

2016

Annual Report



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2016 Highlights

+3.3%
Assets

\$180k
Back to Members

+7.9%
Avg. Members Savings

+3.3%
Deposits

\$130k
Back to Communities

2
New Ways to Bank

+9.6%
Loans

5k
Members Banking Online

558
New Members

15k
Membership



**Credit unions are built on fairness, trust,
equality and independence.**

**We provide honest banking and make a
local impact in our communities.**

Your money stays and works here.



Mission

To provide outstanding service and professional advice to enable our members to reach their financial goals.

Values

Honest

Passionate

Holistic

Spiritual

Evolutionary

Simplistic

Inclusive



Board of Directors



Corey Tremere
President



Wendell Dawson
Vice-President



Jacinta Doiron
Secretary



Alan Hearn Jr.



Jason Doucette



Joey Gauthier



Carol Blum



Cyrlina Campbell



Bryon Poehlman



Michelle Proctor



Bernard Keefe



Rick Gibbs



President's Report

Like most businesses, competition can be tough and the waters sometimes challenging to navigate, particularly in this environment of prolonged low interest rates. With that in mind I am pleased to report the year end results for Provincial Credit Union are once again positive.

With a forward thinking team, Provincial Credit Union operates within a collaborative network of Credit Unions across PEI and the Atlantic Region. We have used the services of Atlantic Central and partner organizations to help guide our vision for the future. On top of that your board of directors and management team have started a process with MRSB, to facilitate the development of a strategic plan for the coming years. In all of these sessions, the needs of our members and the services we provide to them are at the forefront of all decisions, as we work diligently to ensure the continued success of Provincial Credit Union. Discussions are also taking place about upgrading the premises at all four offices, including ATM updates and building enhancements.

As a director I can tell you it is a privilege to serve the membership. At our AGM each year, the board takes an oath to: act honestly and in good faith; exercise the care, diligence and skill of a prudent person; avoid conflicts of interest; and observe strict confidentiality. I am proud of our directors, and have full confidence in our leadership team. Your Board contributes many hours of personal time to attend meetings and training sessions on your behalf. Future plans include exploring options for the board nomination and voting process at our AGMs, to better reflect the size and limitations of the meetings.

The strength of our board, management, and staff gives me continued optimism for the future. The board remains vigilant in its efforts to earn the continued confidence, trust and patronage of you, our members/owners.

In closing thank you to our membership, and the communities we serve. Without your un-ending support, we certainly would not be where we are today.

Sincerely,

Corey Tremere
President



Manager's Report

It is my pleasure to report to you on the operations of Provincial Credit Union, as at December 31, 2016. We enjoyed another successful year, with assets now at \$322,429,950, equity sitting at 9.58%, or \$30,876,673, and a net income of \$1,107,051. Given the uncertainty in the markets and an extended period of low interest rates, we are pleased our credit union continues to perform well.

December 31, 2016 marked another milestone...two full years since the credit union in Montague merged with Provincial Credit Union. Just as a refresher, prior to the Montague amalgamation, Stella Maris joined the team in October of 2013, and so in that space of 15 months, our operation grew from 2 offices to 4, and a staff of 60. As you can imagine there were some growing pains with the increase in size in such a short time frame, but having said that, our operations are aligning very well now, and we look forward to the challenges and opportunities that lie ahead, in all four of the communities we serve.

Of course a main reason our credit union is functioning so well is because of our knowledgeable and capable staff, and I am pleased to pass along that Provincial Credit Union is still recognized as a Best Places to Work and a Top 101 company in Atlantic Canada. On another industry related note, across the country, Canadian Credit Unions have been ranked #1 in Customer Service, for the 12th consecutive year, in an independent survey conducted by Ipsos.

Moving forward we remain committed to meeting the needs of our members. On the product and technology side, we strive to make the latest innovations available. In this past year we introduced Interac on line payments, the ability to shop online and pay directly from your bank account. We have also begun the process

of updating our ATMs, to reflect the newer technology of envelope free ATMs. Still to come in 2017 is Mobile Pay, allowing members to simply tap their smart phone to pay for merchandise. On the commercial banking side there are now standardized operating and investment accounts across the province.

As part of our mission statement we strive to provide outstanding service and professional advice to our members. To help achieve our mission, staff continue to enhance their knowledge and currently, we have a number of staff in each office studying for the mutual funds exam. As well, we have two certified financial planners who specialize in investment/retirement planning, insurance services, and estate planning to assist members in reaching their financial goals.

I would be remiss if I didn't acknowledge the completion of our 10 year partnership with the Canadian Cancer Society Relay for Life. PEI Credit Unions were provincial event sponsor for the last decade, raising over \$500,000 to help fight cancer, with \$312,000 of that raised by credit union staff across the province.

In closing, thank you to our board of directors for your support and guidance. And thank you to our members for their patronage over the last year as well.

Sincerely,

Bernard Gillis
General Manager



Building a Community Together

Being supportive and involved with our members along with the community is, as always, of great importance to credit unions. Our high standard for social responsibility means that we strive to serve our community as best as possible. One of the most significant ways in which we support the community is through donations, sponsorships and volunteering.

This year, we invested over \$130,000 in donations and sponsorships benefiting not only community groups but also numerous local families alike.

As a financial co-operative, our motive is to always assist our members with their financial goals, while also positively impacting our community.





Mikinduri Children of Hope

Provincial Credit Union Stratford Branch Manager Brian Gallant (right) with Ted Grant, representing the Mikinduri Children of Hope. Our credit union has made regular donations over the years to the charitable organization, which helps to feed thousands of hungry children a nutritious meal, in the Mikinduri area of Kenya.

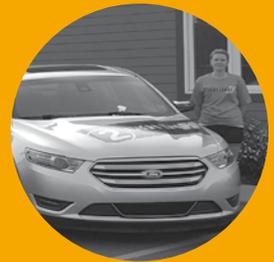
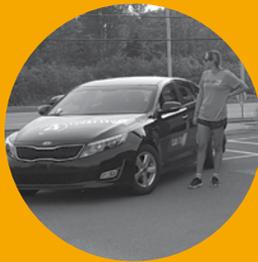
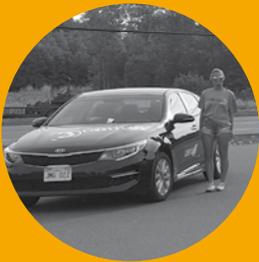
Gulf Shore Kindergarten Visit

Each year the Kindergarten Class at Gulf Shore Consolidated School makes a visit to our Stella Maris Branch in North Rustico. The kids have a wonderful time checking out the vault, and helping to count money! Shown here is Provincial's Colleen M. Doiron spending time with a student.



Cash Dash 2.0

The Cash Dash, our amazing-race styled event, returned this year with added challenges for participants. Instead of a single day event across PEI, the four teams of two raced for two days across three provinces—PEI, New Brunswick, and Nova Scotia. This year the tasks and services focused on the cooperative movement, with activities like balancing ledgers and earning community support. Teams competed against each other for the grand prize of \$5,000. Our following built upon last year's success, with a tremendous response to both interest and overall online social interactions.



