taxes and residual unallocated revenue and expenses are included in "Other" segment. Further information is included in Note 28.

(y) New amendments to accounting standards adopted

Effective January 1, 2017, Central 1 has adopted the following amendments issued by the IASB:

Amendments to IAS 7: Statement of Cash Flows
In January 2016, the IASB issued an amendment to IAS 7, *Statement of Cash Flows*, to improve information provided to users of financial statements about an entity's financing activities. This amendment requires specific disclosures for movements in liabilities arising from financing activities on the Statement of Cash Flows in order to improve presentation and disclosure in financial statement. This amendment is effective for annual periods beginning on or after January 1, 2017. As a result of adopting this amendment, Central 1 has added an additional disclosure as described in Note 19.

Amendments to IAS 12: Income Taxes
In January 2016, the IASB issued amendments to IAS 12, *Income Taxes*, to clarify the requirements for recognizing deferred tax assets on unrealized losses. The amendments clarify that the existence of a deductible temporary difference depends solely on a comparison of the carrying amount of an asset and its tax base at the end of the reporting period, and is not affected by possible future changes in the carrying amount or expected manner of recovery of the asset. The amendments are effective for annual periods beginning on or after January 1, 2017. The adoption of the amendments did not have a significant impact on Central 1's Consolidated Financial Statements.

(z) New accounting standards and interpretations not yet adopted

IFRS 9 – Financial Instruments

In July 2014, International Accounting Standards Board (IASB) issued the complete version of IFRS 9, *Financial Instruments*, which will replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 is effective for Central 1 for the annual periods beginning on January 1, 2018 and is to be applied retrospectively with some exemptions. As permitted, Central 1 will not restate the comparative period financial statements, but instead recognize the transition impact through adjustments to the opening balances of retained earnings and accumulated other comprehensive income as at January 1, 2018.

Implementation approach
Central 1's implementation approach is based on five work streams including Scoping, Analysis, Development, Testing, and Go-live. Central 1's IFRS 9 project has focused on developing accounting policies, assessing business models for the classification and measurement of financial instruments, and developing and validating impairment models to support the IFRS 9 impairment conclusions.

Classification and measurement
Under IFRS 9, financial assets will be classified as amortized cost, fair value through profit or loss (FVTPL), or fair value through other comprehensive income (FVOCI) based on the business model for managing assets and the contractual cash flow characteristics of the financial asset.

Upon transition, the business model assessment will be based on the facts and circumstances as at January 1, 2018. Debt instruments that have contractual cash flows representing solely payments of principal and interest (SPPI) and are managed within a business model that is held-to-collect, are classified as amortized cost. Debt instruments that meet the SPPI test and are managed within a business model that is held-to-collect and for sale, are classified as FVOCI with changes in fair value recognized in other comprehensive income (OCI) until the asset is derecognized, upon which the cumulative gain or loss previously recognized in OCI is reclassified to profit or loss. All other debt instruments will be classified and measured as FVTPL.

Equity instruments would generally be measured at FVTPL unless an irrevocable election is made to classify these instruments at FVOCI which will result in change in fair value recognized in OCI with no subsequent impact to profit or loss upon the sale of the instruments.

The classification and measurement of financial liabilities remain essentially unchanged under IFRS 9 except for financial liabilities designated as FVTPL. Once the designation is made, changes in the fair value attributable to an entity's own credit risk should generally be recognized in other comprehensive income without subsequent reclassification in profit or loss.

Impairment
IFRS 9 introduces a new expected credit loss (ECL) model applicable for all debt instruments financial assets classified as amortized cost or FVOCI, as well as certain off-balance sheet loan commitments and financial guarantees. Compared to the current incurred loss model under IAS 39, *Financial Instruments: Recognition and Measurement*, the new ECL will result in an allowance for credit losses being recorded regardless of whether there has been an actual loss event. For financial assets that are credit impaired or have experienced a significant increase in credit risk, the loss allowance is recognized based on expected credit losses that result from possible default events over the expected lifetime (lifetime ECL). The loss allowance for all other financial assets are recognized based on the expected credit losses that result from possible default events within twelve months of the reporting date (twelve months ECL).

The definition of credit impaired is similar to an incurred credit loss under IAS 39. The determination of ECL requires consideration of past events, current conditions and forward-looking information.

Hedge accounting
IFRS 9 also introduces new hedge accounting rules that align hedge accounting more closely with risk management and expands the scope of hedged items and risks eligible for hedge accounting. IFRS 9 includes an accounting policy choice which permits the application of existing rules under IAS 39 for hedge accounting. Central 1 has elected to retain the hedge accounting requirements under IAS 39. However, Central 1 will implement the revised hedge accounting disclosures that are required by the IFRS 9 related amendments to IFRS 7, *Financial Instruments: Disclosures*, in its 2018 consolidated financial statements.

Jump to table of contents

Transition
Based on December 31, 2017 data and current implementation status, Central 1 expects the adoption of IFRS 9 will lead to a reclassification impact in equity between retained earnings and accumulated other comprehensive income as at January 1, 2018 due to the classification and measurement requirements and the own credit risk assessment. The estimate of the impact of applying the new impairment model for financial assets is not significant. Central 1 will continue to validate and refine its impairment models and the process controls related to classification and measurement as required under IFRS 9.

IFRS 15 - Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15, *Revenue from Contracts with Customers*, which will replace the current revenue recognition standards IAS 18, *Revenue*, and related interpretations. In April 2016, the IASB issued amendments to IFRS 15, clarifying some requirements and providing additional transition relief at the date of initial application. The standard introduces a single comprehensive model to account for revenue arising from contracts with customers and applies to all contracts with customers, except for contracts that are within the scope of other IFRS standards such as leases, insurance contracts and financial instruments. Therefore, the adoption of IFRS 15 will not impact certain revenue streams of Central 1, including interest income, interest expense, gain (loss) on disposal of financial instruments and change in fair value of financial instruments.

IFRS 15 is effective for Central 1 for the annual periods beginning on January 1, 2018. As permitted, Central 1 will not restate the comparative period financial statements, but instead recognize any transition impact through an adjustment to the opening balance of retained earnings as at January 1, 2018. Central 1 has established a project to determine the impact of IFRS 15. Central 1's implementation approach consists of performing a detailed assessment of the significant revenue contracts through applying a five-step model which includes:

- Identifying the contract,
- Identifying the performance obligations within the contract,
- Determining the transaction price,
- Allocating the price to the performance obligations in the contract, and
- Recognizing revenue.

Central 1 is continuing to review its revenue contracts that fall within the scope of IFRS 15 and to assess the impact on its Consolidated Financial Statements, including the additional disclosure requirements. Based on December 31, 2017 data and current implementation status, the standard is not expected to have a material impact on the Consolidated Financial Statements.

IFRS 16 - Leases

In January 2016, the IASB issued IFRS 16, *Leases*, which will replace IAS 17, *Leases*, and related interpretations. IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard, and lessors continue to classify leases as finance or operating leases.

IFRS 16 has a mandatory effective date for annual periods beginning on or after January 1, 2019. The standard may be adopted retrospectively by applying the new lease definition to all contracts, or as of the application date by adjusting the retained earnings at that date and applying the new definition only to new contracts. Central 1 is not able to determine the impact of IFRS 16 on Central 1's Consolidated Financial Statements at this time.

4. Use of estimates and judgements

The preparation of the Consolidated Financial Statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Judgement, estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Critical accounting estimates and assumptions

Information about estimates and assumptions that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities during the years presented is disclosed as follows:

(a) Allowance for credit losses
The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about the counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are reviewed and approved by management. Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and advances with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired loans, but the individual impaired items cannot yet be identified.

In assessing the need for collective loss allowances, management considers factors such as credit quality, portfolio size, concentrations and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on the estimates of future cash flows for specific counterparty allowances and the model assumptions and parameters used in determining collective allowances.

(b) Determining fair value

The determination of fair value for financial assets and liabilities requires the exercise of judgement by management. The determination of fair value of financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. For financial instruments that trade infrequently and have little price transparency, fair value is less objective and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. See Note 31 for further discussion.

(c) Income taxes

Central 1 computes an income tax provision in each of the jurisdictions in which it operates. However, the actual amounts of income tax expense only become final upon filing and acceptance of the tax return by the relevant authorities, which occurs subsequent to the issuance of the Consolidated Financial Statements. Estimation of income taxes includes evaluating the recoverability of deferred tax assets based on an assessment of the ability to use the underlying future tax deductions, before they expire, against future taxable income. The assessment is based upon enacted tax acts and estimates of future taxable income. To the extent estimates differ from the final tax provision, earnings would be affected in a subsequent period.

At the end of every reporting period, the income tax provision is based on an estimate of projected annual earnings by jurisdiction. The estimated average annual effective income tax rates are re-estimated at each reporting date, based on full-year projections of earnings by jurisdiction. To the extent that forecasts differ from actual results, adjustments are recorded in subsequent periods.

(d) Post-employment benefits

Central 1 sponsors defined benefit plans providing pension and other post-retirement benefits to employees. The expense and obligations associated with employee future benefits are calculated by actuaries using assumptions such as the expected return on assets available to fund pension obligations, the discount rate to measure obligations, the expected mortality, the expected rate of future compensation and the expected healthcare cost trend rate. If actual experience differs from the assumptions used, the difference is recognized in the Consolidated Statements of Comprehensive Income.

Critical judgements in applying accounting policies

Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognized in the Consolidated Financial statements is disclosed as follows:

(a) Securitizations

In applying its policies on securitized financial assets, Central 1 has considered both the degree of transfer of risks and rewards on assets transferred to another entity and the degree of control exercised by Central 1 over the other entity:

- When Central 1, in substance, controls the entity to which financial assets have been transferred, the entity is included in these Consolidated Financial Statements and the transferred assets are recognized in Central 1's Consolidated Statements of Financial Position.
- When Central 1 transfers financial assets to an unconsolidated entity and it retains substantially all the risk and rewards relating to the transferred assets, the transferred assets are recognized in Central 1's Consolidated Statements of Financial Position.
- When Central 1 transfers substantially all the risks and rewards relating to the transferred financial assets to an unconsolidated entity, the assets are derecognized from Central 1's Consolidated Statements of Financial Position.
- When Central 1 neither transfers nor retains substantially all the risks and rewards relating to a transferred financial asset and it retains control of the transferred asset, Central 1 continues to recognize the transferred financial asset to the extent of its continuing involvement in that transferred financial asset.

Details of Central 1's securitization activities are given in Notes 6 and 16.

(b) Determining if control exists over an investee

Under IFRS 10, *Consolidated Financial Statements,* an entity must determine whether or not it is exposed to, or has rights to, variable returns from its involvement with the investees and has the ability to affect those returns through its powers over the investees. This requires the entity to use judgement to assess the nature of the operations of the investee, the degree to which it is able to direct those operations and the level of exposure that it has to the variable returns of the investees.

5. Cash

(Thousands of dollars)	December 31, 2017		December 31, 2016		December 31, 2015
With Bank of Canada	$	471,889	$ 407,354	$	15,481
With other regulated financial institutions		78,874	79,774		91,353
	$	550,763	$ 487,128	$	106,834

6. Securities

Trading assets

Total trading assets included in the Consolidated Statements of Financial Position are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Government and government guaranteed securities	$ 6,000,006	$ 6,182,090	$ 4,579,399
Corporate and major financial institution securities AA[1] or greater	1,492,034	2,203,441	1,847,895
Other	1,397,705	386,599	338,263
Fair value	$ 8,889,745	$ 8,772,130	$ 6,765,557
Amortized cost	$ 8,943,209	$ 8,766,263	$ 6,713,809

[1]The credit ratings are provided by Dominion Bond Rating Services (DBRS).

Investment securities

Total investment securities classified as available-for-sale included in the Consolidated Statements of Financial Position are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Fair Value			
Government and government guaranteed securities	$ 4,476,928	$ 3,917,866	$ 3,663,936
Corporate and major financial institution securities AA[1] or greater	283,169	1,457,717	1,605,733
Other	725,957	214,046	378,369
Fair value	$ 5,486,054	$ 5,589,629	$ 5,648,038
Cost			
Other	$ 32,120	$ 32,120	$ 32,120
Total investment securities	$ 5,518,174	$ 5,621,749	$ 5,680,158

[1]The credit ratings are provided by DBRS.

