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Financial statements of

Newfoundland and Labrador Credit Union Limited

December 31, 2012

Newfoundland and Labrador Credit Union Limited

December 31, 2012

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Independent Auditor's Report

To the Owners of
Newfoundland and Labrador Credit Union Limited

We have audited the accompanying financial statements of Newfoundland and Labrador Credit Union Limited, which comprise the statement of financial position as at December 31, 2012 and the statements of comprehensive income and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

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

Deloitte LLP

Chartered Accountants
February 2, 2013

Newfoundland and Labrador Credit Union Limited

Statement of Comprehensive Income

Year ended December 31
(CDN dollars)

	2012	2011
	$	$
Financial revenue		
Owners' loans and mortgages (Note 4)	**21,365,368**	21,628,506
Investment income	**607,593**	658,808
	21,972,961	22,287,314
Cost of funds		
Interest on owners' deposits (Note 5)	**7,399,407**	7,784,024
Net financial income	**14,573,554**	14,503,290
Other income		
Service charges	**2,636,987**	2,099,924
Insurance commissions	**836,722**	697,507
Other	**168,433**	155,959
Rental	**140,060**	128,322
Financial margin and other income	**18,355,756**	17,585,002
Operating expenses		
Personnel	**9,449,419**	8,884,557
General business	**3,786,955**	3,470,673
Occupancy	**1,377,339**	1,237,085
Depreciation	**966,715**	946,510
Owners' security	**899,845**	947,134
Total operating expenses	**16,480,273**	15,485,959
Earnings before income taxes	**1,875,483**	2,099,043
Income taxes (Note 12)		
Current	**471,553**	544,391
Deferred (recovery)	**(24,600)**	8,317
	446,953	552,708
Net earnings	**1,428,530**	1,546,335
Retained earnings, beginning of year	**16,171,350**	14,734,165
Dividends (Note 11)	**(112,420)**	(109,150)
Retained earnings, end of year	**17,487,460**	16,171,350

Newfoundland and Labrador Credit Union Limited

Statement of Financial Position

December 31
(CDN dollars)

	2012	2011
	$	$
Assets		
Cash and cash equivalents (Note 6)	**14,698,124**	8,401,791
Investments (Note 7)	**36,901,417**	37,825,877
Loans and mortgages receivable (Note 8)		
Mortgage loans	**292,918,492**	269,897,802
Personal loans	**97,720,271**	96,020,715
Commercial loans and mortgages	**25,522,641**	33,532,402
	416,161,404	399,450,919
Less allowance for impaired loans and mortgages (Note 9)	**(619,595)**	(742,282)
	415,541,809	398,708,637
Capital assets (Note 10)	**16,844,866**	15,557,348
Derivative financial instrument (Note 17)	**1,911,455**	1,969,625
Other assets	**3,086,774**	2,828,417
	488,984,445	465,291,695
Liabilities		
Bank indebtedness (Note 6)	**-**	2,441,500
Accounts payable and accrued liabilities	**1,305,268**	1,716,420
Government remittances payable	**195,803**	263,019
Severance provisions	**1,326,103**	1,176,934
Owners' deposits (Note 11)	**466,758,356**	441,552,847
Derivative financial instrument (Note 17)	**1,911,455**	1,969,625
	471,496,985	449,120,345
Owners' equity		
Retained earnings	**17,487,460**	16,171,350
	488,984,445	465,291,695

Approved on behalf of the Board:

________________ Director ________________ Director

Newfoundland and Labrador Credit Union Limited

Statement of Cash Flows

Year ended December 31

(CDN dollars)

	2012	2011
	$	$
Operating activities		
Net earnings	**1,428,530**	1,546,335
Adjustments for:		
Provision for impaired loans and mortgages (Note 9)	**51,206**	94,924
Financial revenue	**(21,972,961)**	(22,287,314)
Cost of funds - interest on owners' deposits	**7,399,407**	7,784,024
Depreciation	**966,715**	946,510
Current income taxes (Note 12)	**471,553**	544,391
Future income taxes (recovery) (Note 12)	**(24,600)**	8,317
	(11,680,150)	(11,362,813)
Changes in operating assets/liabilities:		
Change in loans and mortgages receivable	**(16,986,193)**	(36,507,060)
Change in owners' deposits	**25,352,066**	26,780,089
Change in other operating assets	**(233,757)**	245,121
Change in other operating liabilities	**(263,138)**	885,936
Cash used in operating activities before interest and taxes	**(3,811,172)**	(19,958,727)
Interest received	**22,203,538**	22,064,149
Interest paid	**(7,558,242)**	(7,612,964)
Income taxes paid	**(537,614)**	(792,958)
	10,296,510	(6,300,500)
Investing activities		
Increase (decrease) in bank indebtedness	**(2,441,500)**	2,441,500
Decrease in investments	**795,698**	5,950,106
Purchase of capital assets	**(2,254,233)**	(2,532,861)
	(3,900,035)	5,858,745
Financing activities		
Increase (decrease) in membership share capital	**9,008**	(29,975)
Dividends paid on membership shares	**(109,150)**	(100,700)
	(100,142)	(130,675)
Net increase (decrease) in cash and cash equivalents	**6,296,333**	(572,430)
Cash and cash equivalents, beginning of year	**8,401,791**	8,974,221
Cash and cash equivalents, end of year	**14,698,124**	8,401,791

1. Reporting entity

Newfoundland and Labrador Credit Union Limited (the "Credit Union" or "NLCU") is incorporated under the Credit Union Act of Newfoundland and Labrador (the "Act") and is a member of the Credit Union Deposit Guarantee Corporation of Newfoundland and Labrador. The Credit Union commenced operations in 1957. It currently operates thirteen branches that offer a full range of financial services to the people of Newfoundland and Labrador. The registered office of NLCU is at 240 Water Street, St. John's, Newfoundland and Labrador.