The Do Good Project

As a cooperative financial institution, credit unions truly believe in giving back and bettering the communities they serve. In 2016, we launched The Do Good Project, which gave the public the opportunity to decide how to make a positive impact within their neighborhood. In addition to coming up with the ideas, the public also chose the two winning projects based on popular vote.

We had an overwhelming response to this contest; eight plans submitted and close to two thousand votes cast.

The top two finalists, Lynn Thompson and Lewie Sutherland, earned \$2,500 each to make their community plans a reality. Lynn Thompson will be using the money to enhance the outdoor play-space at Morell Early Learning Centre, and Lewie Sutherland will be improving the Alysha Toombs Memorial Park in Kensington.

A decade of Relay For Life

2016 marked our tenth and final year as the proud provincial event sponsor for the Canadian Cancer Society's Relay For Life. Since 2006, PEI credit unions have together contributed over \$500,000 towards cancer research - with an impressive 60% being staff raised. Through this partnership, we have increased staff's involvement with the Society, educated our stakeholders about cancer prevention and raised significant funds to assist in the delivery of the Society's programs on PEI.

In June we were honored to be recognized as Outstanding Sponsorship Partner at the 30th Annual Maritime Philanthropy Awards thanks to a nomination by the Canadian Cancer Society. We would like to extend our gratitude to the Society for allowing us to be an active part of this amazing initiative over the past 10 years.



Fill The YuMob

In December our fourth Annual #FilltheYuMob took place, where not one, but TWO, carloads of toys were collected. All toys were given to Santa's Angels, a volunteer group that delivers the toys on Christmas Day to over 300 local families in need. Thank you to everyone who participated in this notable cause.

Scholarships

We are pleased to announce 5 Provincial Credit Union Scholarship Recipients for 2016. Each scholarship recipient received \$1,500 towards furthering their education. In total, Provincial Credit Union distributed \$7,500.
Not Pictured: Dylan May

We wish all students the best in their studies and future endeavors.



Georgia Potter



Grace Clow



Lacey Rogers



Liam Hatton

Investing In People

Investing in People, our primarily social media based campaign, aims to make a small positive financial impact for individuals during their day to day lives. From paying for car services, to helping furnish a student's new apartment, we have helped Islanders from tip to tip. Since its inception in 2015, over one hundred individuals have benefited, which we hope to grow in the upcoming year.

For 2016, we tried to change things up for the holiday season by launching Investing in Cheer.

Three individuals were each given \$500 to spread some much needed Christmas cheer to deserving groups. These groups included the QEH pediatrics unit, Boys and Girls Club Charlottetown, and two families in need in the Kinkora area.



Inspire Learning Centre

Credit unions on PEI were proud to partner with the new and innovative Inspire Learning Centre in 2016. Located in Summerside the state-of-the-art regional learning centre is a bustling hub for job seekers, entrepreneurs, study groups and people of all ages!

The Inspire Learning Centre, dubbed the “library of tomorrow” offers state of the art facilities including semi-private reading pods, collaborative workstations and borrowable media in every category! Credit unions look forward to the year ahead with the Inspire Learning Centre and the impact it will make on the community and surrounding areas.



Junior Achievement



2016 marked an important partnership for the credit union system on PEI as we teamed up with Junior Achievement to bring our financial knowledge into the classroom. Through JA PEI's Economics for Success program, the credit union has been able to instruct over 1,500 students on the fundamentals of financial literacy and the significance of budgeting.

As a result of the successful and well-received programming, credit union employee, Kate Ryan was awarded JA PEI's Volunteer of the Year award in 2016. Credit unions will continue their partnership with JA for the upcoming year with 500 students already enrolled for the programs upcoming semester.

PEI Symphony

Provincial Credit Union Commercial Account Manager Katelyn Godfrey from Charlottetown office, makes a \$1500 to PEI Symphony President Bruce Craig.

Funds assist in the supporting and mentoring of young talented island musicians who attend secondary schools including UPEI, and go on to gain invaluable experience by playing side-by-side with seasoned professionals.



Town and Country Aquatics Plus

Town and Country Aquatics Plus board member David Miles, left, accepts a \$5,000 donation from Provincial Credit Union in Montague. Presenting the donation were Branch Manager Tanya Ramsay and Commercial Account Manager Jarret O'Rourke. Provincial's donation helped to refurbish the gym and pool facility, which recently re-opened under the management of a new board of directors.



Financial Statements

INDEPENDENT AUDITOR'S REPORT

To the Members of Provincial Credit Union Ltd.

Report on the Financial Statements

We have audited the accompanying financial statements of Provincial Credit Union Ltd., which comprise the statement of financial position as at December 31, 2016 and the statements of comprehensive income, changes in members' equity and cash flow 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 Provincial Credit Union Ltd. as at December 31, 2016 and its financial performance and its cash flow for the year then ended in accordance with International Financial Reporting Standards.

MRSB Chartered Professional Accountants

MRSB CHARTERED PROFESSIONAL ACCOUNTANTS

Charlottetown, PE

February 21, 2017

PROVINCIAL CREDIT UNION LTD.
Statement of Financial Position
December 31, 2016

	2016	2015
Assets		
Cash and cash equivalents (Note 4)	\$ 12,952,545	\$ 18,055,800
Investments (Note 5)	45,961,675	57,765,606
Accounts receivable (Note 6)	6,962,631	2,057,083
Income taxes recoverable	-	396,504
Member loans and mortgages (Note 7)	251,497,490	229,438,463
Provision for impaired loans (Note 8)	(377,531)	(737,648)
Prepaid expense	189,798	193,985
Deferred tax asset (Note 10)	332,399	343,433
Property and equipment (Schedule 1)	2,874,388	3,016,193
Due from CU PEI Investment Corp. (Note 11)	1,999,487	890,723
Real estate held for resale	37,068	671,781
	\$322,429,950	\$312,091,923
Liabilities		
Accounts payable and accrued liabilities	\$ 339,107	\$ 346,641
Employee benefits payable	1,222,764	1,241,150
Accrued interest payable	1,279,202	1,352,225
Income taxes payable	64,027	-
Member deposits (Note 12)	249,098,523	241,268,009
Share deposits	39,549,654	38,110,761
	291,553,277	282,318,786
Contingent liabilities (Note 13)		
Members' equity		
Members' shares (Statement 4)	77,510	81,025
Undistributed earnings (Statement 4)	30,799,163	29,692,112
	30,876,673	29,773,137
	\$322,429,950	\$312,091,923

ON BEHALF OF THE BOARD


 _____ Director


 _____ Director

Notes 1 - 21 are an integral part of these financial statements

PROVINCIAL CREDIT UNION LTD.
Statement of Changes in Members' Equity
Year Ended December 31, 2016