The above table includes $32.1 million of equity investment securities that are measured at cost and for which disclosure of fair value is not provided because the fair value cannot be reliably measured. There have been no changes in this amount in the periods presented.

Jump to table of contents

Reinvestment assets under the Canada Mortgage Bond Program

As principal payments on the underlying securitized assets are received, Central 1 is required to reinvest the proceeds on behalf of Canada Housing Trust (CHT). These reinvestment assets are recognized in the Consolidated Statements of Financial Position at fair value, except for those classified as loans and receivables, which are recognized at amortized cost. The following table provides a breakdown of these reinvestment assets:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Classified as FVTPL			
Government and government guaranteed securities	**$ 409,571**	$ 284,856	$ 101,919
Amortized cost	**$ 411,283**	$ 283,135	$ 101,022
Classified as available-for-sale			
Government and government guaranteed securities	**$ 135,448**	$ 75,714	$ 63,227
Amortized cost	**$ 135,425**	$ 75,344	$ 62,522
Classified as loans and receivables			
Assets acquired under reverse repurchase agreements	**$ 228**	$ –	$ –
Total reinvestment assets under the CMB Program	**$ 545,247**	$ 360,570	$ 165,146

7. Derivative instruments

The following tables summarize the fair value and the notional amounts by term to maturity of derivative assets and liabilities:

(Thousands of dollars) December 31, 2017	Notional amount by term to maturity 1 year or less	1 to 5 years	Over 5 years	Total	Fair value Asset	Liability
Interest rate contracts						
Bond forwards	$ 96,700	$ –	$ –	$ 96,700	$ 74	$ 234
Futures contracts	65,000	–	–	65,000	11	122
Swap contracts	5,662,141	24,027,668	602,877	30,292,686	153,555	135,897
Options purchased	10,000	–	–	10,000	309	–
Options written	10,000	–	–	10,000	–	304
	5,843,841	24,027,668	602,877	30,474,386	153,949	136,557
Foreign exchange contracts						
Forward contracts	247,369	–	–	247,369	2,984	2,477
Other						
Equity index-linked options	54,545	177,199	–	231,744	11,370	11,363
Total fair value before adjustment					168,303	150,397
Adjustment for offsetting					(66,464)	(66,464)
Fair value					**$ 101,839**	**$ 83,933**

The amounts that have been pledged and received as collateral were $19.8 million and $12.4 million, respectively, as at December 31, 2017.

Jump to table of contents

(Thousands of dollars) December 31, 2016	Notional amount by term to maturity 1 year or less	1 to 5 years	Over 5 years	Total	Fair value Asset	Liability
Interest rate contracts						
Bond forwards	$ 79,500	$ –	$ –	$ 79,500	$ 427	$ 455
Futures contracts	432,750	–	–	432,750	52	44
Swap contracts	3,720,886	25,335,611	622,791	29,679,288	161,698	165,727
	4,233,136	25,335,611	622,791	30,191,538	162,177	166,226
Foreign exchange contracts						
Forward contracts	152,435	–	–	152,435	1,205	1,009
Other						
Equity index-linked options	61,738	191,925	–	253,663	13,560	13,560
Total fair value before adjustment					176,942	180,795
Adjustment for offsetting					(95,135)	(95,135)
Fair value					$ 81,807	$ 85,660

The amounts that had been pledged and received as collateral were $9.1 million and $23.5 million, respectively, as at December 31, 2016.

(Thousands of dollars) December 31, 2015	Notional amount by term to maturity 1 year or less	1 to 5 years	Over 5 years	Total	Fair value Asset	Liability
Interest rate contracts						
Bond forwards	$ –	$ 83,600	$ –	$ 83,600	$ 299	$ 147
Futures contracts	205,000	–	–	205,000	118	137
Swap contracts	4,867,985	19,557,494	1,664,861	26,090,340	238,348	252,275
	5,072,985	19,641,094	1,664,861	26,378,940	238,765	252,559
Foreign exchange contracts						
Forward contracts	269,368	–	–	269,368	5,105	5,485
Other						
Equity index-linked options	79,163	199,710	–	278,873	8,287	8,287
Total fair value before adjustment					252,157	266,331
Adjustment for offsetting					(135,526)	(135,526)
Fair value					$ 116,631	$ 130,805

The amounts that had been pledged and received as collateral were $17.8 million and $38.5 million, respectively, as at December 31, 2015.

All derivatives are traded over-the-counter except for futures contracts which are exchange traded.

Hedge accounting

Central 1 uses swap contracts to hedge its exposure to changes in the fair values of selected commercial loans and selected medium-term notes, both of which are at risk of changes in market interest rates. The critical terms of the interest rate swaps are matched to these specific commercial loans and medium-term notes at inception. Central 1 has elected to adopt hedge accounting in respect of the swap contracts and the hedged items.

The fair value of derivatives designated as fair value hedges were as follows:

	December 31, 2017		December 31, 2016		December 31, 2015	
(Thousands of dollars)	Asset	Liability	Asset	Liability	Asset	Liability
Swap contracts	**$ –**	**$ 3,156**	$ 1,614	$ –	$ 421	$ –

Hedging instruments are recorded at fair value, and the commercial loans and medium-term notes that are part of a hedging relationship are adjusted for the changes in value of the risk being hedged (fair value hedge adjustment). To the extent that the change in the fair value of the derivative does not offset changes in the fair value of the hedged item (hedge ineffectiveness), the net amount is recorded directly in the Consolidated Statements of Profit.

The following table presents the impact of fair value hedges on profit:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Change in fair value on hedging derivatives	**$ (4,770)**	$ 1,193	$ 421
Fair value hedge adjustment on loans/medium-term notes	**4,800**	(1,280)	(332)
Hedge ineffectiveness recorded in profit	**$ 30**	$ (87)	$ 89

Jump to table of contents

8. Loans

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amortized cost			
Due on demand			
Credit unions	$ 157,564	$ 31,544	$ 16,290
Commercial and others	1,406	3,716	3,263
	158,970	35,260	19,553
Term			
Credit unions	624,717	297,984	767,800
Commercial and others	622,392	609,357	531,388
Reverse repurchase agreements	591,944	316,362	48,880
Officers and employees	7,937	8,771	9,441
Residential mortgages	139,870	161,557	97,995
	1,986,860	1,394,031	1,455,504
	2,145,830	1,429,291	1,475,057
Accrued interest	2,671	2,146	1,285
Premium	8,897	11,990	14,998
	2,157,398	1,443,427	1,491,340
Allowance for credit losses	(527)	(518)	(501)
Amortized cost	2,156,871	1,442,909	1,490,839
Fair value hedge adjustment[1]	(6,261)	(1,232)	–
Carrying value	$ 2,150,610	$ 1,441,677	$ 1,490,839
Fair value through profit or loss			
Term			
Commercial and others	$ 11,225	$ 11,582	$ –
Accrued interest	35	36	–
Premium	104	128	–
Amortized cost	$ 11,364	$ 11,746	$ –
Fair value	$ 11,449	$ 12,125	$ –
Total loans	$ 2,162,059	$ 1,453,802	$ 1,490,839

[1] *Central 1 enters into fair value hedges to hedge the risks caused by changes in interest rates. See Note 7 for detailed information on hedge accounting.*

Loans to officers and employees bear interest at rates varying from 2.49% to 2.75%.

The activities in the allowance for credit losses during the year and the resulting balances were as follows:

(Thousands of dollars)	Specific Allowance	Collective Allowance	December 31, 2017	December 31, 2016	December 31, 2015
Balance at beginning of year	$ 339	$ 179	$ 518	$ 501	$ 664
Net write-off (recovery) during the year	(4)	133	129	(69)	(77)
Provision for (recovery of) credit losses	–	(120)	(120)	86	(86)
Balance at end of year	$ 335	$ 192	$ 527	$ 518	$ 501

9. Property and equipment

(Thousands of dollars)		Land and Building		IT Equipment		Fixtures		Total
Cost								
Balance at January 1, 2017	**$**	**17,133**	**$**	**14,185**	**$**	**14,767**	**$**	**46,085**
Acquisitions		**–**		**2,162**		**3,885**		**6,047**
Disposals		**–**		**(282)**		**(212)**		**(494)**
Balance at December 31, 2017	**$**	**17,133**	**$**	**16,065**	**$**	**18,440**	**$**	**51,638**
Balance at January 1, 2016	$	17,133	$	14,900	$	13,993	$	46,026
Acquisitions		–		736		1,128		1,864
Disposals		–		(1,451)		(354)		(1,805)
Balance at December 31, 2016	$	17,133	$	14,185	$	14,767	$	46,085
Balance at January 1, 2015	$	15,344	$	15,352	$	13,623	$	44,319
Acquisitions		–		434		742		1,176
Transfers (see Note 13)		1,789		–		–		1,789
Disposals		–		(886)		(372)		(1,258)
Balance at December 31, 2015	$	17,133	$	14,900	$	13,993	$	46,026
Depreciation								
Balance at January 1, 2017	**$**	**9,595**	**$**	**10,202**	**$**	**8,266**	**$**	**28,063**
Depreciation		**594**		**1,073**		**1,227**		**2,894**
Disposals		**–**		**(282)**		**(159)**		**(441)**
Balance at December 31, 2017	**$**	**10,189**	**$**	**10,993**	**$**	**9,334**	**$**	**30,516**
Balance at January 1, 2016	$	9,001	$	10,779	$	7,439	$	27,219
Depreciation		594		795		1,102		2,491
Disposals		–		(1,372)		(275)		(1,647)
Balance at December 31, 2016	$	9,595	$	10,202	$	8,266	$	28,063
Balance at January 1, 2015	$	8,541	$	10,748	$	6,642	$	25,931
Depreciation		460		907		1,169		2,536
Disposals		–		(876)		(372)		(1,248)
Balance at December 31, 2015	$	9,001	$	10,779	$	7,439	$	27,219
Carrying value								
Balance as at December 31, 2017	**$**	**6,944**	**$**	**5,072**	**$**	**9,106**	**$**	**21,122**
Balance as at December 31, 2016	$	7,538	$	3,983	$	6,501	$	18,022
Balance as at December 31, 2015	$	8,132	$	4,121	$	6,554	$	18,807

10. Intangible assets

(Thousands of dollars)	External Software	Internally Developed Software	Total
Cost			
Balance at January 1, 2017	**$ 25,854**	**$ 9,854**	**$ 35,708**
Acquisitions	**8,035**	**5,893**	**13,928**
Disposals	**(32)**	**–**	**(32)**
Balance at December 31, 2017	**$ 33,857**	**$ 15,747**	**$ 49,604**
Balance at January 1, 2016	$ 23,404	$ 4,305	$ 27,709
Acquisitions	2,743	5,549	8,292
Disposals	(293)	–	(293)
Balance at December 31, 2016	$ 25,854	$ 9,854	$ 35,708
Balance at January 1, 2015	$ 16,445	$ 2,810	$ 19,255
Acquisitions	7,000	1,495	8,495
Disposals	(41)	–	(41)
Balance at December 31, 2015	$ 23,404	$ 4,305	$ 27,709
Depreciation			
Balance at January 1, 2017	**$ 9,204**	**$ 1,357**	**$ 10,561**
Depreciation	**3,607**	**803**	**4,410**
Disposals	**(32)**	**–**	**(32)**
Balance at December 31, 2017	**$ 12,779**	**$ 2,160**	**$ 14,939**
Balance at January 1, 2016	$ 6,990	$ 822	$ 7,812
Depreciation	2,493	535	3,028
Disposals	(279)	–	(279)
Balance at December 31, 2016	$ 9,204	$ 1,357	$ 10,561
Balance at January 1, 2015	$ 5,492	$ 517	$ 6,009
Depreciation	1,549	305	1,854
Disposals	(51)	–	(51)
Balance at December 31, 2015	$ 6,990	$ 822	$ 7,812
Carrying value			
Balance as at December 31, 2017	**$ 21,078**	**$ 13,587**	**$ 34,665**
Balance as at December 31, 2016	$ 16,650	$ 8,497	$ 25,147
Balance as at December 31, 2015	$ 16,414	$ 3,483	$ 19,897