2. Basis of preparation

Statement of compliance

These financial statements are general purpose financial statements which have been prepared in accordance with International Financial Reporting Standards ("IFRS") adopted by the International Accounting Standards Board ("IASB").

The financial statements for the year ended December 31, 2012 were authorized for issue by the Board of Directors on February 2, 2013.

Basis of preparation

These financial statements are presented in Canadian dollars which is the Credit Union's functional currency. They are prepared on the historical cost basis except for available-for-sale investments, derivative financial instruments, other financial assets and liabilities held for trading, and financial assets and liabilities designated at fair value through profit or loss ("FVTPL") which are stated at their fair value.

Use of significant accounting judgments, estimates and assumptions

The preparation of these financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, and disclosures of contingent assets and contingent liabilities at the date of these financial statements, and the reported amounts of revenues and expenses during the year. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from estimates made in these financial statements.

The 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 if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of IFRS have a significant effect on these financial statements. The Notes to the Financial Statements set out areas involving a higher degree of judgment or complexity, or areas where assumptions are significant to the Credit Union's financial statements are as follows:

a) *Fair value of financial instruments*

Where the fair values of financial assets and financial liabilities recorded on the Statement of Financial Position cannot be derived from observable markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, and prepayment rates. The valuation of financial instruments is described in more detail in Note 16.

2. Basis of preparation (Continued)

Use of significant accounting judgments, estimates and assumptions (continued)

b) *Impairment losses on loans and advances*

The Credit Union reviews its individually significant loans and advances at each statement of financial position date to assess whether an impairment loss should be recorded in the Statement of Comprehensive Income. In particular, management judgment is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors such as the length of time payments are past due and the amount of security held on the loan. Actual results may differ, resulting in future changes to the allowance.

Loans and advances have been assessed individually for impairment. The impairment loss on loans and advances is disclosed in more detail in Note 9.

c) *Impairment of available-for-sale investments*

The Credit Union reviews its equity instruments classified as available-for-sale investments at each statement of financial position date to assess whether they are impaired. This requires similar judgment as applied to the individual assessment of loans and advances.

The Credit Union also records impairment charges on available-for-sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is ‘significant’ or ‘prolonged’ requires judgment.

d) *Deferred tax assets*

Deferred tax assets are recognized in respect of tax losses to the extent that it is probable that taxable income will be available against which the losses can be utilized. Judgment is required to determine the amount of deferred tax assets to recognize, based upon the likely timing and level of future taxable income, together with future tax planning strategies measured at the tax rate expected to apply.

e) *Economic lives of capital assets*

Management determines the estimated useful lives of its capital assets based on historical experience of the actual lives of capital assets of similar nature and functions, and reviews these estimates at the end of each reporting period.

f) *Provisions*

The amount recognized as provisions relates to the Credit Union’s severance accrual and is the best estimate of the consideration required to settle the related liability, taking into account the risks and uncertainties surrounding the obligation. In addition, severance will only be settled when employees who have been working with the Credit Union for twenty years, cease employment with the Credit Union. Therefore, an assessment of the severance accrual inherently involves the exercise of significant judgment and estimates of the number of employees who will continue working with the Credit Union until their severance vests.

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including reasonable expectations of future events. Management believes the estimates used in preparing these financial statements are reasonable. Actual results in the future may differ from those reported.

2. Basis of preparation (Continued)

New standards and interpretations not yet adopted

Certain new standards, interpretations, amendments and improvements to the existing standards have been issued by the IASB, but are not yet effective for the year ended December 31, 2012, and have not been applied in preparing these financial statements:

a) *Presentation of financial statements*

In June 2011, the IASB amended IAS 1 - *Presentation of Financial Statements: Other Comprehensive Income* ("IAS 1"), which will be applied retrospectively for annual periods beginning on or after July 1, 2012. The amendments require additional disclosures on components of other comprehensive income ("OCI"). The Credit Union is assessing the potential impact of these amendments.

b) *Financial instruments*

In November 2009 and October 2010, the IASB issued IFRS 9 - *Financial instruments* ("IFRS 9"), *Classification and Measurement of Financial Assets and Financial Liabilities*. IFRS 9 will replace IAS 39 - *Financial Instruments: Recognition and Measurement* ("IAS 39") in its entirety. IFRS 9 is effective for annual periods beginning on or after January 1, 2015. The Credit Union is assessing the potential impact of this standard.

c) *Fair Value Measurement*

In May 2011, the IASB issued IFRS 13 - *Fair Value Measurement* ("IFRS 13"). IFRS 13 defines fair value and sets out in a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 is effective for annual periods beginning on or after January 1, 2013. The Credit Union is assessing the potential impact of this new standard.

3. Significant accounting policies

The following significant accounting policies have been applied consistently by the Credit Union to all periods presented in these financial statements without exception.