	2016	2015 (15 months)
Members' shares (Note 14)		
Balance - beginning of period	\$ 81,025	\$ 74,025
Issuance (redemption) of members' shares, net	<u>(3,515)</u>	<u>7,000</u>
Balance - end of period	<u>77,510</u>	<u>81,025</u>
Undistributed earnings		
Balance - beginning of period	29,692,112	23,911,811
Net comprehensive income (Statement 5)	1,107,051	2,032,135
Increase in undistributed earnings from amalgamation	<u>-</u>	<u>3,748,166</u>
Balance - end of period	<u>30,799,163</u>	<u>29,692,112</u>
Members' equity	<u>\$ 30,876,673</u>	<u>\$ 29,773,137</u>

PROVINCIAL CREDIT UNION LTD.
Statement of Comprehensive Income
Year Ended December 31, 2016

	2016	2015 (15 months)
Income		
Interest and investment	\$ 10,290,929	\$ 12,790,129
Cost of capital and borrowings (Note 15)	<u>2,563,669</u>	3,529,055
Financial margin	<u>7,727,260</u>	9,261,074
Other		
Commissions	2,547,361	3,421,347
Miscellaneous	147,989	233,976
Dividends	-	307,589
	<u>2,695,350</u>	3,962,912
	<u>10,422,610</u>	13,223,986
Expenses		
Advertising and promotions	393,925	494,605
Amalgamation	-	51,847
Amortization of property and equipment	208,292	295,710
Automated teller machines	111,274	188,757
Credit Union development	9,636	25,767
Data processing	930,056	522,254
Democracy	128,691	68,478
Dues and memberships	3,560	6,180
Insurance	459,027	552,858
Miscellaneous	27,171	67,139
Office	316,892	395,288
Premises	341,876	400,874
Professional fees	65,020	74,432
Provision for impaired loans	95,047	159,115
Service fees	1,672,690	2,387,521
Telephone	47,952	69,124
Travel	19,844	28,791
Wages and wage levies	<u>3,948,406</u>	4,757,305
	<u>8,779,359</u>	10,546,045
Income before income taxes	<u>1,643,251</u>	2,677,941
Income taxes (recovery)		
Current (Note 16)	525,166	684,803
Deferred	<u>11,034</u>	(38,997)
	<u>536,200</u>	645,806
Net comprehensive income	<u>\$ 1,107,051</u>	\$ 2,032,135

Notes 1 - 21 are an integral part of these financial statements

PROVINCIAL CREDIT UNION LTD.

Statement of Cash Flow

Year Ended December 31, 2016

	2016	2015 (15 months)
Cash flows from operating activities		
Net comprehensive income	\$ 1,107,051	\$ 2,032,135
Items not affecting cash:		
Amortization of property and equipment	208,292	295,710
Deferred income taxes	11,034	(38,997)
Increase in deferred income tax asset from amalgamation	-	(45,301)
	1,326,377	2,243,547
Changes in non-cash working capital:		
Investments	11,803,931	1,198,663
Accounts receivable	(4,905,548)	(844,827)
Prepaid expense	4,187	(67,006)
Accounts payable and accrued liabilities	(7,535)	84,576
Employee benefits payable	(18,386)	277,336
Accrued interest payable	(73,023)	(125,038)
Income taxes payable	460,531	(588,400)
	7,264,157	(64,696)
	8,590,534	2,178,851
Cash flows from investing activities		
Increase in member loans and mortgages, net of provision	(22,419,144)	(42,987,284)
(Increase) decrease in real estate held for resale	634,713	(616,781)
Purchase of property and equipment	(66,486)	(304,185)
Increase in property and equipment from amalgamation	-	(442,273)
	(21,850,917)	(44,350,523)
Cash flows from financing activities		
Increase in member deposits	7,830,514	45,251,065
Increase in share deposits and members' shares	1,435,378	1,240,251
(Increase) decrease in amount due from CU PEI Investment Corp.	(1,108,764)	800,300
Increase in undistributed earnings from amalgamation	-	3,748,166
	8,157,128	51,039,782
Net change in cash and cash equivalents	(5,103,255)	8,868,110
Cash and cash equivalents - end of period	18,055,800	9,187,690
Cash and cash equivalents - end of period	\$ 12,952,545	\$ 18,055,800
Cash flow supplementary information		
Interest received	\$ 10,279,618	\$ 13,540,706
Interest paid	2,461,875	3,203,020
Income taxes paid (recovered)	(857,643)	493,241

Notes 1 - 21 are an integral part of these financial statements

Notes to the Financial Statements

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

1. DESCRIPTION OF BUSINESS

On October 1, 2013 Metro Credit Union Limited amalgamated with Stella Maris Credit Union Limited to form Provincial Credit Union Ltd. On January 1, 2015 the Provincial Credit Union Ltd. amalgamated with Montague Credit Union Ltd and is operating under Provincial Credit Union Ltd. It is incorporated under the Companies Act of Prince Edward Island and is governed by the Prince Edward Island Credit Unions Act. Provincial Credit Union Ltd. is a member-owned financial institution whose principal business activities include financial and banking services for its members at its branches in Charlottetown, Stratford, Montague and North Rustico, Prince Edward Island.

These financial statements were authorized for issue by the Board of Directors on February 21, 2017.

All Credit Unions on Prince Edward Island have changed their year end date from September 30 to December 31 to coincide with most other Credit Unions in the Atlantic Canada region. Provincial Credit Union Limited's financial statements for the year ended December 31, 2016 are comprised of 12 months, compared to 15 months for the period ended December 31, 2015. As a result, the amounts presented in the financial statements are not entirely comparable.

2. BASIS OF PRESENTATION

These financial statements have been prepared in accordance with and are in compliance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). The principal accounting policies applied in the preparation of the financial statements are set out in Note 3.

These financial statements have been presented on the historical cost basis except for certain financial instruments as indicated in Note 3. These financial statements are presented in Canadian dollars, which is the Credit Union's functional currency.

3. SIGNIFICANT ACCOUNTING POLICIES

Cash and cash equivalents

Cash and cash equivalents is comprised of cash on hand and cash in financial institutions.

Investments

Investments for which there are quoted prices in an active market are carried at fair value by the Credit Union. Unrealized gains or losses are reported as part of net comprehensive income. Investments for which there is not an active market are carried at amortized cost, except when it is established that their value is impaired. Impairment losses, or reversal of previously recognized impairment losses, are reported as part of net comprehensive income.

Accounts receivable

Accounts receivable arise from miscellaneous rebates and accrued interest on loans and mortgages and investments. An allowance for bad debts has been calculated through discussions with management, assessment of the other circumstances influencing the collectibility of amounts, and using historical loss experience. Amounts deemed uncollectible are written off and deducted from the carrying value of the receivable. Amounts subsequently recovered from accounts previously written off are credited to the allowance account in the period of recovery.

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PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Loans and mortgages

Member loans and mortgages are initially measured at fair value, net of origination fees and inclusive of transaction costs incurred. Member loans and mortgages are subsequently measured at amortized cost, using the effective interest rate method, less any impairment losses.

Member loans and mortgages are reported at their recoverable amount representing the aggregate amount of principal, less any allowance or provision for impaired loans plus accrued interest. Interest is accounted for on the accrual basis for all loans and mortgages.