Jump to table of contents

11. Deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Deferred tax assets			
Financial instruments	**$ (842)**	$ (838)	$ 5,808
Employee future benefits	**3,803**	5,302	4,881
Equity interest in affiliates	**874**	874	874
Unused tax losses	**11,059**	–	–
Other	**(279)**	(167)	361
	$ 14,615	$ 5,171	$ 11,924
Deferred tax liabilities			
Financial instruments	**$ 13,698**	$ 730	$ 730
Property and equipment	**6,697**	6,079	4,890
Employee future benefits	**447**	633	725
Equity interest in affiliates	**2,158**	1,704	1,062
	23,000	9,146	7,407
Net deferred tax assets (liabilities)	**$ (8,385)**	$ (3,975)	$ 4,517

Changes in deferred tax balances during the year ended December 31, 2017 were as follows:

(Thousands of dollars)	Balance as at January 1, 2017	Recognized in profit or loss	Recognized in other comprehensive income	Balance as at December 31, 2017
Deferred tax assets				
Financial instruments	$ (838)	$ (4)	$ –	**$ (842)**
Employee future benefits	5,302	(1,145)	(354)	**3,803**
Equity interest in affiliates	874	–	–	**874**
Unused tax losses	–	12,609	(1,550)	**11,059**
Other	(167)	(112)	–	**(279)**
	$ 5,171	$ 11,348	$ (1,904)	**$ 14,615**
Deferred tax liabilities				
Financial instruments	$ 730	$ 12,968	$ –	**$ 13,698**
Property and equipment	6,079	618	–	**6,697**
Employee future benefits	633	(38)	(148)	**447**
Equity interest in affiliates	1,704	509	(55)	**2,158**
	9,146	14,057	(203)	**23,000**
Net deferred tax liabilities	$ (3,975)	$ (2,709)	$ (1,701)	**$ (8,385)**

Jump to table of contents

Changes in deferred tax balances during the year ended December 31, 2016 were as follows:

(Thousands of dollars)	Balance as at January 1, 2016	Recognized in profit or loss	Recognized in other comprehensive income	Balance as at December 31, 2016
Deferred tax assets				
Financial instruments	$ 5,808	$ (6,646)	$ –	$ (838)
Employee future benefits	4,881	115	306	5,302
Equity interest in affiliates	874	–	–	874
Other	361	(700)	172	(167)
	$ 11,924	$ (7,231)	$ 478	$ 5,171
Deferred tax liabilities				
Financial instruments	$ 730	$ –	$ –	$ 730
Property and equipment	4,890	1,189	–	6,079
Employee future benefits	725	(121)	29	633
Equity interest in affiliates	1,062	628	14	1,704
	7,407	1,696	43	9,146
Net deferred tax liabilities	$ 4,517	$ (8,927)	$ 435	$ (3,975)

Changes in deferred tax balances during the year ended December 31, 2015 were as follows:

(Thousands of dollars)	Balance as at January 1, 2015	Recognized in profit or loss	Recognized in other comprehensive income	Balance as at December 31, 2015
Deferred tax assets				
Financial instruments	$ 3,741	$ 2,067	$ –	$ 5,808
Employee future benefits	5,288	481	(888)	4,881
Equity interest in affiliates	874	–	–	874
Other	439	(78)	–	361
	$ 10,342	$ 2,470	$ (888)	$ 11,924
Deferred tax liabilities				
Financial instruments	$ 730	$ –	$ –	$ 730
Property and equipment	3,848	1,042	–	4,890
Employee future benefits	677	29	19	725
Equity interest in affiliates	716	290	56	1,062
	5,971	1,361	75	7,407
Net deferred tax assets	$ 4,371	$ 1,109	$ (963)	$ 4,517

12. Investments in affiliates

The carrying value of Central 1's investments in affiliates is as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Credential Financial Inc.	$ 6,058	$ 3,060	$ 2,279
Credit Union Central of Canada	–	–	1,025
The CUMIS Group Limited	135,198	126,271	122,463
Northwest & Ethical Investments L.P.	1,168	–	–
189286 Canada Inc.	1,218	1,369	–
	$ 143,642	$ 130,700	$ 125,767

Investments in Credential Financial Inc. (CFI) and Northwest & Ethical Investments L.P. were classified as held for sale as at December 31, 2017 to reflect the proposed transaction as disclosed in Note 36.

13. Other assets

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Investment property	$ 1,216	$ 1,323	$ 1,431
Prepaid expenses	9,956	6,334	4,581
Post-employment benefits (see Note 27)	3,085	2,624	3,306
Accounts receivable and other	15,636	6,545	4,472
	$ 29,893	$ 16,826	$ 13,790

Investment Property

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Carrying value, beginning balance	$ 1,323	$ 1,431	$ 3,462
Transfers (see Note 9)	–	–	(1,789)
Depreciation	(107)	(108)	(242)
Carrying value, ending balance	1,216	1,323	1,431
Fair value	$ 1,916	$ 1,989	$ 1,883

The fair value of Central 1's investment property has been arrived at based on the internal and external market information of similar properties at the end of each reporting period.

Central 1 earns rental income on its investment property. The terms of existing lease agreements range between one and ten years. The lessees do not have an option to purchase the property on the expiry of the lease period.

14. Deposits

The contractual maturity dates of deposits designated as trading are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amounts			
Due within three months	$ **1,788,615**	$ 2,045,759	$ 1,987,607
Due after three months and within one year	**1,704,206**	1,224,746	1,620,371
Due after one year and within five years	**5,103,429**	5,355,907	3,858,176
Due after five years	**350**	600	11,970
	8,596,600	8,627,012	7,478,124
Accrued interest	**44,622**	37,386	33,641
Amortized cost	$ **8,641,222**	$ 8,664,398	$ 7,511,765
Fair value	$ **8,561,503**	$ 8,659,505	$ 7,546,745

Deposits held at amortized cost are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amounts			
Due on demand	$ **1,577,881**	$ 1,577,567	$ 1,371,545
Due within three months	**79,739**	207,585	431,726
Due after three months and within one year	**805,077**	612,645	922,457
Due after one year and within five years	**968,315**	845,647	510,816
Due after five years	**–**	–	1,000
	3,431,012	3,243,444	3,237,544
Accrued interest	**5,880**	7,026	12,492
Amortized cost	$ **3,436,892**	$ 3,250,470	$ 3,250,036

15. Obligations related to securities sold short

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amortized cost	$ **95,819**	$ 74,532	$ 29,350
Fair value	$ **95,503**	$ 74,100	$ 29,415

16. Funding transactions

Debt securities issued

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amounts			
Due within three months	$ **805,034**	$ 725,288	$ 320,863
Due after three months and within one year	**481,473**	314,674	454,004
Due after one year and within five years	**896,469**	449,325	299,461
	2,182,976	1,489,287	1,074,328
Accrued interest	**5,209**	1,443	1,016
Amortized cost	**2,188,185**	1,490,730	1,075,344
Fair value hedge adjustment[1]	**(9,535)**	–	–
Amortized cost	$ **2,178,650**	$ 1,490,730	$ 1,075,344

[1]Central 1 enters into fair value hedges to hedge the risk caused by changes in interest rates. See Note 7 for detailed information on hedge accounting.

Central 1 has established $200.0 million of unsecured credit facilities with various financial institutions. The unsecured facilities rank equally with the outstanding notes and deposits. As at December 31, 2017, December 31, 2016, and December 31, 2015, the amounts outstanding were $117.4 million, $81.9 million and $60.6 million, respectively.

Central 1 was authorized to issue up to $1.0 billion in short-term commercial paper and up to $1.5 billion in other borrowings which includes Central 1's medium-term note facility in 2017. As at December 31, 2017, a par value of $837.8 million was borrowed under the short-term commercial paper facility (December 31, 2016 - $740.7 million, December 31, 2015 - $476.0 million) and a par value of $1,350.0 million was borrowed under the medium-term note facility (December 31, 2016 - $750.0 million, December 31, 2015 - $600.0 million). In January 2018, Central 1 has been authorized to issue other borrowings up to $1.7 billion, up from $1.5 billion in 2017.

On November 16, 2016, Central 1 issued $450.0 million principal amount of Series 13 medium-term floating rate notes due November 21, 2018. The notes bear interest at 3-month Canadian Dollar Offering Rate (CDOR) plus 62 basis points payable quarterly on the 21st of February, May, August, and November of each year, commencing February 21, 2018.

On March 9, 2017, Central 1 issued $400.0 million principal amount of Series 14 medium-term fixed rate notes due March 16, 2020. The notes bear interest at a fixed rate of 1.87%, payable semi-annually on the 16th of March and September of each year, commencing September 16, 2017.

On November 1, 2017, Central 1 issued $500.0 million principal amount of Series 15 medium-term fixed rate notes due November 7, 2022. The notes bear interest at a fixed rate of 2.60%, payable semi-annually on the 7th of May and November of each year, commencing May 7, 2018.

On January 31, 2018, Central 1 issued $350.0 million principal amount of Series 16 medium-term floating rate notes due February 5, 2021. The notes bear interest at 3-month CDOR plus 35 basis points payable and reset quarterly on the 5th of February, May, August, and November of each year, commencing May 5, 2018. The notes issued on January 31, 2018 were not included in the Consolidated Financial Statements as at December 31, 2017.

Jump to table of contents

Obligations under the CMB Program

Central 1 has recognized its obligations to CHT under the CMB Program at fair value in the Consolidated Statements of Financial Position. The contractual maturity dates of these obligations are indicated below.

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amounts			
Due within one year	**$ 213,156**	$ 182,814	$ –
Due after one year and within five years	**982,886**	1,041,201	970,329
	1,196,042	1,224,015	970,329
Accrued interest	**966**	1,231	733
Amortized cost	**$ 1,197,008**	$ 1,225,246	$ 971,062
Fair value	**$ 1,190,108**	$ 1,236,058	$ 989,611

The underlying assets which are designated to offset these obligations are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Fair value			
Total reinvestment assets under the CMB Program (see Note 6)	**$ 545,247**	$ 360,570	$ 165,146
Assets recognized as securities	**519,193**	755,787	822,051
Fair value	**$ 1,064,440**	$ 1,116,357	$ 987,197
Amortized cost			
Assets recognized in loans	**$ 130,933**	$ 121,132	$ –
Total underlying assets designated	**$ 1,195,373**	$ 1,237,489	$ 987,197

Securities under repurchase agreements

Securities under repurchase agreements are classified as other financial liabilities and recognized in the Consolidated Statements of Financial Position at amortized cost.

The following table summarizes the amount of securities under repurchase agreements outstanding at each period end:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amounts under the CMB Program	**$ 500,472**	$ 298,416	$ 170,325
Other	**–**	–	50,886
Amortized cost	**$ 500,472**	$ 298,416	$ 221,211

Jump to table of contents

17. Subordinated liabilities

The following table summarizes the amount of subordinated liabilities outstanding at each year ended:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Series 3	$ –	$ –	$ 18,000
Series 4	200,000	200,000	200,000
Series 5	21,000	21,000	–
Series 6	200,000	200,000	–
Principal amount	421,000	421,000	218,000
Discount	(1,646)	(1,997)	(824)
Accrued interest	2,411	2,403	1,071
Amortized cost	$ 421,765	$ 421,406	$ 218,247

On July 6, 2011, Central 1 issued $18.0 million principal amount of Series 3 subordinated notes due July 6, 2021. The notes bore interest at a floating rate based on 90-day Bankers' Acceptance plus 10 basis points, payable quarterly until July 6, 2016, and Central 1 had the option to redeem the outstanding notes in whole or in part on or after July 6, 2016, subject to regulatory approval. Central 1 received regulatory approval and exercised the option to fully redeem $18.0 million of Tier 2 qualifying Series 3 subordinated debt on July 6, 2016. This redemption was replaced by $21.0 million of new Tier 2 qualifying Series 5 subordinated debt further discussed below.

On April 25, 2014, Central 1 issued $200.0 million principal amount of Series 4 subordinated notes due April 25, 2024. The notes bear interest at a fixed rate of 2.89%, payable semi-annually, until, but excluding April 25, 2019, and thereafter at a floating rate based on 90-day Bankers' Acceptance plus 81 basis points, payable quarterly. Central 1 has the option to redeem the notes on or after April 25, 2019, subject to regulatory approval.

On July 6, 2016, Central 1 issued $21.0 million principal amount of Series 5 subordinated notes due July 6, 2026. The notes bear interest at a floating rate based on 90-day Bankers' Acceptance plus 10 basis points, payable quarterly until July 6, 2021, and Central 1 has the option to redeem the outstanding notes in whole or in part on or after July 6, 2021, subject to regulatory approval.