Financial instruments

Financial assets and financial liabilities are recognized when the Credit Union becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially recognized at fair value and their subsequent measurement is dependent on their classification as described below. Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics and the Credit Union's designation of such instruments.

The Credit Union is required to classify all financial assets either as fair value through profit or loss (FVTPL), available-for-sale, held-to-maturity, or loans and receivables and, financial liabilities are classified as either fair value through profit or loss, or other liabilities. The standards require that all financial assets and financial liabilities, including derivatives, be subsequently measured at fair value with the exception of loans and receivables, debt securities classified as held-to-maturity, available-for-sale financial assets that do not have quoted market prices in an active market and whose fair value cannot be reliably estimated, and other liabilities.

3. Significant accounting policies (Continued)

Financial instruments(continued)

a) <u>Classification</u>

Cash	Loans and receivables
Investments:	
Equity investments	Available-for-sale
Liquidity reserve	Loans and receivables
Loans and mortgages	Loans and receivables
Other assets:	
Accounts receivable	Loans and receivables
Accounts payable and accrued liabilities	Other liabilities
Owners' deposits	Other liabilities
Other liabilities	Other liabilities
Derivative financial instruments	Fair value through profit or loss

b) <u>Fair value through profit or loss ("FVTPL")</u>

Financial assets and financial liabilities are classified as FVTPL when the financial asset or financial liability is held for trading or it is designated as FVTPL if certain criteria are met.

Financial assets and financial liabilities at FVTPL are stated at fair value, with any gains or losses arising on remeasurement recognized in profit or loss. The Credit Union's financial instruments designated as FVTPL consist of derivative financial instruments.

c) <u>Available-for-sale financial assets</u>

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale and are initially recognized at fair value. Subsequent to initial recognition, available-for-sale financial assets are measured at fair value, and the gains and losses on such assets are recorded in other comprehensive income until the investment is derecognized or until the investment is identified as being subject to impairment.

Dividend income is recognized in profit or loss when the Credit Union's right to receive the dividends is established. Interest income is recognized in income using the effective interest method.

Shares in Central 1, League Data, and Concentra held by the Credit Union are not traded in an active market and are classified as available-for-sale. Available-for-sale equity investments that do not have a quoted price in an active market and whose fair value cannot be reliably measured are measured at cost less any identified impairment losses at the end of each reporting period.

d) <u>Loans and receivables</u>

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which the Credit Union does not intend to sell immediately or in the near term. Loans and receivables including cash, liquidity reserve investments, loans to owners, accrued interest on loans, accrued interest on investments and accounts receivable, are measured at amortized cost using the effective interest method, net of impairment losses.

Interest income is recognized by applying the effective interest rate.

e) <u>Effective interest method</u>

The effective interest method is a method of calculating the amortized cost of a financial asset or financial liability and of allocating interest income/expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees, transaction costs and other premiums or discounts) through the expected life of the asset/liability or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

3. Significant accounting policies (Continued)

Financial instruments(continued)

f) Impairment of financial assets and allowance for impaired loans

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at each statement of financial position date. Financial assets are impaired when there is objective evidence that, because of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the asset have been affected.

The amount of impairment on financial assets carried at amortized cost is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The impairment loss on financial assets is based on a review of all outstanding amounts at period end. The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of loans to owners, where the carrying amount is reduced using an allowance account. The allowance for impaired loans is maintained in an amount considered adequate to absorb incurred losses in the loan portfolio. The allowance for impaired loans reflects management's best estimate of the losses existing in the loan portfolio and their judgments about economic conditions. If the circumstances under which these estimates and judgments were made change, there could be a change to the allowance for impaired loans currently recognized. The allowance for impaired loans consists of a specific provision component attributable to individually significant exposures and, where applicable, a collective provision, established for groups of loans with similar risk characteristics. Changes in the carrying amount of the allowance account are recognized in profit and loss. Write-offs are generally recorded after all reasonable restructuring or collection activities have taken place and there is no realistic prospect of recovery. The methodology and assumptions used are reviewed regularly. Each component of the allowance for impaired loans is reviewed at least on the reporting date.

When an available-for-sale financial asset is considered to be impaired, cumulative gains or losses previously recognized in other comprehensive income are reclassified to profit or loss in the period.

Subsequent to an impairment loss, events can occur that provide objective evidence that the financial asset is no longer impaired. When this occurs the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment, at the date the impairment is reversed, does not exceed the amortized cost that would have resulted had the impairment not been recognized.

g) Derecognition of financial assets

The Credit Union derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

The Credit Union continues to recognize the transferred asset to the extent that the Credit Union neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset or when the Credit Union retains substantially all the risks and rewards of ownership. In the latter case, the Credit Union also recognizes collateralized borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received/receivable and any cumulative gain or loss that had been recognized in other comprehensive income and accumulated in equity is recognized in profit or loss.

h) Other financial liabilities

Other financial liabilities (including borrowings) are subsequently measured at amortized cost using the effective interest method.

3. Significant accounting policies (Continued)

Financial instruments (continued)

i) *Derecognition of financial liabilities*

The Credit Union derecognizes financial liabilities when, and only when, the Credit Union's obligations are discharged, cancelled or they expire.

j) *Embedded derivatives*

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at FVTPL.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits with banks and Credit Union Centrals and other highly liquid investments with original maturities of three months or less. Cash and cash equivalents are classified as loans and receivables and are carried at amortized cost, which is considered equivalent to fair value due to the short-term nature of these assets.