Impairment

Loans and mortgages are considered impaired when there has been deterioration in credit quality. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Credit Union makes judgments as to whether there is any observable data indicating an impairment followed by a measurable decrease in the estimated future cash flows from a loan or mortgage. Deterioration of estimated future cash flows is determined considering the financial condition of the borrower, payment history, and security pledged.

The Credit Union first assesses whether objective evidence of impairment exists individually for member loans and mortgages. If it is determined that no objective evidence of impairment exists for individual assets, the asset is included in a group of financial assets with similar credit characteristics and that group is assessed collectively for impairment. Assets that are individually assessed for impairment are not included in the collective assessment. The expected cash flows for a group of financial assets with similar credit risk characteristics are estimated based on historical loss experience, future estimates based on current events, and objective evidence of impairment similar to those in the portfolio.

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

Member loans and mortgages considered uncollectible are written off.

Interest on an impaired loan or mortgage continues to be recognized in earnings on an accrual basis and is provided for in the provision from impaired loans. At December 31, 2016, there was no interest accrued on impaired loans and mortgages (2015 - \$NIL).

Non-financial assets are assessed for impairment at least annually and, where impairment exists, the carrying value is reduced to the recoverable amount.

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred income taxes

Income tax expense comprises current and deferred tax.

Current income taxes are recognized for the estimated income taxes payable or receivable on taxable income or loss for the current period and any adjustment to income taxes payable in respect of previous periods. Current income taxes are measured at the amount expected to be recovered from or paid to the taxation authorities. This amount is determined using tax rates and tax laws that have been enacted or substantively enacted by the year end date.

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base, except for taxable temporary differences arising on the initial recognition of goodwill and temporary differences arising on the initial recognition of an asset or liability in a transaction and at the time of the transaction affects neither accounting or taxable profit or loss.

Recognition of deferred tax assets for unused tax losses, tax credits, and deductible temporary differences is restricted to those instances where it is probable that future taxable profit will be available which allows the deferred tax asset to 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.

The amount of the deferred tax asset or liability is measured at the amount expected to be recovered from or paid to the taxation authorities. This amount is determined using tax rates and tax laws that have been enacted or substantively enacted by the year end date and are expected to apply when the liabilities/assets are settled/recovered.

Property and equipment

Property and equipment is stated at cost less accumulated amortization. Property and equipment is amortized over its estimated useful life at the following rates and methods:

Buildings	5%	straight-line method
Buildings	5%	declining balance method
Equipment	20%	declining balance method
ATMs	20%	straight-line method
Computer hardware	30%, 45%, and 55%	declining balance method
Pavement	8%	declining balance method
Computer software	100%	declining balance method

One-half of the annual rate is recorded in the year of acquisition; no amortization is recorded in the year of disposal.

Finance charges

The Credit Union periodically purchases mortgages from Concentra Financial, Omista Credit Union, and League Savings and Mortgage. Generally a premium is paid for the mortgages purchased, calculated by reference to the interest rate inherent in the mortgages and the rate of interest in effect at the time of purchase. The premium paid is amortized using the straight-line method over the life of the mortgage purchase plan and is netted to the applicable mortgage asset.

Fees related to the purchase of Index-Linked RRSP units are amortized using the straight-line method over the term of the investment and are netted against the cost of the liability.

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PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Real estate held for resale

Real estate held for resale is carried at the market value of the loan or mortgage foreclosed, adjusted for estimates of revenues to be received and costs to be incurred subsequent to foreclosure, and the estimated net proceeds from the sale of the assets.

Employee future benefits

The Credit Union records annually the estimated liabilities for pension and other benefit obligations, which are payable to its employees in subsequent years under the Credit Union's policy.

The Credit Union provides post employment benefits through a defined contribution plan. Pension expenses for the defined contribution pension plan include the required employer contributions. Contributions to the plan are recognized as an expense in the period that the relevant employee services are rendered. During the period, the contributions by the Credit Union to the defined contribution pension plan were \$235,490 (2015 - \$258,287).

Liabilities are recorded for employee benefits including salaries and wages, deductions at source, paid annual or sick leave, and bonuses that are expected to be settled within 12 months of the financial statement date. These represent present obligations resulting from employees' services provided to the financial statement date and are calculated at the undiscounted amounts based on the remuneration rate that the Credit Union expects to pay at the financial statement date. The expected cost bonus payments is recognized as a liability when the Credit Union has a present legal or constructive obligation to pay as a result of past events and the obligation can be estimated reliably.

Benefits such as medical care are non-vesting and are expensed by the Credit Union as the benefits are taken by the employees.

Severance benefits are recognized as an expense when the Credit Union is committed, without realistic opportunity for withdrawal, to a formal detailed plan to provide severance benefits under certain circumstances. If material benefits are payable more than 12 months after the reporting period, they are discounted to their present value.

Member deposits

Deposits are measured at fair value on recognition, net of transaction costs directly attributable to issuance. Subsequent measurement is at amortized cost using the effective interest method. Chequing accounts, call deposits, and term deposits are on a call basis and earn interest at various rates.

Share deposits pay a dividend return at the discretion of the Board of Directors. Privileges of the shares are under the authority of the Board of Directors. The dividend rate declared and paid for 2016 was 0.5% (2015 - 0.5%), and was based on the average of the lowest monthly share balances.

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Share deposits

The Credit Union has authorized an unlimited number of voting equity shares, with a value of \$5 per share. The shares are non-transferable, redeemable by the Credit Union, retractable by members subject to the Credit Union's right to suspend redemption, if the redemption would impair the financial stability of the Credit Union, for a period of up to twelve months by Board resolution and indefinitely by Board resolution with the approval of the Credit Union Deposit Corporation.

As at the financial statement date, the Credit Union has 15,502 member shares issued and outstanding with a value of \$77,510 (2015 - 16,205 shares with a value of \$81,025).

Revenue and expense recognition

Revenues are recognized to the extent that it is probable that the economic benefits will flow to the Credit Union and the revenue can readily be measured. The principal sources of revenue are interest and fee income. Interest on loans and mortgages is recognized and reported on an accrual basis using the effective interest method. Dividend income is recognized when the shareholder's right to receive payment is established.

Operating expenses are recognized upon the utilization of the services or at the date of their origin. Expenses incurred directly in the origination of loans and mortgages are deferred and recognized in the statement of comprehensive income, as a reduction to income over the expected life of the relevant loans and mortgages.

Foreign currency translation

Accounts in foreign currencies have been translated into Canadian dollars using the temporal method. Under this method, monetary assets and liabilities have been translated at the period end exchange rate. Non-monetary assets have been translated at the rate of exchange prevailing at the date of transaction. Revenues and expenses have been translated at the average rates of exchange during the year, except for amortization, which has been translated at the same rate as the related assets.

Foreign exchange gains and losses on monetary assets and liabilities are included in the determination of net comprehensive income.