On October 14, 2016, Central 1 issued $200.0 million principal amount of Series 6 subordinated notes due October 14, 2026. The notes bear interest at a fixed rate of 3.06%, payable semi-annually, until, but excluding October 14, 2021, and thereafter at a floating rate based on 90-day Bankers' Acceptance plus 198 basis points, payable quarterly. Central 1 has the option to redeem the notes on or after October 14, 2021, subject to regulatory approval.

The notes are recognized in the Consolidated Statements of Financial Position at amortized cost.

Jump to table of contents

18. Provisions

Central 1 maintains provisions for unpaid insurance claims as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Balance at beginning of year	**$ 1,688**	$ 1,882	$ 2,958
Claims incurred	**1,025**	828	204
Claims paid	**(859)**	(1,022)	(1,280)
Balance at end of year	**$ 1,854**	$ 1,688	$ 1,882

As at year-end, the impact of a 1.0% increase in the expected net loss ratio would have less than a 1.0% impact on Central 1's profit for the year and Central 1's equity as at year-end.

19. Changes in liabilities arising from financing activities

The following table summarizes the changes in liabilities arising from financing activities for the year ended December 31, 2017:

			Non-cash changes		
(Thousands of dollars)	December 31, 2016	Cash flow changes	Fair value changes	Other	December 31, 2017
Debt securities issued	$ 1,490,730	$ 693,689	$ –	$ (5,769)	**$ 2,178,650**
Obligations under the CMB Program	1,236,058	(28,176)	(17,712)	(62)	**1,190,108**
Subordinated liabilities	421,406	–	–	359	**421,765**
Securities under repurchase agreements	298,416	201,872	–	184	**500,472**
Dividends payable	13,580	(18,580)	–	23,129	**18,129**
	$ 3,460,190	$ 848,805	$ (17,712)	$ 17,841	**$ 4,309,124**

20. Other liabilities

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Post-employment benefits (see Note 27)	**$ 22,503**	$ 23,625	$ 22,828
Short-term employee benefits	**6,548**	7,416	5,449
Dividends payable (see Note 21)	**18,129**	13,580	14,428
Unearned insurance premiums	**1,138**	1,325	1,343
Accounts payable and other	**17,967**	12,417	12,334
	$ 66,285	$ 58,363	$ 56,382

21. Share capital

Central 1 may issue an unlimited number of Class “A”, “B”, “C”, “D”, and “E” shares and may, at its option and with the approval of the Board of Directors, redeem its shares. There are no restrictions on the number of shares that may be held by a member shareholder. The holders of each class of share are entitled to receive dividends as declared from time to time. The Class “A”, “B”, “C”, and “D” shares have a par value of $1 per share, and the Class E shares have a par value of $0.01 per share and a redemption value of $100 per share.

The allocation of Class A shares is based on the assets of each credit union in proportion to the combined assets of the British Columbia credit union network and the Ontario credit union network. This allocation is adjusted periodically to reflect changes in credit union assets. On matters concerning Central 1’s role as a trade association, Class A members are entitled to one vote for every 100 of their members. Each Class B or C shareholder has one vote on certain issues.

Central 1 may issue an unlimited number of Class F shares and may redeem its shares at its option with the approval of the Board of Directors. The shares will be issued to Class A members in proportion to their share of mandatory deposits with Central 1. The holders of these shares are entitled to receive dividends as declared from time to time. The shares have a par value of $1 per share.

In the event of a liquidation, dissolution or winding-up of Central 1, the holders of Class F shares will be entitled to receive a pro rata distribution from the available property and assets of Central 1 contained in or designated by the Board of Directors to be a part of the Mandatory Liquidity Pool (MLP) together with all declared and unpaid dividends. Any surplus, after the distribution to the holders of Class F shares, shall be distributed rateably and proportionally among the holders of Class A, B, C, D, and E shares according to the number of shares held at that time. The amount paid to a member in respect of each Class E share held by that member shall not exceed $100 per Class E share.

The numbers of shares issued are as follows:

(Thousands of shares)	December 31, 2017	December 31, 2016	December 31, 2015
Class A – credit unions			
Balance at beginning of year	**416,952**	370,952	333,074
Issued during the year	**41,149**	46,000	38,000
Redeemed during the year	**(30,000)**	–	(122)
Balance at end of year	**428,101**	416,952	370,952
Class B – co-operatives			
Balance at beginning and end of year	**5**	5	5
Class C – other			
Balance at beginning and end of year	**7**	7	7
Class E – credit unions			
Balance at beginning of year	**3,157**	3,157	3,158
Redeemed during the year	**(106)**	–	(1)
Balance at end of year	**3,051**	3,157	3,157
Class E – treasury shares			
Balance at beginning of year	**–**	–	–
Reaquired during the year	**44**	–	–
Balance at end of year	**44**	–	–

The amounts outstanding are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Outstanding $1 par value shares						
Class A – credit unions	**$**	**428,101**	$	416,952	$	370,952
Class B – cooperatives		**5**		5		5
Class C – other		**7**		7		7
Outstanding $0.01 par value shares						
Class E – credit unions		**30**		32		32
	$	**428,143**	$	416,996	$	370,996

There were no Class F shares issued or outstanding as of December 31, 2017.

The dividend amounts are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Dividend payable, balance at beginning of year	**$**	**13,580**	$	14,428	$	22,448
Declared during the year		**23,129**		13,580		14,428
Paid during the year		**(18,580)**		(14,428)		(22,448)
Dividend payable, balance at end of year	**$**	**18,129**	$	13,580	$	14,428

22. Gain (loss) on disposal of financial instruments

The components of gain on disposal of financial instruments are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Net gain (loss) on disposal of trading assets	**$**	**(21,323)**	$	19,955	$	33,188
Net gain on disposal of investment securities		**8,739**		5,773		16,639
Net loss on disposal of obligations under the CMB Program		**–**		(1,320)		(115)
Net loss on disposal of derivative instruments		**(20,744)**		(11,406)		(36,636)
Net loss on disposal of deposits		**(3,326)**		(5,778)		(4,344)
Net gain (loss) on disposal of obligations related to securities sold short		**2,024**		950		(6,621)
	$	**(34,630)**	$	8,174	$	2,111

Jump to table of contents

23. Change in fair value of financial instruments

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Trading assets	**$ (59,328)**	$ (45,879)	$ 8,645
Loans	**(294)**	379	–
Activities under the CMB Program			
Reinvestment assets	**(3,432)**	827	535
Derivative instruments	**3,379**	(542)	5,433
Obligations under the CMB Program	**17,712**	7,737	(10,650)
Derivative instruments	**22,139**	8,857	30,523
Financial liabilities at FVTPL			
Deposits designated as trading	**74,827**	39,873	(12,531)
Obligations related to securities sold short	**(117)**	495	854
	$ 54,886	$ 11,747	$ 22,809

24. Other income

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Mandatory Liquidity Pool	**$ (381)**	$ (32)	$ 8
Wholesale Financial Services			
Lending fees	**6,364**	5,630	4,690
Securitization fees	**7,380**	6,928	5,004
Foreign exchange income	**5,871**	6,041	5,892
Other	**7,365**	7,585	8,001
Digital & Payment Services			
Payment processing and other fees	**53,721**	53,002	50,613
Digital banking fees	**31,772**	30,509	28,837
Dues Funded Activities	**11,787**	12,009	13,414
Other			
Equity interest in affiliates	**14,409**	7,965	6,666
Income from investees	**3,741**	4,957	4,120
Litigation settlement	**1,135**	–	7,735
Other	**6,725**	5,905	5,726
	$ 149,889	$ 140,499	$ 140,706

During 2015, an agreement was reached to settle a legal action brought by Central 1 and other claimants. Central 1 received $1.1 million as the final settlement of this litigation in 2017.

25. Other administrative expenses

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Cost of sales and services	$	**13,893**	$	13,918	$	15,326
Cost of payments processing		**17,613**		15,541		15,341
Management information systems		**13,925**		9,500		6,913
Professional fees		**22,671**		10,455		5,433
Membership dues		**6,292**		5,535		5,001
Business development projects		**1,156**		1,603		1,246
Other		**3,710**		3,570		3,712
	$	**79,260**	$	60,122	$	52,972

26. Provision for income taxes

Income taxes reported in the Consolidated Financial Statements are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Provision for income taxes in the Consolidated Statements of Profit	$	**10,321**	$	9,305	$	8.963
Income tax benefit related to dividends accrued and reacquisition of Class E shares		**(6,635)**		(2,507)		(2,387)
	$	**3,686**	$	6,798	$	6,576

Components of income taxes recognized in the Consolidated Statements of Profit are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Current income taxes	$	**7,612**	$	378	$	10,072
Deferred income taxes (recoveries)		**2,709**		8,927		(1,109)
	$	**10,321**	$	9,305	$	8,963

Central 1's effective tax rate differs from the amount that would be computed by applying the federal and provincial statutory rates of 26.1% (December 31, 2016 - 26.1%, December 31, 2015 - 26.1%).

The federal deduction available to credit unions which provides access to a lower income tax rate for income that is not eligible for the small business deduction has been phased out completely in 2017. The impact of phasing out the deduction will be partially mitigated by the availability of a general rate reduction. The B.C. credit union deduction has been fully re-established in October 2017 and is effective for 2017.

Jump to table of contents

	December 31, 2017	December 31, 2016	December 31, 2015
	%	%	%
Combined federal and provincial statutory income tax rates	**26.1**	26.1	26.1
Credit union deduction	**(8.7)**	(7.6)	(9.8)
Tax credits	**–**	(1.5)	(0.5)
Rate differential on equity interests in affiliates	**(2.9)**	(1.9)	(1.3)
Change in estimated future tax rates on deferred tax balances	**(0.3)**	(0.7)	–
Other	**3.3**	(0.4)	0.1
Total	**17.5**	14.0	14.6

27. Post-employment benefits

Central 1 provides various registered retirement plans for employees including defined benefit plans and defined contribution plans. A non-registered supplemental pension plan is also provided to eligible employees whose registered pension plan benefits are limited by the Income Tax Act. In addition to providing retirement plans, Central 1 also funds a non-pension retiree benefits plan for eligible employees.

(a) Defined benefit plans

Subject to eligibility requirements, employees of Central 1 may be eligible to participate in one of the following defined benefit plans.

- The defined benefit plan under the B.C. Credit Union Employees' Pension Plan, which is a multi-employer plan governed by a Board of Trustees; and
- The single-employer defined benefit plan administered by Central 1 for certain Ontario-based employees.

The defined benefit pension plans are contributory and provide pension benefits based on the employee's years of service and average earnings for a limited period prior to retirement. The plan is a multi-employer contributory defined benefit pension plan governed by a 12-member Board of Trustees. The Board of Trustees is responsible for overseeing the management of the plan, including investment of the assets and administration of the benefits. Central 1 is one of several employers participating in the 1.75% Division of the B.C. Credit Union Employees' Pension Plan.

Every three years, an actuarial valuation is performed to assess the financial position of the multi-employer plan, the adequacy of the funding level, and to determine the present value of accrued pension benefits and recommended plan contributions based on projections of the employees' average compensation levels at retirement. The most recent actuarial valuation for the multi-employer plan, which was conducted as at December 31, 2015, indicated a going concern unfunded liability in the 1.75% Division of $25.1 million (December 31, 2012 - $32.3 million) and a solvency deficiency of $123.0 million (December 31, 2012 - $129.9 million). The deficit is targeted to be financed over time through increased contributions. The recommended minimum required employer contributions to the 1.75% Division has increased from 14.8% as of October 1, 2013 to 15.05% starting from January 1, 2017.

As this is a multi-employer plan, the assets and liabilities are pooled and the actuary does not determine an individual employer's own unfunded liability. It is not possible to determine the portion of the deficit related to Central 1.

The next actuarial valuation for the multi-employer plan should be performed no later than as at December 31, 2018 with results available in 2019.

The defined benefit pension option under the B.C. Credit Union Employees' Pension Plan is subject to the provisions under Pension Benefits Standards Act (the Act) regulated by Financial Institution Commission of British Columbia (FICOM). The Act prescribes that, with respect to a solvency deficiency, amortization payments must be made over a period not exceeding five years from the review date that established the solvency deficiency.