Loans to owners

Loans to owners include personal loans, mortgages and commercial loans and are recognized when the cash is advanced to the borrower. All loans to owners are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and have been classified as loans and receivables, which are subsequently measured at amortized cost using the effective interest method.

Capital assets

Capital assets are measured at cost less accumulated depreciation and any accumulated impairment losses. When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate assets.

Depreciation is recognized in profit or loss on a straight-line basis over the respective assets' estimated useful lives with the exception of depreciation of paved areas and furniture and equipment, which is recognized using the declining balance method.

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

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating.

Rental income from operating leases is recognized on a straight-line basis over the term of the related lease.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred.

Deposits from owners

Deposits from owners are disclosed in Note 11 and are the Credit Union's main source of funding. They are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method.

3. Significant accounting policies (Continued)

Provisions

Provisions are recognized when the Credit Union has a present obligation (legal or constructive), as a result of a past event, it is probable that the Credit Union will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognized as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Employee benefits

a) *Short-term employee benefits*

Short-term employee benefits include salaries and wages, employee benefits, allowances, bonuses and burdens. Short-term employee benefits are expensed as the related service is provided.

b) *Severance benefits*

Severance benefits are accounted for on an accrual basis and are calculated based upon years of service and current salary levels. The right to be paid severance pay vests with employees with twenty years of continual service with the Credit Union. Severance is payable when the employee ceases employment with the Credit Union.

Ownership shares

The Credit Union’s ownership shares are presented in the Statement of Financial Position as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. These shares qualify as capital for regulatory purposes. All ownership shares of the Credit Union are classified as liabilities. Payments of dividends on ownership shares presented as a financial liability are recognized as a distribution of profit or loss. Dividends are recorded when declared by the Board of Directors.

Revenue recognition

Interest income is accrued monthly by reference to the principal outstanding at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset’s net carrying amount on initial recognition.

Dividend income is recognized when the right to receive payment is established. Dividends are included in interest income in the Statement of Comprehensive Income.

Other fees and commission income include account service fees, investment management fees, and insurance fees which are recognized over the period the services are performed.

Income taxes

Income tax expense comprises current and deferred tax.

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

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

3. Significant accounting policies (Continued)

Income taxes (continued)

Future tax assets are recognized to the extent that it is probable that taxable income will be available against which the asset can be utilized.

Current tax and future tax relating to items recognized directly in equity are also recognized in equity and not in the Statement of Comprehensive Income.

Foreign currency translation

The financial statements are presented in Canadian dollars ($).

Transactions in foreign currencies are initially translated into Canadian dollars at the rate of exchange in effect at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rate of exchange at the statement of financial position date.

Translation gains and losses are recognized immediately in profit or loss and are included in the ‘other income’ line item in the Statement of Comprehensive Income.

Financial guarantees

Financial guarantees are contracts that require the Credit Union to make specified payments to reimburse the holder for a loss incurred because a specified debtor fails to make payment due in accordance with the debt instrument. Financial guarantee liabilities are recognized at fair value.

4. Financial revenue – owners’ loans and mortgages

	2012	2011
	$	$
Personal loans	**6,011,712**	6,066,712
Residential mortgages	**13,653,710**	13,492,110
Commercial loans and mortgages	**1,699,946**	2,069,684
	21,365,368	21,628,506

5. Interest on owners’ deposits

	2012	2011
	$	$
Personal chequing accounts	**17,824**	19,417
Savings accounts	**724,944**	656,437
Term deposits	**3,168,755**	3,387,252
Registered savings accounts	**2,418,604**	2,671,230
Tax free savings accounts	**314,182**	212,718
Index linked deposits	**751,783**	824,753
Other	**3,315**	12,217
	7,399,407	7,784,024

(CDN dollars)

6. Cash and cash equivalents

	2012	2011
	$	$
Cash on hand	**4,338,157**	3,728,547
Cash held with Credit Union Central	**5,782,019**	1,046,198
Cash held with other chartered banks	**4,577,948**	3,627,046
	14,698,124	8,401,791

The Credit Union has available lines of credit with Central 1 and Atlantic Central in the amounts of $7,500,000 and $3,000,000. As at December 31, 2012, there were no balances drawn on these facilities (2011 - $2,441,500).

7. Investments

The following table provides information on the investments held by the Credit Union.

	2012	2011
	$	$
Loans and receivables		
Mandatory liquidity reserve deposits	**29,473,500**	27,940,000
Other deposits	**6,730,850**	9,060,048
Available-for-sale		
Equity investments	**457,107**	457,107
	36,661,457	37,457,155
Accrued interest	**239,960**	368,722
Carrying value	**36,901,417**	37,825,877
Market value	**36,901,417**	37,825,877

Central 1 Credit Union - liquidity reserve deposit

As a condition of maintaining membership in good standing with Central 1, the Credit Union is required to maintain on deposit with Central 1 an amount equal to 6% of the total assets as at each month end. At maturity, these deposits are reinvested at market rates for various terms as determined by management. The deposit can be withdrawn only if there is a sufficient reduction in the Credit Union’s assets or upon withdrawal of membership from Central 1.

Equity investments

Equity investments are recorded at cost as they do not have quoted market prices in an active market.

8. Loans to owners

Mortgages are repayable in monthly blended principal and interest installments over a maximum term of seven years based on a maximum amortization as prescribed by Provincial law. Mortgages are secured by residential properties.