Measurement uncertainty

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Credit Union's accounting policies. The estimates and underlying assumptions are continually reviewed on an ongoing basis based on historical experience, best knowledge of current events and conditions, and other factors that are believed to be reasonable under the circumstances, including expectations of future events. The resulting accounting estimates will, by definition, seldom equal the related actual results, and actual results may ultimately differ from these estimates.

Revisions to accounting estimates are recorded in the period in which the estimate is reversed if the revision affects only that period or in the period of revision and in future periods if the revision affects both the current and future periods.

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Measurement uncertainty (continued)

The areas involving a high degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements include the provision for impaired loans, measurement of employee benefits, and the estimates of useful lives for depreciation of property and equipment.

Financial instruments

The Credit Union classifies its financial assets and financial liabilities according to their characteristics and management's intentions related thereto for the purposes of ongoing measurements. Financial assets and liabilities are initially recognized at fair value regardless of classification choice and are subsequently accounted for based on their classification as described below.

Financial assets must be classified as fair value through profit or loss (FVTPL), available for sale (AFS), held-to-maturity (HTM), or loans and receivables (L&R). Financial liabilities are required to be classified as FVTPL or other financial liabilities (OFL). All financial instruments, including all derivatives, are measured at fair value on the statement of financial position with the exception of loans and receivables, held-to-maturity investments and other financial liabilities which are measured at amortized cost.

A financial asset is derecognized when the contractual rights to the cash flows from the asset have expired, or the Credit Union transfers the contractual rights to receive the cash flows from the asset, or has assumed an obligation to pay those cash flows to a third party and the Credit Union has transferred all of the risks and rewards of ownership of that asset to a third party. A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

Changes in fair value of financial assets and financial liabilities classified as FVTPL are reported in net income, while the changes in value of available for sale financial assets are reported within other comprehensive income (OCI) until the financial asset is disposed of, or becomes impaired.

Accumulated OCI is reported on the statement of financial position as a separate component of members' equity. It includes, on a net of taxes basis, the net unrealized gains and losses on available for sale financial assets. The Credit Union has classified its equity investments as AFS; however, because there is no active market for these investments and their fair value cannot be estimated reliably, the Credit Union has not recorded any other comprehensive income as a result of these.

The Credit Union has classified its financial instruments as follows:

FVTPL	Cash and cash equivalents
AFS	Investments - shares
HTM	Investments - debentures
L&R	Accounts receivable, member loans and mortgages and amount due from CU PEI Investment Corp.
OFL	Accounts payable and accrued liabilities, employee benefits payable, accrued interest payable, member deposits and share deposits

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

The Credit Union utilizes settlement date accounting for all purchases and sales of financial assets in its investment portfolio. Transactions costs other than those related to financial instruments classified as fair value through profit or loss, which are expensed as incurred, are added to the fair value of the financial asset or liability on initial recognition and amortized using the effective interest method.

Changes in accounting standards

A number of new standards, and amendments to standards and interpretations, are not yet effective for the year ended December 31, 2016 and have not been adopted by the Credit Union in preparing these financial statements. Other than the introduction of IFRS 9, these changes are not expected to have a material impact on the financial statements.

IFRS 9 - Financial Instruments

In 2009 and 2010, the IASB issued IFRS 9 Financial Instruments which contains new requirements for accounting for financial assets and liabilities, and will contain new requirements for impairment and hedge accounting, replacing the corresponding requirements in IAS 39. It will lead to significant changes in the way the Credit Union accounts for financial instruments. The key changes issued and proposed relate to:

- Financial assets - financial assets will be held at either fair value or amortized cost, except for equity investments not held for trading and certain eligible debt instruments, which may be held at fair value through other comprehensive income;
- Financial liabilities - gains and losses on fair value changes arising on non-derivative financial liabilities designated at fair value through profit or loss will be taken to other comprehensive income;
- Impairment - credit losses expected (rather than only losses incurred in the year) on loans, debt securities and loan commitments not held at fair value through profit or loss will be reflected in impairment allowances; and
- Hedge accounting - hedge accounting will be more closely aligned with financial risk management.

In 2014, the IASB tentatively decided that the mandatory effective date of IFRS 9 will be for annual periods beginning on or after January 1, 2018. The impact of IFRS 9 on the Credit Union has not yet been determined.

The IASB has issued two new standards, IFRS 16 Leases and IFRS 15 Revenue from Contracts with Customers which are effective for annual periods beginning on or after January 1, 2019 and January 1, 2018, respectively. The Credit Union is currently assessing the impact of these standards.

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value of financial instruments

The determination of the fair value of financial instruments requires the exercise of judgement by management. The fair value of financial instruments traded in active markets at the financial statement date is based on their quoted market prices. Where independent quoted market prices do not exist, fair value may be based on other observable current market transactions or based on a valuation technique which maximizes the use of observable market inputs.

For certain types of equity instruments, fair value is assumed to approximate carrying value where the range of reasonable valuation techniques is significant and the probabilities of such valuation techniques cannot be reasonably assessed. In such instances, fair value may not be reliably measurable due to the equity instruments' unique characteristics, including trading restrictions or that quoted market prices for similar securities are not available.

4. CASH AND CASH EQUIVALENTS

	<u>2016</u>	<u>2015</u>
Cash in financial institutions	\$ 10,375,281	\$ 15,412,189
Cash on hand	<u>2,577,264</u>	<u>2,643,611</u>
	<u>\$ 12,952,545</u>	<u>\$ 18,055,800</u>

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

5. INVESTMENTS

	<u>2016</u>	<u>2015</u>
Shares		
Atlantic Central Credit Union Limited - common shares	\$ 2,944,580	\$ 2,755,500
Atlantic Central Credit Union Limited - Class B preferred shares	821,400	821,400
Atlantic Central Union Limited Class LSM Shares	416,603	416,603
Concentra Financial Class D preferred shares	250,000	250,000
League Data 10.034 Class B Preferred Shares	100,340	100,340
Atlantic Central Union Limited Class PEI shares	2,400	2,400
CU PEI Investment Corp. - 2,000 Class A common shares, 25 Class B common shares, and 1,510 Class A preferred shares	60	60
Concentra shares	10	10
	<u>4,535,393</u>	<u>4,346,313</u>
Debentures		
Atlantic Central Credit Union Limited liquidity - 0.82%	19,790,994	18,919,293
League Savings and Mortgage - 1.50%; matures February 6, 2017	7,105,288	7,000,000
Atlantic Central - 1.7%; matures April 2, 2018	5,000,000	5,000,000
Concentra Financial - 1.5%; matures January 10, 2017	5,000,000	2,000,000
Atlantic Central Credit Union Limited - 1.50%; matures March 10, 2017	2,030,000	2,000,000
Concentra Financial - 2.36%; matures July 9, 2017	1,500,000	1,500,000
Concentra Financial - 2.60%; matures July 9, 2018	1,000,000	1,000,000
Concentra - 1.55%; matured August 8, 2016	-	10,000,000
Atlantic Central Credit Union Limited - 1.55%; matured May 7, 2016	-	4,000,000
Concentra Financial - 1.05%; matured April 8, 2016	-	2,000,000
	<u>41,426,282</u>	<u>53,419,293</u>
	<u>\$ 45,961,675</u>	<u>\$ 57,765,606</u>

Liquidity deposits are investments placed with Atlantic Central Credit Union Limited to provide protection against cash flow demands. National standards have been established requiring 6% of Provincial Credit Union Ltd. assets to be held on deposit.