On October 24, 2016, FICOM amended its regulations to implement two new solvency funding relief measures for pension plans with a defined benefit component:

- Solvency deficiency payments may be made over a ten-year period commencing on the review date, rather than the regular five-year amortization period.
- All existing solvency deficiencies may be consolidated into one new solvency deficiency as at the review date.

The single-employer plan is registered under the Ontario Pension Benefits Act and administered by Central 1 which is responsible over matters affecting the benefit entitlements earned by plan members and beneficiaries. As at December 31, 2016, the actuary reported that the single-employer plan had an excess of plan assets over actuarial liabilities for accrued pension benefits of $3.9 million. The solvency valuation indicated that the value of assets exceeds the actuarial liabilities by $1.6 million. Since both the going-concern excess surplus and the solvency surplus exceed the estimated employer normal cost contributions payable, Central 1 is prohibited from making contributions under the defined benefit component under the defined benefit component until the date of the next valuation. The next actuarial valuation is expected to be performed no later than as at December 31, 2019.

Details of the single-employer defined benefit plan, as determined by the plan actuary as at year-end are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Defined benefit obligation	**$**	**(13,914)**	$	(13,423)	$	(12,799)
Fair value of plan assets		**16,999**		16,047		16,105
Net defined benefit asset	**$**	**3,085**	$	2,624	$	3,306
Defined benefit obligation						
Defined benefit obligation, beginning of year	**$**	**(13,423)**	$	(12,799)	$	(11,805)
Current service costs		**(176)**		(179)		(198)
Employee contributions		**(55)**		(60)		(68)
Interest cost on accrued benefit obligation		**(501)**		(510)		(472)
Past service cost (including curtailment)		**–**		–		(814)
Benefit payments		**599**		555		558
Actuarial loss		**(358)**		(430)		–
Defined benefit obligation, end of year	**$**	**(13,914)**	$	(13,423)	$	(12,799)
Fair value of plan assets						
Plan assets, beginning of year	**$**	**16,047**	$	16,105	$	15,091
Employee contributions		**55**		60		68
Interest income on plan assets		**592**		634		594
Excess (shortfall) of actual returns on plan assets, excluding interest income		**969**		(148)		961
Benefit payments		**(599)**		(555)		(558)
Administration costs (other than costs from managing plan assets)		**(65)**		(49)		(51)
Plan assets, end of year	**$**	**16,999**	$	16,047	$	16,105
Expense recognized in profit or loss						
Current service costs	**$**	**176**	$	179	$	198
Administration costs (other than costs from managing plan assets)		**65**		49		51
Past service cost (including curtailment)		**–**		–		814
Interest cost on accrued benefit obligation		**501**		510		472
Interest income on plan assets		**(592)**		(634)		(594)
	$	**150**	$	104	$	941

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Amounts recognized in other comprehensive income (OCI)			
Actuarial gain (loss) on defined benefit obligation	$ (358)	$ (430)	$ –
Actuarial gain (loss) on plan assets	969	(148)	961
	$ 611	$ (578)	$ 961
Actuarial assumptions used to determine defined benefit expense:			
Weighted average discount rate on benefit obligation	3.75%	4.00%	4.00%
Weighted average salary escalation	2.85%	3.00%	3.00%
Expected return on plan assets	3.50%	3.75%	4.00%
Actuarial assumptions used to determine accumulated benefit obligation:			
Weighted average discount rate on benefit obligation	3.50%	3.75%	4.00%
Weighted average salary escalation	2.85%	3.00%	3.00%
Expected return on plan assets	3.75%	3.75%	4.00%

Sensitivity of assumptions

Key economic assumptions used in measuring the accumulated benefit obligations and related expenses for the defined benefit option are outlined in the table below. The sensitivity analysis provided is hypothetical as changes in assumptions may not be linear and the sensitivities in each key variable have been calculated independently of the other key variables.

(Thousands of dollars)	Accumulated benefit obligation	2017 expense
Assumed discount rate		
Impact of 1% increase	$ 1,675	$ 20
Impact of 1% decrease	$ (2,070)	$ (20)
Weighted average salary escalation		
Impact of 1% increase	$ (377)	$ 28
Impact of 1% decrease	$ 334	$ (25)

(b) Defined contribution plans

Subject to eligibility requirements, employees of Central 1 may be eligible to participate in one of the following defined contribution plans.

- The money purchase option under the B.C. Credit Union Employees' Pension Plan, which is a multi-employer plan governed by a Board of Trustees;
- The single-employer money purchase option administered by Central 1 operated for Ontario employees; and
- The group registered retirement savings plan under the B.C. Central 1 Retirement Savings Plan (group RRSP).

Contributions for defined contribution plan and expense for group RRSP included in the Consolidated Statements of Profit were $2.4 million (December 31, 2016 - $2.2 million; December 31, 2015 - $2.0 million).

(c) Retiree non-pension benefits

In addition to the base retirement plans, Central 1 provides post-retirement benefits consisting of extended health, Medical Services Plan, dental and life insurance premiums to employees that qualify.

Details of the unfunded non-pension retirement benefit program, as determined by the program actuary as at year-end, are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Defined benefit obligation	**$**	**(17,413)**	$	(18,397)	$	(17,369)
Net defined benefit liability	**$**	**(17,413)**	$	(18,397)	$	(17,369)
Defined benefit obligation						
Defined benefit obligation, beginning of year	**$**	**(18,397)**	$	(17,369)	$	(18,990)
Current service costs		**(294)**		(329)		(533)
Interest cost on accrued benefit obligation		**(732)**		(695)		(740)
Benefit payments		**544**		418		381
Actuarial liability experience gain (loss)		**2,657**		(398)		2,530
Actuarial liability financial assumptions loss		**(1,191)**		(24)		(17)
Defined benefit obligation, end of year	**$**	**(17,413)**	$	(18,397)	$	(17,369)
Expense recognized in profit or loss						
Current service costs	**$**	**294**	$	329	$	533
Interest cost on accrued benefit obligation		**732**		695		740
	$	**1,026**	$	1,024	$	1,273
Amounts recognized in OCI						
Actuarial gain (loss) on defined benefit obligation	**$**	**1,466**	$	(422)	$	2,513
Actuarial assumptions used to determine retiree non-pension benefit expense:						
Weighted average discount rate on benefit obligation		**3.50%**		4.00%		4.00%
Actuarial assumptions used to determine accumulated benefit obligation:						
Weighted average discount rate on benefit obligation		**3.50%**		4.00%		4.00%
Health care cost trend assumptions:						
Health care cost trend rate on benefit obligation		**8.00%**		8.00%		8.00%
Ultimate trend rate on benefit obligation		**5.00%**		5.00%		5.00%
Year that the rate reaches the ultimate trend rate		**2024**		2023		2022

Jump to table of contents

Sensitivity of assumptions

Key economic assumptions used in measuring the accumulated benefit obligations and related expenses for non-pension retiree benefits are outlined in the table below. The sensitivity analysis provided is hypothetical as changes in assumptions may not be linear and the sensitivities in each key variable have been calculated independently of the other key variables.

(Thousands of dollars)	Accumulated benefit obligation	2017 expense
Assumed discount rate		
Impact of 1% increase	$ (1,883)	$ 12
Impact of 1% decrease	$ 2,402	$ (15)
Assumed overall health care cost trend rate		
Impact of 1% increase	$ (253)	$ 5
Impact of 1% decrease	$ 222	$ (10)

(d) Non-registered supplemental pension plan

Central 1 also offers supplemental pension retirement benefits to employees who qualify.

Details of the unfunded supplemental pension plan, as determined by the plan actuary as at year-end, are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Defined benefit obligation	$ (5,273)	$ (5,362)	$ (5,560)
Fair value of plan assets	183	134	101
Net defined benefit liability	$ (5,090)	$ (5,228)	$ (5,459)
Defined benefit obligation			
Defined benefit obligation, beginning of year	$ (5,362)	$ (5,560)	$ (6,769)
Current service costs	(77)	(92)	(149)
Interest cost on accrued benefit obligation	(206)	(213)	(241)
Benefit payments	561	605	550
Actuarial gain (loss)	(189)	(102)	1,049
Defined benefit obligation, end of year	$ (5,273)	$ (5,362)	$ (5,560)
Expense recognized in profit or loss			
Current service costs	$ 77	$ 92	$ 149
Interest cost on accrued benefit obligation	206	213	241
	$ 283	$ 305	$ 390
Amounts recognized in OCI			
Actuarial gain (loss) on defined benefit obligation	$ (189)	$ (102)	$ 437
Prior year adjustment	–	–	612
	$ (189)	$ (102)	$ 1,049

Jump to table of contents

Actuarial assumptions used to determine retiree non-pension benefit expense:			
Weighted average salary escalation	**3.00%**	3.00%	3.00%
Weighted average discount rate on benefit obligation	**3.50%**	4.00%	4.00%
Actuarial assumptions used to determine accumulated benefit obligation:			
Weighted average salary escalation	**3.00%**	3.00%	3.00%
Weighted average discount rate on benefit obligation	**3.50%**	4.00%	4.00%

Sensitivity of assumptions

(Thousands of dollars)	Accumulated benefit obligation
Assumed discount rate	
Impact of 1% increase	$ **(445)**
Impact of 1% decrease	$ **537**

(e) Risks

The defined benefit plans and other post-employment plans expose Central 1 to a number of risks. The pension obligation is mainly impacted by the changes to the discount rate, longevity of plan members and future inflation levels. The pension plan assets are subject to market risk resulting from changes in interest rate, foreign exchange rates and credit and swap spreads.

28. Segment information

For management reporting purposes, Central 1's operations and activities are organized around three key business segments: MLP, Wholesale Financial Services (WFS), and Digital & Payment Services. In addition, Central 1 offers a variety of additional services that are funded by membership dues. All other activities or transactions are reported in "Other".

A description of each business segment is as follows:

Mandatory Liquidity Pool

The MLP is responsible for providing extraordinary liquidity to the credit union networks in the event of a liquidity crisis. The MLP is funded by the mandatory deposits of, and associated capital from, member credit unions, either by liquidity lock-in agreement or by statute. Central 1 manages the MLP within the regulatory constraints and leverages its economies of scale to reduce costs associated with the MLP. Assets held in the MLP remain highly liquid in order to ensure immediate access to funds. Members receive interest on their deposits and dividends on Class A shares which in aggregate equals to the return on the liquidity portfolio after expenses.

Wholesale Financial Services

WFS supports the structural and tactical liquidity needs of member credit unions in pursuit of regular, day-to-day business objectives. The segment is funded by Class A members' non-mandatory deposits augmented by capital market funding and deposits from non-Class A members.

WFS fosters the credit union network's growth through supporting the financial needs of member credit unions. Many of the products and services that this business segment provides, including credit union lending and access to securitization vehicles, allows members to take advantage of Central 1's strong financial ratings, industry expertise and access to the capital markets for short-term and long-term funding. WFS also supports the short-term liquidity requirement for the Digital & Payment Services segment. Central 1 provides foreign exchange services, derivative capabilities and other ancillary treasury services under the WFS segment.

The WFS segment includes the Group Clearer settlement operations function as Central 1 is a Group Clearer under the rules of Payments Canada, a Large Value Transfer System (LVTS) participant, and acts as the credit union networks' financial institution connection to the Canadian payments system.

With a focus on expanding our markets, solidifying our funding and providing holistic and proactive solutions to our members and clients, Central 1 reorganized its Trade Services functions in September 2017 and moved a number of functions into WFS, including risk solutions and product compliance & design. Comparative information has been restated to reflect this change.

Digital & Payment Services

Digital & Payment Services develops and operates innovative digital banking technologies and payment processing transactions for member credit unions, financial institutions and other corporate clients. This segment offers *MemberDirect*® services, a multi-platform solution that allows member credit unions to offer a variety of digital banking services to their individual customers through their online banking platform. The products and services offered through *MemberDirect*® help credit unions attract new members, deepen their relationships with existing members and support them in delivering high quality member services.

Payments operations encompass processing paper items and electronic transactions such as automated funds transfer and bill payments on behalf of member credit unions. The payment processing solutions under the *PaymentStream*™ brand are secure and reliable tools that allow financial and corporate-sector clients to complete a variety of digital, paper and remittance transactions. They also provide cash management services, including automated funds transfers, bill payments and wire transfers.