Personal loans, including line of credit loans, are repayable to the Credit Union in monthly blended principal and interest installments over a period acceptable by Provincial law, except for line of credit loans, which are repayable on a revolving credit basis and require minimum monthly payments. All loans, except for mortgage loans, are open and, at the option of the borrower, may be repaid at any time without notice. Types of collateral generally obtained by the Credit Union include, but are not limited to, the following: member’s personal property such as vehicles; cash and marketable securities; mortgage charges; fixed, floating or specific general security agreements; and personal guarantees.

(CDN dollars)

8. Loans to owners (Continued)

Credit quality of loans

Security held on a portfolio basis is as follows:

	2012	2011
	$	$
Uninsured mortgages	**109,558,089**	108,349,135
Insured mortgages	**203,267,776**	188,261,599
Unsecured loans	**36,906,314**	36,989,886
Secured loans	**66,429,225**	65,850,299
	416,161,404	399,450,919

Syndicated loans
At December 31, 2012, the Credit Union did not hold any syndicated loans or mortgages (2011 - $8,774,242).

9. Allowance for impaired loans

The activity in the allowance for impaired loans is summarized as follows:

	2012				2011
	Personal	Mortgages	Commercial	Total	Total
	$	$	$	$	$
Balance, beginning of year	**664,056**	**-**	**78,226**	**742,282**	901,232
Loans written-off as uncollectible	**(153,983)**	**-**	**(19,910)**	**(173,893)**	(253,874)
Provision for impaired loans and mortgages	**51,128**	**-**	**78**	**51,206**	94,924
Balance, end of year	**561,201**	**-**	**58,394**	**619,595**	742,282

Credit quality of owner loans is summarized as follows:

	Personal	Mortgages	Commercial	Total 2012
	$	$	$	$
Neither past due [(1)] nor impaired	**97,019,169**	**292,837,217**	**25,464,247**	**415,320,633**
Past due but not impaired				
31 to 90 days	**99,965**	**-**	**-**	**99,965**
91 and greater	**39,936**	**81,275**	**-**	**121,211**
Impaired	**561,201**	**-**	**58,394**	**619,595**
	97,720,271	**292,918,492**	**25,522,641**	**416,161,404**
Less: specific allowances	**(561,201)**	**-**	**(58,394)**	**(619,595)**
	97,159,070	**292,918,492**	**25,464,247**	**415,541,809**

[(1)] A loan is considered to be past due w hen the counterparty has not made a payment the day of the contractual payment date.

(CDN dollars)

9. Allowance for impaired loans (Continued)

	Personal	Mortgages	Commercial	Total 2011
	$	$	$	$
Neither past due [1] nor impaired	95,191,401	269,433,500	33,454,176	398,079,077
Past due but not impaired				
31 to 90 days	130,172	239,198	-	369,370
91 and greater	35,086	225,104	-	260,190
Impaired	664,056	-	78,226	742,282
	96,020,715	269,897,802	33,532,402	399,450,919
Less: specific allowances	(664,056)	-	(78,226)	(742,282)
	95,356,659	269,897,802	33,454,176	398,708,637

[1] A loan is considered to be past due w hen the counterparty has not made a payment the day of the contractual payment date.

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(CDN dollars)

10. Capital assets

2012

	Land	Buildings	Roof & Air Conditioning	Paved Areas	Leasehold Improvements	Furniture and Equipment	Computer Terminals	Automated Banking Machines	Automobile	Personal Computers and Software	Total 2012
	$	$	$	$	$	$	$	$	$	$	$
Rate		50 Years	25 Years	8.00%	5 Years	20.00%	5 Years	5 Years	5 Years	3 Years	
Cost											
Balance, beginning of year	3,947,706	11,217,503	1,539,913	484,594	1,672,155	5,141,243	518,366	1,722,439	53,708	1,581,204	27,878,831
Additions	3,637	1,180,086	513,921	76,978	51,074	276,508	-	77,557	-	74,472	2,254,233
Disposals	-	-	-	-	-	-	-	-	-	-	-
Balance, end of year	3,951,343	12,397,589	2,053,834	561,572	1,723,229	5,417,751	518,366	1,799,996	53,708	1,655,676	30,133,064
Accumulated depreciation											
Balance, beginning of year	-	2,697,262	491,693	198,521	1,373,027	4,137,365	447,150	1,496,387	21,483	1,458,595	12,321,483
Depreciation expense	-	249,189	69,011	24,882	90,629	256,078	31,661	126,592	10,742	107,931	966,715
Disposals	-	-	-	-	-	-	-	-	-	-	-
Balance, end of year	-	2,946,451	560,704	223,403	1,463,656	4,393,443	478,811	1,622,979	32,225	1,566,526	13,288,198
Net Book Value	3,951,343	9,451,138	1,493,130	338,169	259,573	1,024,308	39,555	177,017	21,483	89,150	16,844,866