6. ACCOUNTS RECEIVABLE

	<u>2016</u>	<u>2015</u>
Miscellaneous receivables	\$ 6,239,605	\$ 1,290,208
Accrued interest - loans and mortgages	500,361	489,978
Accrued interest - investments	222,665	276,897
	<u>\$ 6,962,631</u>	<u>\$ 2,057,083</u>

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

7. MEMBER LOANS AND MORTGAGES

2016	Total loans	Specific allowance	Net loans
Mortgages	\$ 85,344,908	\$ (47,000)	\$ 85,297,908
Commercial	75,345,820	(141,864)	75,203,956
Concentra mortgage syndication	42,734,778	-	42,734,778
Indirect auto	14,802,780	(153,000)	14,649,780
Lines of credit and overdrafts	13,598,130	(26,063)	13,572,067
Personal	8,162,191	(9,604)	8,152,587
Farming and fishing	6,359,123	-	6,359,123
League Savings & Mortgage high ratio mortgages	2,912,065	-	2,912,065
Omista mortgage pool	2,237,695	-	2,237,695
	\$251,497,490	\$ (377,531)	\$251,119,959

2015	Total loans	Specific allowance	Net loans
Mortgages	\$ 78,177,870	\$ (145,000)	\$ 78,032,870
Commercial	67,397,542	(318,356)	67,079,186
Concentra mortgage syndication	27,979,021	-	27,979,021
Indirect auto	18,817,501	(260,244)	18,557,257
Lines of credit and overdrafts	16,516,116	-	16,516,116
Personal	8,632,806	(14,048)	8,618,758
Farming and fishing	5,701,815	-	5,701,815
League Savings & Mortgage high ratio mortgages	3,863,371	-	3,863,371
Omista mortgage pool	2,352,421	-	2,352,421
	\$229,438,463	\$ (737,648)	\$228,700,815

8. PROVISION FOR IMPAIRED LOANS

	2016	2015
Provision for impaired loans - beginning of period	\$ 737,648	\$ 686,330
Provision for impaired loans	95,047	159,115
Transfer upon amalgamation	-	186,400
Recovery of loans written off	42,211	68,477
Loans written off - current period	(497,375)	(362,674)
Provision for impaired loans - end of period	\$ 377,531	\$ 737,648

Members' loans can have either variable or fixed rate of interest. The rates offered to members are determined by the type of security offered, the member's credit worthiness, competition from other lenders, and the current prime rate.

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

9. LOANS IN ARREARS

The following is an analysis of loans in arrears based on the age of repayments outstanding:

	<u>2016</u>	<u>2015</u>
31 to 60 days	\$ 302,381	\$ 407,775
61 to 90 days	3,095	550,304
91 to 180 days	1,061	20,920
Over 180 days	5,020	213,699
	<u>\$ 311,557</u>	<u>\$ 1,192,698</u>

10. DEFERRED TAX ASSET

Deferred income taxes reflects the tax consequences of 'temporary differences' between the statement of financial position carrying amounts and the tax bases of assets and liabilities. These deferred income taxes are calculated using the income tax rates and tax laws that are expected to apply when these temporary differences are reflected in taxable income.

Temporary differences which give rise to deferred income tax assets are as follows:

	<u>2016</u>	<u>2015</u>
Property and equipment	\$ 128,228	\$ 131,341
Retirement allowance	204,171	212,092
	<u>\$ 332,399</u>	<u>\$ 343,433</u>

11. DUE FROM CU PEI INVESTMENT CORP.

Provincial Credit Union Ltd. owns Class A and B common shares of CU PEI Investment Corp. The amount due from CU PEI Investment Corp. bears interest at 1% and there are no set terms of repayment. Interest earned on the investment during the period was \$14,520 (2015 - \$10,442).

12. MEMBER DEPOSITS

	<u>2016</u>	<u>2015</u>
Chequing accounts	\$ 73,537,238	\$ 66,465,530
Term deposits	57,037,011	59,255,409
Registered Retirement Savings Plan (RRSP) deposits	45,220,193	47,659,063
Call deposits	33,353,722	32,734,736
Tax Free Savings Account (TFSA) deposits	23,275,294	19,876,873
Registered Retirement Income Fund (RRIF) deposits	16,675,065	15,276,398
	<u>\$249,098,523</u>	<u>\$241,268,009</u>

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

13. CONTINGENT LIABILITIES

Provincial Credit Union Ltd. has provided letters of credit on behalf of members in the amount of \$70,000.

14. MEMBERS' SHARES

	Number of shares	December 31 2016	Number of shares	December 31 2015
Balance - beginning of period	16,205	\$ 81,025	14,805	\$ 74,025
Shares issued (redeemed), net	(703)	(3,515)	1,400	7,000
Balance - end of period	15,502	\$ 77,510	16,205	\$ 81,025

15. COST OF CAPITAL AND BORROWINGS

	2016	2015
Interest and service charges	\$ 2,383,774	\$ 3,266,847
Share dividends	179,895	262,208
	\$ 2,563,669	\$ 3,529,055

16. INCOME TAXES

The income tax provision recorded differs from the income tax obtained by applying the statutory income tax rate of 31.00% (2015 - 31.11%) to the income for the year and is reconciled as follows:

	2016	2015
Income before income taxes	\$ 1,643,251	\$ 2,677,941
Income tax expense at the combined basic federal and provincial tax rate:	\$ 509,408	\$ 833,107
Increase (decrease) resulting from:		
Capital cost allowance claimed in excess of amortization	(983)	10,739
Dividends	-	(95,353)
Non-deductible expenses	44,034	(62,127)
Adjustment to previous year	(2,991)	6
Tax reserves	87,334	42,904
Provision for loan loss reserve	29,465	47,579
Recovery of loans previously written off	13,085	15,028
Loans written off in the current year	(154,186)	(105,511)
Adjustments for October to December 2014 tax provision included in 15 month financial statements	-	(1,569)
Effective tax expense	\$ 525,166	\$ 684,803

The effective income tax rate is 31.96% (2015 - 25.57%).

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

17. LINE OF CREDIT AVAILABILITY

Provincial Credit Union Ltd. has an approved line of credit with Atlantic Central Credit Union Limited for \$6,100,000 which is due for renewal on December 1, 2017 and was not utilized at the year end. The line of credit bears an interest rate of 2.2% and is secured by a general security agreement.

18. RELATED PARTY TRANSACTIONS

Provincial Credit Union Ltd. provides financial services to members. These members hold the loans, deposits and share deposits and therefore the interest income and interest expense are transacted in the ordinary course of business with these members.