Dues Funded Activities

As a trade association, Central 1's services to its members include operational support, marketing, economics, market research and creative services, communications, strategic and people solutions tailored to the needs of member credit unions. These value-added services give member credit unions access to a wealth of expertise, while remaining affordable through economies of scale.

Other

Other segment comprises enterprise level activities which are not allocated to the three core business segments and dues funded activities, including the costs of implementing strategic initiatives and exploring strategic alternatives to enhance the ability to support credit unions in the future. The costs of Corporate Support functions are also included in Other and are attributed to business lines as appropriate. Central 1's investments in equity shares of network-related entities other than the wholly owned subsidiaries as described in Note 35, together with consolidation adjustments, corporate level tax items and other assets and liabilities not allocated to the three core business segments and dues funded activities, are also included in the Other segment.

Management reporting framework

Central 1's management reporting framework is intended to measure the performance of each business segment as if it were a stand-alone business and reflects the way the business segments are managed. This approach is intended to ensure that the business segments' results reflect all relevant revenue and expenses associated with the conduct of their businesses. Management regularly monitors these segments' results for the purpose of making decisions about resource allocation and performance assessment. These items do not impact the consolidated results.

The expenses in each business segment may include cost of services incurred directly as well as attributed corporate costs. For costs not directly attributable to one of the business segments, a management reporting framework that uses assumptions, estimates and judgements for allocating overhead costs and indirect expenses to each of the business segments is used. The management reporting framework assists in the attribution of capital and the transfer pricing of funds to the business segments in a manner that fairly and consistently measures and aligns the economic costs with the underlying benefits and risks of that specific business segment. Central 1's capital plan allows for tactical capital allocations within all segments. Central 1 does not have any inter-segment revenue between business segments. Income tax provision or recovery is generally applied to each segment based on a statutory tax rate and may be adjusted for items and activities unique to each segment. All other corporate level activities that are not allocated to the three core business segments and dues funded activities are reported under the Other segment.

Basis of presentation

The accounting policies used to prepare these segments are consistent with those followed in the preparation of Central 1's Consolidated Financial Statements as described in Note 3.

Periodically, certain business lines and units are transferred among business segments to closely align Central 1's organizational structure with its strategic priorities. Results for prior periods are restated to conform to the current period presentation.

Results by segment

The following table summarizes the segment results for the year ended December 31, 2017:

(Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including recovery of credit losses	$ 26,555	$ 51,536	$ (292)	$ –	$ (4,234)	$ 73,565
Other income	(381)	26,980	85,493	11,787	26,010	149,889
Net financial and other income	26,174	78,516	85,201	11,787	21,776	223,454
Operating expenses	8,045	25,971	84,763	11,240	34,470	164,489
Profit (loss) before income taxes	18,129	52,545	438	547	(12,694)	58,965
Income taxes (recoveries)	3,154	10,006	71	88	(2,998)	10,321
Profit (loss) for the period	**$ 14,975**	**$ 42,539**	**$ 367**	**$ 459**	**$ (9,696)**	**$ 48,644**
Total assets at December 31, 2017	$ 8,600,303	$ 9,178,135	$ 21,496	$ –	$ 268,966	$ 18,068,900
Total liabilities at December 31, 2017	$ 8,078,455	$ 8,731,281	$ (1,108)	$ (459)	$ 141,610	$ 16,949,779
Total equity attributable to members of Central 1 at December 31, 2017	$ 521,848	$ 436,766	$ 22,604	$ 459	$ 127,356	$ 1,109,033
Non-controlling interest at December 31, 2017	–	10,088	–	–	–	10,088
Total equity at December 31, 2017	$ 521,848	$ 446,854	$ 22,604	$ 459	$ 127,356	$ 1,119,121

The following table summarizes the segment results for the year ended December 31, 2016:

(Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including recovery of credit losses	$ 21,159	$ 50,719	$ (255)	$ –	$ (4,180)	$ 67,443
Other income	(32)	26,184	83,511	12,010	18,826	140,499
Net financial and other income	21,127	76,903	83,256	12,010	14,646	207,942
Operating expenses	7,547	25,586	74,452	12,396	21,616	141,597
Profit (loss) before income taxes	13,580	51,317	8,804	(386)	(6,970)	66,345
Income taxes (recoveries)	2,507	9,465	1,625	(71)	(4,221)	9,305
Profit (loss) for the period	$ 11,073	$ 41,852	$ 7,179	$ (315)	$ (2,749)	$ 57,040
Total assets at December 31, 2016	$ 8,251,282	$ 8,817,909	$ 10,480	$ –	$ 234,348	$ 17,314,019
Total liabilities at December 31, 2016	$ 7,746,384	$ 8,327,314	$ (11,758)	$ 315	$ 166,889	$ 16,229,144
Total equity attributable to members of Central 1 at December 31, 2016	$ 504,898	$ 480,552	$ 22,238	$ (315)	$ 67,459	$ 1,074,832
Non-controlling interest at December 31, 2016	–	10,043	–	–	–	10,043
Total equity at December 31, 2016	$ 504,898	$ 490,595	$ 22,238	$ (315)	$ 67,459	$ 1,084,875

The following table summarizes the segment results for the year ended December 31, 2015:

(Thousands of dollars)	Mandatory Liquidity Pool	Wholesale Financial Services	Digital & Payment Services	Dues Funded Activities	Other	Total
Net financial income (expense), including recovery of credit losses	$ 21,405	$ 33,311	$ (242)	$ –	$ (4,320)	$ 50,154
Other income	8	23,587	79,450	13,414	24,247	140,706
Net financial and other income	21,413	56,898	79,208	13,414	19,927	190,860
Operating expenses	6,985	25,098	70,320	13,778	13,366	129,547
Profit (loss) before income taxes	14,428	31,800	8,888	(364)	6,561	61,313
Income taxes (recoveries)	2,365	5,212	1,563	(60)	(117)	8,963
Profit (loss) for the period	$ 12,063	$ 26,588	$ 7,325	$ (304)	$ 6,678	$ 52,350
Total assets at December 31, 2015	$ 7,536,163	$ 7,182,102	$ 2,208	$ –	$ 228,545	$ 14,949,018
Total liabilities at December 31, 2015	$ 7,081,608	$ 6,719,827	$ (42,136)	$ 304	$ 200,395	$ 13,959,998
Total equity attributable to members of Central 1 at December 31, 2015	$ 454,555	$ 452,316	$ 44,344	$ (304)	$ 28,150	$ 979,061
Non-controlling interest at December 31, 2015	–	9,959	–	–	–	9,959
Total equity at December 31, 2015	$ 454,555	$ 462,275	$ 44,344	$ (304)	$ 28,150	$ 989,020

29. Guarantees, commitments and contingencies

Central 1 is a Group Clearer under the rules of Payments Canada and acts as the credit union networks' financial institution connection to the Canadian payments system. Pursuant to a joint venture agreement, Central 1 provides payment services to the credit union centrals of Alberta, Manitoba, and Saskatchewan (collectively, the Prairie Centrals). Central 1 guarantees payment of items drawn on or payable by the Prairie Centrals and their member credit unions. Each of the Prairie Centrals in return provides Central 1 with a guarantee for those payments.

In the normal course of business, Central 1 enters into various off-balance sheet credit instruments to meet the financing, credit and liquidity requirements of its member credit unions. These are in the form of commitments to extend credit, guarantees, standby letters of credit, and mortgage purchase commitment.

The table below presents the maximum amount of credit that Central 1 could be required to extend if commitments were to be fully utilized, and the maximum amount of guarantees that could be in effect if the maximum authorized amount were transacted.

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Commitments to extend credit	**$ 4,327,871**	$ 4,447,323	$ 3,857,075
Guarantees			
Financial guarantees	**$ 367,500**	$ 390,000	$ 347,000
Performance guarantees	**$ 810,000**	$ 440,000	$ 340,000
Standby letters of credit	**$ 187,910**	$ 173,502	$ 145,392
Mortgage purchase commitment	**$ –**	$ –	$ 16,066
Future prepayment swap reinvestment commitment	**$ 770,314**	$ 431,516	$ –

Amounts utilized under these agreements representing off-balance sheet amounts for commitments to extend credit, guarantees, and standby letter of credit, were $17.4 million, $455.3 million and $102.8 million, respectively, as at December 31, 2017 (December 31, 2016 - $13.5 million, $273.1 million and $103.0 million; December 31, 2015 - $29.6 million, $313.5 million and $86.7 million).

Central 1 is also involved in legal actions in the ordinary course of business, in which the likelihood of a loss and amount of loss, if any, is not readily determinable.

In September 2016, Central 1 has made a commitment to support the capital call from CFI, an affiliate of Central 1 as disclosed in Note 35. This commitment requires Central 1 to subscribe for additional Class B shares of CFI, which will require Central 1 to contribute up to $4.7 million to be funded over the next three years, of which $1.8 million was contributed in January 2017. Central 1 has also committed to contribute up to $2.4 million to The CUMIS Group Ltd. (CUMIS), another affiliate of Central 1 as disclosed in Note 35. This contribution represents Central 1's share of CUMIS subscription in Class A shares of CFI over a period of three years. As at December 31, 2017, Central 1 had not received any request from CUMIS and CFI to make such contribution.

Pledged assets

In the normal course of business, Central 1 pledges securities and other assets as collateral. A breakdown of encumbered assets pledged as collateral is provided in the following table. These transactions are conducted in accordance with standards terms and conditions for such transactions.

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Assets pledged to Bank of Canada & Direct Clearing Organizations[(1) (2)]	**$ 57,206**	$ 54,122	$ 56,653
Assets pledged in relation to:			
Derivative financial instrument transactions	**19,828**	9,109	17,787
Securities lending	**10,496**	35,552	100,759
Obligations under the CMB Program	**604,105**	851,456	824,951
Reinvestment assets under the CMB Program	**545,247**	360,570	165,146
Securities under repurchase agreements	**500,472**	298,416	221,174
	$ 1,737,354	$ 1,609,225	$ 1,386,470

[1]Includes assets pledged as collateral for LVTS activities.
[2]Central 1 also acts as a Group Clearer on behalf of certain other credit union centrals. These centrals are required to pledge securities in respect of their LVTS settlements. Central 1 administers the collateral on their behalf.

30. Commitments under leasing agreements

Central 1 as lessee - finance leases

Finance leases relate to computer equipment with lease terms of 36 months. Central 1 has options to purchase the equipment for a nominal amount upon completion of an optional 13-month lease extension. Central 1 has the right to return leased assets at the conclusion of the lease term or continue to rent them at the same monthly rate on a month-to-month basis. Central 1's obligations under finance leases are secured by the lessor's title to the leased assets.

Jump to table of contents

Future minimum lease payments are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Due within one year	**$ 837**	$ 702	$ 581
Due after one year and within three years	**770**	631	520
	$ 1,607	$ 1,333	$ 1,101

Central 1 as lessor - operating leases

Central 1 leases office premises in two locations. Future minimum operating lease commitments are as follows:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Due within one year	**$ 1,049**	$ 994	$ 975
Due after one year and within five years	**3,509**	3,438	3,639
Due after five years	**1,420**	2,130	2,799
	$ 5,978	$ 6,562	$ 7,413

Total lease payments charged to profit for the year was $0.9 million (December 31, 2016 - $0.8 million; December 31, 2015 - $0.8 million).

31. Financial instruments – Fair value

Certain financial instruments are recognized in the Consolidated Statements of Financial Position at fair value. These include derivative instruments, trading assets, investment securities, deposits designated as trading, a portfolio of commercial loans and instruments held under the CMB Program. The fair value is the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants which takes place in the principal (or most advantageous) market at the measurement date under current market conditions. The fair value of financial instruments is best evidenced by unadjusted quoted prices in active markets. When there is no quoted price in an active market, valuation techniques which maximize the use of relevant observable inputs and minimize the use of unobservable inputs are used to derive the fair value.

Financial instruments are recorded at fair value upon initial recognition, which is normally equal to the fair value of the consideration given or received. Where financial instruments are measured at fair value subsequent to initial recognition, fair value is determined as described above. The use of valuation techniques to determine the fair value of a financial instrument requires management to make assumptions such as the amount and timing of future cash flows, discount rates, and use of appropriate benchmarks and spreads.

Financial instruments whose carrying value approximate fair value

Fair value is assumed to be equal to the carrying value for cash, loans due on demand classified as loans and receivables and deposits due on demand classified as other financial liabilities because of their short-term nature.