2011

	Land	Buildings	Roof & Air Conditioning	Paved Areas	Leasehold Improvements	Furniture and Equipment	Computer Terminals	Automated Banking Machines	Automobile	Personal Computers and Software	Total 2011
	$	$	$	$	$	$	$	$	$	$	$
Rate		50 Years	25 Years	8.00%	5 Years	20.00%	5 Years	5 Years	5 Years	3 Years	
Cost											
Balance, beginning of year	3,262,212	10,196,543	1,465,250	457,524	1,326,277	4,880,948	518,366	1,722,439	53,708	1,462,703	25,345,970
Additions	685,494	1,020,960	74,663	27,070	345,878	260,295	-	-	-	118,501	2,532,861
Disposals	-	-	-	-	-	-	-	-	-	-	-
Balance, end of year	3,947,706	11,217,503	1,539,913	484,594	1,672,155	5,141,243	518,366	1,722,439	53,708	1,581,204	27,878,831
Accumulated depreciation											
Balance, beginning of year	-	2,469,839	431,645	175,999	1,262,189	3,886,396	414,542	1,374,900	10,742	1,348,721	11,374,973
Depreciation expense	-	227,423	60,048	22,522	110,838	250,969	32,608	121,487	10,741	109,874	946,510
Disposals	-	-	-	-	-	-	-	-	-	-	-
Balance, end of year	-	2,697,262	491,693	198,521	1,373,027	4,137,365	447,150	1,496,387	21,483	1,458,595	12,321,483
Net Book Value	3,947,706	8,520,241	1,048,220	286,073	299,128	1,003,878	71,216	226,052	32,225	122,609	15,557,348

(CDN dollars)

11. Owners' deposits

	2012	2011
	$	$
Personal chequing accounts	**79,461,240**	71,510,479
Savings accounts	**107,105,258**	94,690,638
Term deposits	**118,970,600**	124,254,260
Registered retirement savings plans	**114,900,121**	113,033,056
Registered retirement income funds	**17,540,604**	16,195,804
Tax free savings accounts	**21,766,584**	14,866,128
Share accounts	**7,013,949**	7,002,482
	466,758,356	441,552,847

Term deposits

Term deposits for periods of one to seven years generally may not be withdrawn prior to maturity.

Registered retirement plans

The Credit Union has engaged a third party to act as the trustee for the registered retirement plans offered to owners. Under an agreement with the third party, owners' contributions to these plans, as well as income earned on them, are deposited in the Credit Union. On withdrawal, payment of the plan proceeds is made to the owners, or the parties designated by them, by the Credit Union, on behalf of the trustee.

Share accounts

Owner equity shares consist of 20 shares at a par value of five dollars ($5.00) per share. The holders of owner equity shares have all of the rights and privileges and are subject to the restrictions of an owner, as provided for in the Credit Union Act and Regulations and in the By-laws of the Credit Union. Currently, there are 16,829 (2011 – 16,832) fully paid equity share accounts with an aggregate value of $2,359,044 (2011 - $2,278,817).

Surplus shares may be issued in an unlimited number at par value of five dollars ($5.00) per share. The holders of surplus shares have all of the rights and privileges and are subject to the restrictions applicable to owners, as outlined in the Credit Union Act and Regulations and in the By-laws of the Credit Union. Currently, there are 2,231 (2011 – 2,543) fully paid surplus share accounts with an aggregate value of $11,155 (2011 - $13,415).

Incentive shares may be issued by the Credit Union to a maximum number of ten thousand shares as approved by the Regulator in accordance with the Credit Union Act and Regulations and in the By-laws of the Credit Union. Currently, there are 873 (2011 – 959) shares accounts outstanding with an aggregate value of $4,643,750 (2011 - $4,710,250).

Share accounts are not insured by the Credit Union Deposit Guarantee Corporation, however, they qualify as capital for regulatory purposes, notwithstanding their financial statement classification as liabilities.

Dividends

Dividends on shares may be declared by the Board of Directors, subject to availability of sufficient earnings to meet the regulatory requirements of the Act as described in Note 13.

The Board of Directors declared a dividend of $112,420 as of December 31, 2012 (2011 - $109,150).

(CDN dollars)

12. Income taxes

The provision for income taxes reported for the year ended December 31 differs from the amount computed by applying the Canadian statutory rate to income before income taxes for the following reasons:

	2012	2011
	$	$
Earnings before income taxes	1,875,483	2,099,043
Income tax expense based on statutory rate of 25% (2011 - 25%)	468,871	524,761
Effect of non-deductible expenses	44,232	104,946
Other	(41,550)	(85,316)
	471,553	544,391
Deferred income tax expense (recovery)	(24,600)	8,317
Total income tax expense	446,953	552,708

Temporary differences, which give rise to the deferred income tax asset, are as follows:

	2012	2011
	$	$
Deferred income tax assets (liabilities)		
Capital assets and other	(241,962)	(229,270)
Severance	331,526	294,234
Deferred income tax asset	89,564	64,964

13. Capital adequacy

Capital management

The Board approves annually the capital management policy and the annual business plan. This policy outlines the Credit Union's overall objectives and guidelines to ensure that the Credit Union has the required quantity, quality and appropriate composition of capital needed to address the inherent risks of the Credit Union and to support the current and future operating plans.

The Act requires credit unions to maintain a minimum capital adequacy reserve (consists of share capital and retained earnings) of 5% of total assets or alternatively, using an 8% risk weighted model. Additionally, retained earnings cannot be less than 3% of the total assets. The Credit Union is in compliance with its policies and those of the Act regarding regulatory capital as at December 31 as outlined in the table below.