As at year end, some members of the Board of Directors, management, and employees had loans and mortgages from Provincial Credit Union Ltd. These loans and mortgages were in the normal course of operations with interest rates at the regular rates offered to all members of the Credit Union. Interest rates on deposits and dividends on shares were at identical rates offered to all Credit Union members.

Key management personnel include the General Manager and other senior officers of the Credit Union. The components of total compensation received by key management personnel and balances due to and from key management personnel including only non-joint accounts are as follows:

	<u>2016</u>	<u>2015</u>
Short-term employee benefits	\$ 1,034,128	\$ 1,006,897
Contributions to a retirement pension plan	54,067	64,276
Mortgages, loan balances, and lines of credit due from key management at December 31	135,683	372,193
Deposit balances due to key management at December 31	159,460	144,972

Short-term employee benefits include salaries, variable compensation, and other benefits. The mortgage and deposit transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

19. RISK MANAGEMENT

The Credit Union manages significant risks through a comprehensive infrastructure of policies, procedures, methods, oversight, and independent review designed to reduce the significant risks and to manage those risks within an appropriate threshold. The Board of Directors is provided with timely, relevant, accurate, and complete reports on the management of significant risks. Significant risks managed by the Credit Union include credit, liquidity, currency, and interest rate risks.

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

19. RISK MANAGEMENT (continued)

Credit risk

Credit risk is the risk that a member will fail to meet their obligation to the Credit Union. Providing credit facilities to qualified members is one of the Credit Union's primary sources of earnings and is the area where the Credit Union is exposed to the most significant risk. Approval of these facilities is based on the member's ability to repay principal and interest over the term of the facility, which is determined by following Board approved policies and procedures, which includes assessing the member's credit history, character, collateral, and debt servicing capacity. In addition, the Credit Union provides to its employees comprehensive training to ensure compliance with Credit Union lending policies and procedures. Also, formal policies governing approval of credit facilities including acceptable risk assessment and security requirements are in place.

Overdue loan accounts, or lending delinquency, is closely monitored and frequently reported to senior management to ensure all allowances for potential loan losses are adequately provided for and written-off when collection efforts have been exhausted. Credit risk is mitigated primarily by the nature and quality of the underlying security as described by approved lending agreements.

The Credit Union's loan portfolio is focused in two main areas: consumer loans and mortgages and commercial loans and mortgages, the latter of which are to mainly small and mid-sized companies. A syndication process is available with other Credit Unions for larger commercial loans, when considered necessary, to appropriately mitigate the Credit Union's credit risk. Consumer mortgages are made available on a conventional basis up to 80% of the lesser of cost or appraised value of single family housing, up to 75% on other residential properties, up to 65% of the lesser of cost or appraised value on commercial properties having general purpose usage, and up to 50% of the lesser of cost or appraised value on commercial properties designed for specific use. Other credit facilities provided include personal overdrafts that have no recourse to the Credit Union.

The Credit Union maintains both specific and collective allowances for credit losses. Specific allowances are established on an account by account basis using management's knowledge of the account and prevailing conditions. In addition, accounts delinquent greater than ninety days are included in the specific allowance. Collective allowances are maintained to cover any impairment in the loan portfolio that cannot yet be associated with specific loans and includes factors such as market conditions, concentration of credit risk for member accounts, and the general state of the economy. Senior management regularly monitors credit risk and reports to the Board of Directors on a monthly basis.

The Credit Union's maximum exposure to credit risk at the reporting date in relation to each class of recognized financial asset is the carrying amount of those assets indicated in the statement of financial position. The maximum credit exposure does not take into account the value of any collateral or other security held, in the event parties fail to perform their obligations. The principal collateral and other credit enhancements held as security for loans include a) insurance and mortgages over properties, b) recourse to sell assets such as real estate, equipment, inventory, and accounts receivable and c) recourse to liquid assets, guarantees, and securities.

Cash and equivalents and investments have low credit risk exposure as these assets are high quality investments with low risk counterparties. For the loan portfolio, the Credit Union reviews the member's capacity to repay the loan rather than relying exclusively on collateral.

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

19. RISK MANAGEMENT (continued)

Liquidity risk

Liquidity risk is the risk of being unable to meet financial commitments without having to raise funds at unreasonable prices or sell assets on a forced basis. The Credit Union has established policies to ensure the Credit Union is able to generate sufficient funds to meet all of its financial commitments in a timely and cost effective manner. The Credit Union's liquidity management practices include ensuring the quality of investment acquired for liquidity purposes meet very high standards, matching maturities of assets and liabilities and monitoring cash flow on a regular basis. Management monitors the Credit Union's liquidity position and reports to the Board on a regular basis.

The Credit Union is required to maintain 6% of prior quarter's assets in liquid investments in which 100% must be held by Atlantic Central Credit Union Limited and the Credit Union was in compliance with this requirement at year end. Cash flows payable under financial liabilities by remaining contractual maturities are disclosed in Schedule 2. The Credit Union expects that many members will not request repayment on the earliest date the Credit Union could be required to pay.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Credit Union is exposed to currency risk through its cash accounts and member deposits. The Credit Union maintains deposits in foreign currencies to service its member accounts.

Interest rate risk

Interest rate risk is the sensitivity of the Credit Union's financial position to movements in interest rates. The Credit Union is exposed to interest rate risk when it enters into banking transactions with its members, namely deposit taking and lending. When asset and liability principal and interest cash flows have different payment or maturity dates, this results in mismatched positions. An interest-sensitive asset or liability is repriced when interest rates change, when there is cash flow from final maturity, normal amortization, or when members exercise prepayment, conversion or redemption options offered for the specific product. The Credit Union's exposure to interest rate risk depends on the size and direction of interest rate changes, and on the size and maturity of the mismatched positions. It is also affected by new business volumes, renewals of loans or deposits, and how actively members exercise options, such as prepaying a loan before its maturity date. The Credit Union's interest rate risk is subject to extensive risk management controls and is managed within the framework of policies and limits approved by the Board. Overall responsibility for asset/liability management rests with the Board. As such, the Board receives regular reports on risk exposures and performance against approved limits.

20. FAIR VALUE OF FINANCIAL INSTRUMENTS

Provincial Credit Union Ltd. has evaluated the fair value of its financial instruments based on the current interest rate environment, market values, and the actual prices of financial instruments with similar terms. Fair value represents the amount at which a financial instrument could be exchanged in an arm's length transaction between willing parties under no compulsion to act and is best evidenced by a quoted market price, if one exists. Quoted market prices are not available for a significant portion of the Credit Union's financial instruments.

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PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

20. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

A three-tier hierarchy is used as a framework for disclosing fair values based on inputs used to value the Credit Union's financial instruments recorded at fair value. Valuation methods used in this framework are categorized under the following fair value hierarchy:

Level 1 - Quoted prices for active markets for identical financial instruments that the entity can assess at the measurement date.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar financial instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets.

Level 3 - Valuations derived from valuation techniques in which one or more significant inputs are not based on observable market data.

The carrying value of cash and cash equivalents approximates their fair value as they are short-term in nature or are receivable on demand.