Financial instruments for which fair value is determined using valuation techniques

The fair value of fixed rate performing loans is determined by discounting contractual cash flows at market interest rates. For both loans to and deposits with members, Central 1 discounts the expected cash flows using interest rates currently being offered on instruments with similar terms. The fair values of debt securities issued and subordinated debt are determined by discounting remaining cash flows by reference to current market yields on similar instruments.

Jump to table of contents

Fair value of assets and liabilities classified using the fair value hierarchy

Central 1 measures fair value using the following hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1: Inputs that are quoted market price (unadjusted) in an active market for an identical instrument.

Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly. This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3: Inputs that are unobservable. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instruments' valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect the differences between the instruments.

Transfers into and out of Levels 1, 2, and 3 occur when there are changes to the relevant inputs which are consistent with the characteristics of the asset or liability. Transfers are recognized at the end of the reporting period.

The following tables present the fair value of Central 1's assets and liabilities classified in accordance with the fair value hierarchy:

(Millions of dollars) December 31, 2017	Level 1	Level 2	Level 3	Amounts at Fair Value	Amounts at Amortized Cost[1]	Total Carrying Value
Financial assets						
Cash	$ –	$ –	$ –	$ –	$ 550.8	$ 550.8
Deposits with regulated financial institutions	–	–	–	–	6.0	6.0
Trading assets	–	8,889.7	–	8,889.7	–	8,889.7
Reinvestment assets under the CMB Program	–	545.0	–	545.0	0.2	545.2
Derivative assets	–	101.8	–	101.8	–	101.8
Loans	–	–	11.4	11.4	2,150.7	2,162.1
Investment securities	–	5,476.2	9.9	5,486.1	32.1	5,518.2
Total financial assets	**$ –**	**$ 15,012.7**	**$ 21.3**	**$ 15,034.0**	**$ 2,739.8**	**$ 17,773.8**
Financial liabilities						
Deposits designated as trading	$ –	$ 8,561.5	$ –	$ 8,561.5	$ –	$ 8,561.5
Obligations related to securities sold short	–	95.5	–	95.5	–	95.5
Derivative liabilities	–	83.9	–	83.9	–	83.9
Debt securities issued	–	–	–	–	2,178.7	2,178.7
Deposits	–	–	–	–	3,436.9	3,436.9
Obligations under the CMB Program	–	1,190.1	–	1,190.1	–	1,190.1
Subordinated liabilities	–	–	–	–	421.8	421.8
Securities under repurchase agreements	–	–	–	–	500.5	500.5
Total financial liabilities	**$ –**	**$ 9,931.0**	**$ –**	**$ 9,931.0**	**$ 6,537.9**	**$ 16,468.9**

[1] *Amounts carried at amortized cost include financial instruments classified as loans and receivables or other financial liabilities.*

There were no transfers of financial instruments between the different levels of the fair value hierarchy during the year ended December 31, 2017.

(Millions of dollars) December 31, 2016	Level 1	Level 2	Level 3	Amounts at Fair Value	Amounts at Amortized Cost[1]	Total Carrying Value
Financial assets	$ –	$ 14,794.2	$ 22.0	$ 14,816.2	$ 1,966.8	$ 16,783.0
Financial liabilities	$ –	$ 10,055.4	$ -	$ 10,055.4	$ 5,461.0	$ 15,516.4

(Millions of dollars) December 31, 2015	Level 1	Level 2	Level 3	Amounts at Fair Value	Amounts at Amortized Cost[1]	Total Carrying Value
Financial assets	$ –	$ 12,686.0	$ 9.3	$ 12,695.3	$ 1,635.8	$ 14,331.1
Financial liabilities	$ –	$ 8,696.6	$ –	$ 8,696.6	$ 4,764.7	$ 13,461.3

The following tables present the change in fair value for financial instruments included in Level 3 of the fair value hierarchy:

(Millions of dollars)	Fair Value at December 31, 2016	Purchases	Disposals	Transfers	Changes in fair value of assets in profit or loss	Fair Value at December 31, 2017
Equity shares	$ 9.9	$ –	$ –	$ –	$ –	**$ 9.9**
Loans	12.1	–	(0.3)	–	(0.4)	**11.4**
Total financial assets	$ 22.0	$ –	$ (0.3)	$ –	$ (0.4)	**$ 21.3**

(Millions of dollars)	Fair Value at December 31, 2015	Purchases	Disposals	Transfers	Changes in fair value of assets in profit or loss	Fair Value at December 31, 2016
Equity shares	$ 9.3	$ 2.3	$ (1.7)	$ –	$ –	$ 9.9
Loans	–	59.6	(47.3)	–	(0.2)	12.1
Total financial assets	$ 9.3	$ 61.9	$ (49.0)	$ –	$ (0.2)	$ 22.0

(Millions of dollars)	Fair Value at December 31, 2014	Purchases	Disposals	Transfers	Changes in fair value of assets in profit or loss	Fair Value at December 31, 2015
Equity shares	$ 9.2	$ –	$ –	$ –	$ 0.1	$ 9.3
Total financial assets	$ 9.2	$ –	$ –	$ –	$ 0.1	$ 9.3

Jump to table of contents

The following table sets out the fair values of on-balance sheet and derivative instruments of Central 1 using the valuation methods and assumptions described in Note 4. Fair values have not been attributed to assets and liabilities that are not considered financial instruments, such as property and equipment.

	Fair Value			Carrying Value			Unrealized Gain (Loss)		
(Millions of dollars)	December 31, 2017	December 31, 2016	December 31, 2015	December 31,2017	December 31, 2016	December 31, 2015	December 31, 2017	December 31, 2016	December 31, 2015
Assets									
Cash	**$ 550.8**	$ 487.1	$ 106.8	**$ 550.8**	$ 487.1	$ 106.8	**$ –**	$ –	$ –
Deposits with regulated financial institutions[1]	**6.0**	5.9	6.1	**6.0**	5.9	6.1	**–**	–	–
Trading assets and investment securities	**14,407.9**	14,393.9	12,445.7	**14,407.9**	14,393.9	12,445.7	**–**	–	–
Reinvestment assets under the CMB Program	**545.2**	360.6	165.1	**545.2**	360.6	165.1	**–**	–	–
Derivative assets	**101.8**	81.8	116.6	**101.8**	81.8	116.6	**–**	–	–
Loans[2]	**2,165.3**	1,455.8	1,491.1	**2,162.1**	1,453.8	1,490.8	**3.2**	2.0	0.3
Liabilities									
Deposits designated as trading	**8,561.5**	8,659.5	7,546.8	**8,561.5**	8,659.5	7,546.8	**–**	–	–
Obligations related to securities sold short	**95.5**	74.1	29.4	**95.5**	74.1	29.4	**–**	–	–
Derivative liabilities	**83.9**	85.7	130.8	**83.9**	85.7	130.8	**–**	–	–
Debt securities issued[1]	**2,176.0**	1,492.6	1,076.7	**2,178.7**	1,490.7	1,075.3	**2.7**	(1.9)	(1.4)
Deposits[1]	**3,445.0**	3,256.0	3,260.4	**3,436.9**	3,250.5	3,250.0	**(8.1)**	(5.5)	(10.4)
Obligations under the CMB Program	**1,190.1**	1,236.1	989.6	**1,190.1**	1,236.1	989.6	**–**	–	–
Subordinated liabilities[1]	**423.3**	421.8	221.4	**421.8**	421.4	218.2	**(1.5)**	(0.4)	(3.2)
Securities under repurchase agreements	**500.5**	298.4	221.2	**500.5**	298.4	221.2	**–**	–	–
Total							**$ (3.7)**	$ (5.8)	$ (14.7)

[1] *Where the carrying values are at cost, the fair value calculations for these instruments are based on Level 2 inputs.*
[2] *Where the carrying values are at cost, the fair value calculations for these instruments are based on Level 3 inputs.*

32. Financial instruments – Risk management

The nature of Central 1's holdings of financial instruments exposes Central 1 to credit and counterparty, liquidity and funding, and market risk.

(a) Credit and counterparty risk

Credit and counterparty risk is the risk of loss or opportunity cost resulting from the default or failure of a borrower, endorser, guarantor, or issuer to fulfil their financial obligations as they come due. Central 1 incurs credit and counterparty risk through loans, payment services, and the purchasing of credit instruments, and entering into contracts with counterparties in return for bilateral value-exchange of services. Central 1 has direct control over the types and amounts of credit and counterparty risk it accepts.

In managing credit and counterparty risk exposure, Central 1 establishes policies and procedures that include:

- application of safe and sound, stringent lending and/or funding criteria to all credit exposures prior to their acquisition;
- clearly defined management and policy limits on the amount, types, and concentrations of credit risk;
- regular evaluation and assessment of existing credit risk exposures and allowances; and
- continuous monitoring of credit exposures so as to promptly identify deteriorating situations and take appropriate action.

Information regarding Central 1's key exposure to credit and counterparty risk is provided in Notes 6 and 8.

(b) Liquidity and funding risk

Liquidity and funding risk is the risk for Central 1 to have the potential inability to meet cash flows obligations in a timely manner due to an inability to generate sufficient cash from assets or funding sources. Central 1 also provides liquidity support to the credit union network in British Columbia and Ontario and considers the liquidity and funding risks for each of its member credit unions as part of Central 1's risk. Sound liquidity management by Central 1 ensures the safety of credit union members' deposits and the health of the credit union network.

Central 1's liquidity management framework is designed to ensure that reliable and cost-effective funding sources are available to satisfy current and prospective commitments of Central 1 and its member credit unions. Diversification of funding sources provides flexibility and minimizes concentration risk. It is a crucial component of Central 1's overall liquidity management strategy.

Central 1 has established a comprehensive liquidity risk framework that is comprised of:

- a robust risk governance framework;
- investment strategies focused on maintaining sufficient unencumbered highly liquid assets to meet cash flow requirements in normal and stressed conditions;
- access to diversified funding sources – member deposits and capital markets;
- monitoring of credit union network liquidity, performance and financial health;
- an enterprise Contingency Funding Plan; and
- frequent measurement of portfolio liquidity.

Information regarding Central 1's high quality liquid securities is provided in Note 6. Information regarding Central 1's derivative liabilities, funding liabilities and off-balance sheet guarantees, commitments and contingencies is provided in Notes 7, 14, 15, 16, 17, and 29.

(c) Market risk

Market risk is the risk of loss resulting from unfavourable movements in interest rates, foreign exchange rates, and asset prices/yields. The level of market risk to which Central 1 is exposed varies depending on market conditions, future price and market movements and the composition of Central 1's investment, lending and derivative portfolios.

Central 1 manages its exposure to market risk through a range of governance and management processes. Central 1's policies detail the measurement of market risk and establish exposure limits in keeping with Central 1's overall risk appetite. Central 1 independently monitors exposure against limits, investigates any breaches and reports them at the appropriate level for review and action. This management framework is complemented by a series of rigorous stress test scenarios that are run on a regular basis.

Interest rate and credit spread risk

Central 1 regularly monitors its exposure to interest rate changes in order to assess their potential effects on financial margin. Central 1 Corporate Risk Management Policy defines exposure limits in relation to 1-day 99% Value at Risk (VaR). VaR provides a dollar estimate of loss due to 1-day movements in market risk factors at the 99% level. Interest rate VaR includes movements in sovereign and swap interest rate curves. Credit Spread VaR measures the loss associated with changes in credit spreads within the portfolio – CMB, Provincial, Bank and Corporate spreads. Central 1's exposure was largely due to potential movements in credit spreads, specifically widening credit spreads.

Foreign exchange rate risk

Central 1 has assets and liabilities denominated in several major currencies and buys foreign currencies from, and sells these currencies to its member credit unions. The risk associated with changing foreign currency values is managed by applying limits on the amounts (short or long positions) that can be maintained in the various currencies, and by utilizing derivative exchange contracts to lessen the impact of on-balance sheet positions and through VaR management limits.

Information regarding Central 1's exposure to foreign currency risk is provided in Note 33.

Contractual repricing or maturity dates of financial instruments

The majority of the obligations is incurred in Central 1's role as a liquidity manager and consists of member deposits or short- and long-term notes. Central 1 also has contractual obligations to CHT under the CMB Program. Deposits in the mandatory liquidity pool are either required to be renewed with Central 1 by regulation or contract or are anticipated to be re-deposited with Central 1.