(CDN dollars)

13. Capital adequacy (Continued)

	2012	2011
	$	$
Retained earnings	**17,487,460**	16,171,350
Owners' shares	**7,013,949**	7,002,482
Future tax asset	**(89,564)**	(64,964)
Capital base	**24,411,845**	23,108,868
Risk weighted assets	**154,774,184**	157,964,091
Capital adequacy		
Actual	**15.77%**	14.63%
Regulatory requirement	**8.00%**	8.00%
Retained earnings as a percentage of assets		
Actual	**3.58%**	3.48%
Regulatory requirement	**3.00%**	3.00%

On a risk weighted basis the Credit Union's capital position for the year ended December 31, 2012 was 15.79% (2011 – 14.63%) and the capital held in retained earnings was 3.58% (2011 – 3.48%) of total assets. NLCU has exceeded the risk weighted capital required by regulators by 7.79% (2011 – 6.63%) and exceeded retained earnings capital requirement by 0.58% (2011 – 0.48%).

14. Related party transactions

At December 31, 2012, the aggregate value of personal and mortgage loans outstanding to directors and officers totaled $1,601,800 (2011 – $1,431,049). The maximum balances of these loans during the year was $1,751,321 (2011 – $1,536,144). The aggregate value of deposits outstanding to directors and officers totaled $2,457,262 (2011 – $2,289,651).

The interest rates charged on balances outstanding from directors are the same as those charged in an arm's length transaction and loans to designated officers are granted at a discount rate, consistent with industry practices and in accordance with board approved policy. Loan and mortgage balances with directors and officers are secured as per the Credit Union's lending policies.

There was no allowance for impaired loans required in respect of these loans as at December 31, 2012 and December 31, 2011.

Key management personnel received salaries and other short-term employee benefits during the year of $3,593,284 (2011 – $3,168,200).

At December 31, 2012, directors received expense reimbursement of $37,573 (2011 – $28,156) and remuneration of $58,050 (2011 – $59,400) for serving the Credit Union.

(CDN dollars)

15. Commitments

Under present lease agreements for rental space the Credit Union is committed to the following expenditures:

	$
2013	127,385
2014	92,929
2015	87,823
2016	26,380
	334,517

16. Fair value of financial instruments

Fair value

The Credit Union's financial instruments are calculated using the valuation methods and assumptions described below. The fair values do not reflect the value of assets/liabilities that are not considered financial instruments, such as prepaids, capital assets, future tax asset and accrued severance liability.

The estimated fair value amounts are designed to approximate amounts at which instruments could be exchanged in a current transaction between willing parties who are under no compulsion to act. Fair values are based on estimates using present value and other valuation techniques, which are significantly affected by the assumptions used concerning the amount and timing of estimated future cash flows and discount rates, which reflect varying degrees of risk. Because of the estimation process and the need to use judgment, the aggregate fair value amounts should not be interpreted as being necessarily realizable in an immediate settlement of the instruments.

Fair value hierarchy

Financial instruments recorded at fair value on the Statement of Financial Position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);

Level 3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The fair values of cash and cash equivalents, certain other assets and certain other liabilities are assumed to approximate their carrying values, due to their short-term nature.

The estimated fair value of fixed rate loans, fixed rate deposits and liabilities qualifying as regulatory capital is determined by discounting the expected future cash flows of these loans, deposits and capital accounts at current market rates for products with similar terms and credit risks.

The fair value of investments is based on quoted market values where available (see Note 3).

16. Fair value of financial instruments (Continued)

Fair value hierarchy (continued)

Shares in Central 1, League Data, and Concentra are measured at cost less any identified impairment losses at the end of each reporting period. These investments do not have a quoted price in an active market and their fair value cannot be reliably measured.

The Credit Union holds derivative financial instruments classified as FVTPL. These are classified as Level 2 financial instruments.

There has been no significant transfer of amounts between Level 1, Level 2 and Level 3 financial instruments for the years ended December 31, 2012 and 2011.

Additionally, there are no financial instruments classified in Level 3.

17. Nature and extent of risks arising from financial instruments

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

Credit risk

The business of the Credit Union necessitates the management of credit risk. Credit risk is the potential for loss due to the failure of a borrower to meet its contractual obligations.

The Board of Directors of the Credit Union oversees the risk management process. Senior management coordinates policy setting on risk management issues, assesses the risk exposure of the Credit Union and reviews the effectiveness of internal control processes.

The Credit Union uses a disciplined lending approach with standard underwriting parameters for each category of loans. These parameters are used to assist the Credit Union in implementing a prudent and effective process to assess the borrower's ability to repay.

The Credit Union mitigates credit risk by obtaining quality collateral. The Credit Union considers collateral to be of good quality if it can determine the legal validity and market value on an on-going basis. The Credit Union's internal policy provides additional information regarding the appropriate collateral based on the category of loan. Types of collateral generally obtained by the Credit Union include, but are not limited to, the following: member's personal property such as vehicles; cash and marketable securities; mortgage charges; fixed, floating or specific general security agreements; and personal guarantees.

In addition, the Credit Union monitors its loan concentration to ensure that it is in compliance with its policies.

Liquidity risk

The business of the Credit Union necessitates the management of liquidity risk. Liquidity risk is the risk of being unable to meet financial commitments, under all circumstances, without having to raise funds at unreasonable prices or sell assets on a forced basis.

The Credit Union's objective is to implement a policy that addresses limits on the sources, quality and amount of the assets to meet normal operational, contingency funding for significant deposit withdrawals and regulatory requirements.