Long-term investments in shares in the Credit Union System and others have been classified as available for sale and are required to be measured at fair value with any changes in fair value recorded in other comprehensive income. The Credit Union has determined the fair value of these investments cannot be measured reliably and therefore measures these investments at cost with no adjustment to other comprehensive income. The Credit Union's investments in system debentures have been classified as held-to-maturity and are required to be measured at amortized cost.

The differences between the book and fair values of the Credit Union's loans and deposits are primarily due to changes in interest rates. The carrying value of the Credit Union's financial instruments are not adjusted to reflect increases or decreases in fair value as a result of interest rate changes, as it is the Credit Union's intention to realize their value over time by holding them to maturity.

21. CAPITAL MANAGEMENT

Provincial Credit Union Ltd. provides lending services to its members in the form of loans, lines of credit, and mortgages. The Credit Union's objective in the lending process is to remain within the lending guidelines set for the institution and to provide an adequate return to its members through adjusting risk premiums with the level of assessed risk on an individual basis. These services are provided to members at the discretion of the General Manager and lending personnel within the established parameters. Total lending activities managed by the Credit Union at December 31, 2016 amounted to \$251,497,490.

Consistent with other Prince Edward Island Credit Unions, Provincial Credit Union Ltd. is required by the Credit Union Deposit Insurance Corporation to maintain an equity level of 5% of the Credit Union's total assets. This ratio is calculated by adding the undistributed earnings at the end of the previous year plus the operating surplus in the current year and members' shares, divided by the total assets of the Credit Union.

	<u>2016</u>	<u>2015</u>
Undistributed earnings	\$ 30,799,163	\$ 29,692,112
Members' shares	77,510	81,025
Total regulatory equity	30,876,673	29,773,137

(continues)

PROVINCIAL CREDIT UNION LTD.

Notes to Financial Statements

Year Ended December 31, 2016

21. CAPITAL MANAGEMENT (continued)

Total assets	<u>322,429,950</u>	<u>312,091,923</u>
	<u>9.58 %</u>	<u>9.54 %</u>

Credit Union bylaws require Provincial Credit Union Ltd. to maintain sufficient liquid assets and a line of credit to meet its normal cash flow requirements. Overall, a minimum liquid asset level of 10% of total assets must be maintained to ensure ongoing cash flow requirements are met.

	<u>2016</u>	<u>2015</u>
Total assets	<u>\$322,429,950</u>	<u>\$312,091,923</u>
Liquid assets	<u>65,876,851</u>	<u>77,878,489</u>
	<u>20.43 %</u>	<u>24.95 %</u>

PROVINCIAL CREDIT UNION LTD.
Schedules to Financial Statements
Statement of Property and Equipment
Year Ended December 31, 2016

(Schedule 1)

	Cost beginning of year	Additions	Disposals	Cost end of year	Amort beginning in year	Amort in year	Amort end of year	NBV Dec 31, 2016	NBV Dec 31, 2015
Buildings	\$3,976,113	\$ -	\$ -	\$3,976,113	\$1,962,753	\$123,571	\$2,086,324	\$1,889,789	\$2,013,360
Equipment	1,766,894	10,564	-	1,777,458	1,547,470	44,942	1,592,412	185,046	219,423
ATMs	624,859	42,185	-	667,044	586,031	20,386	606,417	60,627	38,828
Computer hardware	791,535	-	-	791,535	772,315	9,330	781,645	9,890	19,220
Pavement	72,394	-	-	72,394	32,463	3,194	35,657	36,737	39,931
Computer software	21,527	13,736	-	35,263	21,527	6,868	28,395	6,868	-
	\$7,938,753	\$ 66,485	\$ -	\$8,005,238	\$4,922,559	\$ 208,291	\$5,130,850	\$2,874,388	\$3,016,193

Notes 1-21 are an integral part of these financial statements

PROVINCIAL CREDIT UNION LTD.
Schedules to Financial Statements
Interest Rate Sensitivity
Year Ended December 31, 2016

(Schedule 2)

	Under 1 year	Over 1 to 5 years	Over 5 years	Not interest rate sensitive	Total
ASSETS					
Cash and cash equivalents	\$ 9,098,092	\$ -	\$ -	\$ 3,854,453	\$ 12,952,545
Effective interest rate	0.44 %	- %	- %	- %	
Investments	35,426,282	6,000,000	-	4,535,393	45,961,675
Effective interest rate	1.16 %	1.85 %	- %	- %	
Accounts receivable	-	-	-	6,962,631	6,962,631
Personal and commercial loans and mortgages	71,303,637	166,268,556	6,287,468	888,799	244,748,460
Effective interest rate	3.77 %	3.73 %	4.25 %	- %	
Lines of credit and overdrafts	6,371,499	-	-	-	6,371,499
Effective interest rate	6.42 %	- %	- %	- %	
Prepaid expense	-	-	-	189,798	189,798
Deferred tax asset	-	-	-	332,399	332,399
Property and equipment	-	-	-	2,874,388	2,874,388
Due from CU PEI Investment Co	-	-	-	1,999,487	1,999,487
Real estate held for resale	-	-	-	37,068	37,068
	\$122,199,510	\$172,268,556	\$ 6,287,468	\$ 21,674,416	\$322,429,950

LIABILITIES AND MEMBERS' EQUITY

Accounts payable and accrued liabilities	\$ -	\$ -	\$ -	\$ 339,107	\$ 339,107
Employee benefits payable	-	-	-	1,222,764	1,222,764
Accrued interest payable	-	-	-	1,279,202	1,279,202
Income taxes payable	-	-	-	64,027	64,027
Member deposits	99,883,034	76,667,440	-	72,548,049	249,098,523
Effective interest rate	0.93 %	1.81 %	- %	- %	
Share deposits	39,549,654	-	-	-	39,549,654
Effective interest rate	0.50 %	- %	- %	- %	
Members' shares	77,510	-	-	-	77,510
Effective interest rate	0.50 %	- %	- %	- %	
Undistributed earnings	-	-	-	30,799,163	30,799,163
	\$139,510,198	\$ 76,667,440	\$ -	\$106,252,312	\$322,429,950

The above table sets out assets and liabilities on the earlier of contractual maturity or repricing date. Use of the table to derive information about the Credit Union's interest rate risk position is limited by the fact that certain borrowers may choose to terminate their financial instruments at a date earlier than contractual maturity or repricing dates. For example, personal and commercial loans and mortgages are shown at contractual maturity but could prepay earlier.

As at December 31, 2016, Provincial Credit Union Ltd.'s net interest spread was 2.29%. The net interest spread is calculated by expressing the difference between (a) the percentage of income earned on the average year end interest bearing assets and (b) the percentage of costs of capital and borrowings on the average year end interest bearing liabilities.



**We don't answer to distant
shareholders,
we answer to you.**



We're more than a bank. We make a local impact—your money stays here and works here.

You are more than a customer, you're a member.

We provide expert financial advice and services, but we also invest in our members and their communities.

We don't answer to distant shareholders, we answer to you.

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