The following table summarizes carrying amounts by the earlier of the contractual repricing or maturity dates for the following financial instruments:

(Millions of dollars)	Floating[1]	Within 3 Months	3 Months to 1 Year	1 Year to 5 Years	Over 5 Years	Not Rate Sensitive	Total
Assets							
Cash	$ 550.8	$ –	$ –	$ –	$ –	$ –	$ 550.8
Deposits with regulated financial institutions	–	–	3.4	2.5	–	0.1	6.0
Securities	–	314.1	1,928.1	12,016.3	85.0	64.4	14,407.9
Reinvestment assets under the CMB Program	–	60.2	138.9	270.6	–	75.5	545.2
Derivative assets	–	–	–	–	–	101.8	101.8
Loans	–	1,474.0	188.8	431.5	33.3	34.4	2,162.0
Other assets	–	–	–	–	–	295.2	295.2
Total	$ 550.8	$ 1,848.3	$ 2,259.2	$ 12,720.9	$ 118.3	$ 571.4	$ 18,068.9
Liabilities							
Deposits	$ 1,577.9	$ 1,868.4	$ 2,509.3	$ 6,071.7	$ 0.4	$ (29.3)	$ 11,998.4
Obligations related to securities sold short	–	–	–	95.5	–	–	95.5
Derivative liabilities	–	–	–	–	–	83.9	83.9
Debt securities issued	–	805.0	481.6	886.9	–	5.1	2,178.6
Obligations under the CMB Program	–	–	213.2	982.9	–	(6.0)	1,190.1
Subordinated liabilities	–	–	–	–	421.0	0.8	421.8
Securities under repurchase agreements	–	500.2	–	–	–	0.3	500.5
Other liabilities	–	–	–	–	–	481.0	481.0
Equity	–	–	–	–	–	1,119.1	1,119.1
Total	$ 1,577.9	$ 3,173.6	$ 3,204.1	$ 8,037.0	$ 421.4	$ 1,654.9	$ 18,068.9
On-balance sheet gap	(1,027.1)	(1,325.3)	(944.9)	4,683.9	(303.1)	(1,083.5)	–
Off-balance sheet gap	(1,421.6)	233.3	(23.7)	1,022.9	189.1	–	–
Total Gap – December 31, 2017	**$ (2,448.7)**	**$ (1,092.0)**	**$ (968.6)**	**$ 5,706.8**	**$ (114.0)**	**$ (1,083.5)**	**$ –**
Total Gap – December 31, 2016	$ (668.5)	$ (1,700.6)	$ (1,077.3)	$ 5,065.5	$ (428.4)	$ (1,190.7)	$ –
Total Gap – December 31, 2015	$ (1,146.1)	$ (60.1)	$ (1,667.0)	$ 3,539.2	$ 128.0	$ (794.0)	$ –

[1] *Represents those instruments whose interest rates change immediately with a change in an underlying interest rate basis. An example would be prime rate loans.*

Jump to table of contents

33. Financial instruments – Foreign currency exposure

Central 1 has various financial instruments denominated in foreign currencies. The details of Central 1's financial instruments, which are denominated in U.S. dollars, are as follows:

(Thousands of U.S. dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Assets			
Cash	**$ 48,124**	$ 26,597	$ 41,464
Securities	**790,392**	724,633	658,006
Loans	**663**	46	119
Derivative assets	**820**	1,361	2,499
Other	**50**	50	2,911
	$ 840,049	$ 752,687	$ 704,999
Liabilities			
Deposits	**$ 949,877**	$ 764,091	$ 701,022
Derivatives liabilities	**4,260**	4,116	4,071
Other	**2,685**	2,355	–
	956,822	770,562	705,093
On-balance sheet exposure	**(116,773)**	(17,875)	(94)
Off-balance sheet exposure	**133,888**	5,976	2,157
	$ 17,115	$ (11,899)	$ 2,063

Central 1 does not have significant exposure to other foreign currencies.

Jump to table of contents

34. Capital management

Central 1's Capital Policy ensures that each business segment has sufficient capital to support its business activities. The objective of managing capital is to optimize various pressures, including but not limited to the following:

- ensuring that regulatory capital adequacy requirements are met at all times;
- ensuring internal capital targets are not breached; and
- earning an appropriate risk adjusted rate of return on members' equity.

Capital management framework

The capital management framework provides the policies and processes for defining, measuring, and allocating all types of capital across Central 1. The process of attributing capital to business segments is linked to the budgeting process and to the Internal Capital Adequacy Assessment Process (ICAAP). The budget process establishes expected business activities over the course of the following fiscal year and the ICAAP establishes the required amount of capital based on an internal risk assessment. Central 1's capital plan allows for tactical capital allocations within all segments. Capital, other than that which is attributed to business segments, is held in the Other segment.

On April 28, 2017 Central 1's members approved changes to Central 1's capital structure and received regulatory approval by FICOM on December 5, 2017. The changes include the creation of a new class of shares, Class F shares, which will be the primary form of capital growth in the MLP segment. Credit unions will be required to subscribe to Class F shares based on the deposits they place in the MLP segment rather than their share of credit union network assets. For the details of the upcoming capital restructuring, refer to Note 36.

Regulatory capital

Central 1's capital levels are regulated under provincial regulations administered by FICOM. FICOM has also adopted the previous federal regulations administered by the Office of the Superintendent of Financial Institutions (OSFI). This regulation requires Central 1 to maintain a borrowing multiple, the ratio of deposit liabilities and other loans payable to total regulatory capital, of 20.0:1 or less.

FICOM requires Central 1 to maintain a federal borrowing multiple for each of the MLP and WFS segments. Effective August 16, 2017, FICOM amended the borrowing multiple requirements from no more than 16.0:1 to 17.0:1 for the MLP segment and from no more than 14.0:1 to 15.0:1 for the WFS segment.

In order to ensure that Central 1 maintains regulatory capital sufficient to absorb sudden increases in borrowings or a reduction in capital due to mark-to-market fluctuations, Central 1 sets targets for its operating borrowing multiples. Shortly after FICOM amended the regulatory requirements for MLP and WFS, Central 1 amended its targets from no more than 15.8:1 to 16.8:1 for the MLP segment and from no more than 13.0:1 to 14.0:1 for the WFS segment. This amendment of capital targets allowed Central 1 to return $50.0 million in capital to its Class A members. On September 29, 2017, Central 1 redeemed $30.0 million of Class A shares and paid $5.0 million dividends to Class A shareholders. On October 27, 2017, Central 1 reacquired $15.0 million of Class E shares.

Provincial regulations in B.C., which apply to B.C. credit unions as well as to Central 1, use a risk-weighted approach to capital adequacy that is based on standards issued by the Bank for International Settlements. The provincial risk weightings generally parallel the methodology used by the OSFI to regulate Canadian chartered banks. Provincial Legislation requires Central 1's total capital ratio, calculated by dividing regulatory capital by risk-weighted assets, to be no less than 8.0%. FICOM guidance requires Central 1's total capital ratio to be no less than 10.0%. Additionally, Central 1 must maintain a total capital ratio of at least 10.0% to enable member credit unions to risk-weight their deposits with Central 1 at 0.0%.

Central 1's capital base includes Tier 1 capital in the form of share capital, contributed surplus and retained earnings. Subject to certain conditions, Central 1 may include its subordinated debt in Tier 2B capital. In calculating Central 1's capital base, certain deductions are required for certain assets.

Central 1 was in compliance with all regulatory capital requirements throughout the years ended December 31, 2017, December 31, 2016 and December 31, 2015.

35. Related party disclosures

Related parties of Central 1 include:

- key management personnel and their close family members;
- Board of Directors and their close family members;
- entities over which Central 1 has control or significant influence; and
- Central 1's post-employment plans as described in Note 27.

Transactions with key management personnel

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of Central 1, which include Central 1's Executive Management and Vice-Presidents.

Transactions between Central 1 and key management personnel and their close family members are as follows:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Mortgage loans outstanding at end of year	**$**	**364**	$	377	$	389
Maximum mortgage loans outstanding during the year	**$**	**377**	$	389	$	692

As at December 31, 2017, the mortgage to key member of management personnel bears interest at the rate of 2.50% and is secured over properties of the borrower. No impairment losses have been recorded against this balance during the year ended December 31, 2017 (December 31, 2016 - $nil; December 31, 2015 - $nil).

The following table presents the compensation to key management personnel:

(Thousands of dollars)		December 31, 2017		December 31, 2016		December 31, 2015
Salaries and short-term employee benefits	**$**	**2,613**	$	2,980	$	3,129
Incentive		**1,217**		746		684
Post-employment benefits		**228**		242		301
Termination benefits		**1,279**		152		102
Other cash-based compensation		**–**		–		20
	$	**5,337**	$	4,120	$	4,236

In addition to their salaries, Central 1 also provides non-cash benefits to members of key management personnel and contributes to post-employment defined plans on their behalf.

Incentive compensation includes amounts paid in the current year reflecting achievement of performance objectives earned in the previous fiscal period.

Termination benefits represent amounts paid or payable, pursuant to contractual arrangements, to members of key management personnel who left or announced their intention to leave Central 1 during the period.

Other cash-based compensation includes relocation costs payable per contractual terms for certain executive officers.

Transactions with Board of Directors

The following table presents the aggregate remuneration received by Central 1's Board of Directors:

(Thousands of dollars)	December 31, 2017	December 31, 2016	December 31, 2015
Total remuneration	$ **737**	$ 628	$ 592

Significant subsidiaries

The following table presents Central 1's significant subsidiaries:

(% of direct ownership of common shares outstanding)	December 31, 2017	December 31, 2016	December 31, 2015
Central 1 Trust Company	**100%**	100%	100%
CUPP Services Ltd.	**100%**	100%	100%

Central 1's other subsidiaries represent less than 1.0% of Central 1's consolidated assets, revenue and profit before income taxes.

Transactions with subsidiaries are eliminated on consolidation and are not disclosed as related party transactions.

Investments in affiliates

Central 1 uses the equity method of accounting to record its interests in the following entities over which Central 1 has significant influence:

(% of direct ownership outstanding)	December 31, 2017	December 31, 2016	December 31, 2015
Credential Financial Inc.	**26%**	26%	26%
The CUMIS Group Limited	**27%**	27%	27%
Northwest & Ethical Investments L.P.	**26%**	26%	26%
189286 Canada Inc.	**52%**	52%	–%

Central 1 has indirect ownership of shares of certain affiliates through investments in other companies.

Substantial investments

Central 1 also has substantial investments in the following entities over which Central 1 does not have significant influence:

(% of direct ownership outstanding)	December 31, 2017	December 31, 2016	December 31, 2015
The Co-operators Group Limited	**21%**	21%	21%
Canadian Credit Union Association	**59%**	59%	–%

36. Proposed transactions

Aviso Wealth

In December 2017, Desjardins Financial Holding Inc. (Desjardins), CUMIS and Canada's five provincial credit union centrals (Centrals) including Central 1 entered into a master merger agreement to merge the businesses of Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. This transaction, when complete, will create one of Canada's largest independent wealth management firms with more than 500 thousand clients across the country and over $55.0 billion in combined client assets under administration.

The new entity, Aviso Wealth, will be jointly owned by Desjardins and a limited partnership comprised of Centrals and CUMIS, with each holding a 50.0% stake. Aviso Wealth will give credit unions access to a vertically integrated wealth management organization that is owned by the network and that will focus on meeting the expanding wealth management needs of credit union partners and their members across Canada. The merger of these businesses will offer a significant opportunity for credit unions to grow their wealth business and compete with other financial institutions such as the large banks. The transaction is expected to close in the first quarter of 2018.

Capital restructuring

As a result of members' approval of changes to Central 1's Rules, Class A shares will be reduced and Class F shares will be issued to Class A members in proportion to their portion of mandatory deposits. The remaining aggregate level of Class A shares will be based on Central 1's estimate of regulatory capital to support strategic and operational initiatives over Central 1's planning cycle, which is currently $50.0 million. The credit union members' holding of these Class A shares will continue to be based on their share of the network assets. On December 5, 2017, Central 1 received FICOM approval of these changes. Central 1 plans to reacquire 750 thousand of Class E shares with an aggregate value of $75.0 million, which would reduce Central 1's regulatory capital. This series of transactions is anticipated to be completed by March 31, 2018.