The Board of Directors is ultimately responsible for the liquidity risk management policy. Management reports monthly, to the Board, the Credit Union's compliance with the policy and regulatory requirements; concentration of large deposits of single/connected depositors as a percentage of total deposits; and reports borrowings for liquidity purposes, the level of borrowings and the liquidity less borrowings in relation to the statutory minimum.

(CDN dollars)

17. Nature and extent of risks arising from financial instruments (Continued)

Liquidity risk (contined)

The Act requires credit unions to maintain 6% of liabilities for adequate liquidity. Assets held by the Credit Union for such purposes are outlined in the table below.

	2012	2011
	$	$
Cash and cash equivalents	**14,698,124**	8,401,791
Investments		
Concentra Financial (matures April 2013)	**2,000,000**	2,044,425
Concentra Financial (matures July 2013)	**2,075,093**	2,063,924
Concentra Financial (matures July 2013)	**1,000,000**	1,030,297
Central 1 (matures June 2013)	**1,000,000**	1,000,000
Liquidity reserve deposit	**29,473,500**	27,940,000
Total assets held for liquidity	**50,246,717**	42,480,437

Contractual maturities of financial liabilities are shown under interest rate risk. The Credit Union has no material commitments for capital expenditures and there is no need for such expenditures in the normal course of business.

Market risk

Market risk is the risk of loss that may arise from change in market factors such as interest rates and foreign exchange rates. The Credit Union is exposed to this market risk in its investing and asset/liability management activities.

Senior management is responsible for managing market risk in accordance with the Credit Union's Asset and Liability Management and Investment Policy set by the Board. Senior management reports monthly to the Board its compliance with the policy and regulatory requirements; dollar volume and yields of all investments by investment category; and the particulars of all investment transactions entered into by the Credit Union. All exceptions noted are reported to the Board.

The Board is responsible for monitoring significant variances and ensuring that corrective measures are implemented.

Interest rate risk

Interest rate risk refers to the potential impact of changes in interest rates on the Credit Union's earnings when maturities of its financial liabilities are not matched with the maturities of its financial assets or which are priced on a different basis. It is the policy of the Credit Union to keep exposure to interest rate fluctuations within limits set by the Board and regulations.

The table below summarizes the carrying amounts of financial instruments exposed to interest rate risk by maturity dates.

(CDN dollars)

17. Nature and extent of risks arising from financial instruments (Continued)

Interest rate risk (continued)

2012

	On Demand	Less than 3 months	3 months to one year	One to five years	Non-rate sensitive	Total	Effective interest rate
	$	$	$	$	$	$	%
Investments	-	13,418,858	15,179,665	8,261,247	41,647	36,901,417	1.39
Loans and advances to owners	86,431,249	11,501,242	60,168,791	255,272,259	2,787,863	416,161,404	4.90
Deposits from owners	116,290,128	33,267,126	83,238,684	130,972,422	102,989,996	466,758,356	1.53

2011

	On Demand	Less than 3 months	3 months to one year	One to five years	Non-rate sensitive	Total	Effective interest rate
	$	$	$	$	$	$	%
Investments	-	28,407,645	6,006,841	3,369,744	41,647	37,825,877	1.58
Loans and advances to owners	84,438,421	11,081,795	57,713,872	243,343,678	2,873,153	399,450,919	5.04
Deposits from owners	99,481,746	33,183,784	76,229,004	138,272,084	94,386,229	441,552,847	1.79

At December 31, 2012, if interest rates at that date had been 100 (2011 – 100) basis points lower with all other variables held constant, after-tax net income for the year would have been approximately $110,490 (2011 - $197,276) lower, arising mainly as a result of lower interest revenue on variable loans and mortgages, and lower interest revenue on liquidity investments. If interest rates had been 100 (2011 – 100) basis points higher, with all other variables held constant, after-tax net income would have been approximately $85,818 (2011 - $146,565) higher, arising mainly as a result of higher interest revenue on variable loans and mortgages, and higher interest on liquidity investments.

Foreign currency exchange risk

Foreign currency exchange risk refers to the potential impact of changes in foreign exchange rates on the Credit Union's earnings when balances or currencies of its foreign currency liabilities are not matched with the balances of its foreign currency assets. It is the policy of the Credit Union to mitigate exposure to foreign exchange rate fluctuations by matching its foreign currency liabilities to its foreign currency assets. The Credit Union does not hold foreign investments beyond cash required to meet daily operational requirements.

Index-linked deposits

At December 31, 2012, the Credit Union has issued $35,954,718 (2011 - $32,666,782) of index-linked term deposits (registered and non-registered deposits) to its owners. These term deposits have maturities of three and five years and pay interest to the depositors at the end of the term based on the performance of various Toronto Stock Exchange ("TSX") indices. The Credit Union has entered into derivative agreements with Central 1 to offset the exposure to these indices associated with these products. The Credit Union pays Central 1 a fixed amount on the face value of these term deposit products. At the end of the respective terms, the Credit Union receives payments from the counterparty, Central 1, equal to the amount that will be paid to the depositors based on the performance of various TSX indices.

17. Nature and extent of risks arising from financial instruments (Continued)

Index-linked deposits (continued)

The purpose of these agreements is to provide a hedge against market fluctuations. These agreements have a fair value that varies based on the particular contract and changes in interest rates. The fair value of these agreements is $1,911,455 (2011 - $1,969,625) at year end and has been accounted for as an embedded derivative in accordance with the Credit Union's accounting policy.