

**SALMON ARM SAVINGS AND
CREDIT UNION**
Consolidated Financial Statements
For the year ended December 31, 2008

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BDO Dunwoody LLP
Chartered Accountants
and Advisors

Auditors' Report

To the Members of Salmon Arm Savings and Credit Union

We have audited the consolidated balance sheet of Salmon Arm Savings and Credit Union as at December 31, 2008 and the consolidated statements of operations and retained earnings and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Credit Union's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Salmon Arm Savings and Credit Union as at December 31, 2008 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the Financial Institutions Act, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

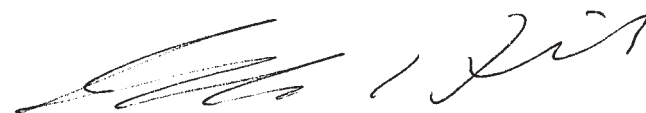
Chartered Accountants

Salmon Arm, British Columbia
February 6, 2009

**Salmon Arm Savings and Credit Union
Consolidated Balance Sheet**

December 31	2008	2007
Assets		
Cash resources (Note 3)	\$ 44,677,892	\$ 34,596,360
Members' loans (Note 4)	404,130,078	378,060,595
Other assets (Note 5)	1,185,150	773,733
Income tax receivable	-	121,202
Future income tax (Note 11)	87,807	94,840
Investments (Note 6)	1,236,230	2,134,866
Property, buildings and equipment (Note 7)	7,668,147	5,461,323
	\$458,985,304	\$421,242,919
Liabilities and Members' Equity		
Members' deposits (Note 8)	\$432,080,510	\$395,191,107
Accounts payable	1,877,434	1,557,923
Income tax payable	9,954	-
Dividends payable	3,377,762	3,674,394
Equity shares (Note 10)	996,038	1,046,592
	438,341,698	401,470,016
Members' equity		
Retained earnings	20,643,606	19,772,903
	\$458,985,304	\$421,242,919

Approved on behalf of the Board:



Chair of the Board



Chair of the Audit Committee

**Salmon Arm Savings and Credit Union
Consolidated Statement of Operations and Retained Earnings**

For the year ended December 31	2008	2007
Interest earned		
Interest on members' loans	\$ 22,354,389	\$ 21,265,806
Interest on investments	1,393,798	1,160,409
	23,748,187	22,426,215
Interest expense		
Members' deposits	11,012,393	9,407,866
Other	57,397	332,507
	11,069,790	9,740,373
Financial margin	12,678,397	12,685,842
Other income	4,248,848	3,976,402
	16,927,245	16,662,244
Operating expenses		
Salaries and employee benefits	6,727,593	6,155,629
Office, premises and supplies	2,814,155	2,593,665
Other administrative expenses	1,827,464	1,760,629
Community support	181,158	236,363
Amortization	617,630	564,981
Provision for losses on loans	217,479	178,268
	12,385,479	11,489,535
Income from operations	4,541,766	5,172,709
Dividends to members		
Shares	19,409	20,230
Patronage	3,366,661	3,657,624
	3,386,070	3,677,854
Income before income taxes	1,155,696	1,494,855
Income taxes (Note 11)		
Current	277,960	284,212
Future	7,033	19,824
	284,993	304,036
Net income for the year	870,703	1,190,819
Retained earnings, beginning of year	19,772,903	18,582,084
Retained earnings, end of year	\$ 20,643,606	\$ 19,772,903

**Salmon Arm Savings and Credit Union
Consolidated Statement of Cash Flows**

For the year ended December 31	2008	2007
Cash flows from operating activities		
Interest received	\$ 23,748,187	\$ 22,426,215
Other income	4,194,926	3,893,106
Interest paid	(11,069,790)	(9,740,373)
Dividends received	53,922	83,296
Cash paid to employees and suppliers	(11,248,890)	(10,769,547)
Income taxes paid	(146,804)	(769,482)
	<u>5,531,551</u>	<u>5,123,215</u>
Cash flows from investing activities		
Net increase in member loans and accrued interest	(26,268,930)	(58,651,009)
Net proceeds (purchases) of investments	898,636	(89,085)
Net purchases of property, buildings and equipment	(2,824,455)	(521,549)
Net decrease (increase) in other assets	(411,417)	14,947
	<u>(28,606,166)</u>	<u>(59,246,696)</u>
Cash flows from financing activities		
Net increase in deposits from members and accrued interest	36,889,403	61,449,748
Decrease in equity shares	(50,554)	(91,927)
Dividends paid	(3,682,702)	(3,100,104)
	<u>33,156,147</u>	<u>58,257,717</u>
Net increase in cash resources	10,081,532	4,134,236
Cash resources , beginning of year	<u>34,596,360</u>	<u>30,462,124</u>
Cash resources , end of year	<u>\$ 44,677,892</u>	<u>\$ 34,596,360</u>

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

1. Nature of Operations

The Credit Union is incorporated under the Credit Union Incorporation Act of the Province of British Columbia ("the Province") and operates branches in the communities of Salmon Arm, Sicamous and Sorrento. The operation of the Credit Union is subject to the Financial Institutions Act of British Columbia.

Member Plus Financial Planning and Investment Services Ltd. is incorporated under the Company Act of British Columbia and provides financial planning services.

SASCU Insurance Services Ltd. is incorporated under the Company Act of British Columbia and provides insurance services.

2. Significant Accounting Policies

a) Principles of Consolidation

The consolidated financial statements include the accounts of the Credit Union and those of its wholly-owned subsidiaries Member Plus Financial Planning and Investment Services Ltd. and SASCU Insurance Services Ltd. All significant intercompany transactions and accounts have been eliminated.

b) Members' Loans

The Credit Union records loans to members at the lower of principal plus accrued interest and net realizable value. The Credit Union recognizes interest income from loans on the effective interest basis for all loans not classified as impaired.

A loan is classified as impaired when there is reasonable doubt as to the timely collection of some portion of principal or interest. Loan interest income is not recognized on loans that are contractually past due for 90 days or more, unless there is no reasonable doubt as to the collectibility of all interest and principal. Any subsequent payments received on an impaired loan are applied to reduce the recorded investment in the loan. Loans or portions of loans considered uncollectible are written off.

c) Allowance for Loan Impairment

The Credit Union maintains an allowance for loan impairment for an amount considered adequate to absorb credit related losses in its loan portfolio. The allowance is increased by a provision for loan impairment which is charged to income and reduced by writeoffs, net of recoveries. The allowance for loan impairment consists of:

- A specific allowance on an individual loan basis, to reduce the carrying book values to estimated realizable values as determined by reference to market prices for the loans or their underlying security; and

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

2. Significant Accounting Policies - continued

- A general allowance when evidence of impairment within groups of loans exists but is not sufficient to allow identification of individual impaired loans. Impairment is estimated using historical credit loss experience, known risks in the portfolio and current economic conditions and trends. As individual impaired loans are identified, a specific provision is assigned to that loan and the collective provision is adjusted accordingly.

d) Investments

Investments are carried at the lower of cost and net realizable value as there is no quoted active market.

e) Property, Buildings and Equipment

Property, buildings and equipment are recorded at cost and are amortized over their estimated useful life using the following methods and annual rates:

Buildings	2.5% to 5% straight line
Furniture and equipment	5% to 30% declining balance or straight line
Leasehold improvements	5% to 50% straight line
Pavement	5% to 8.33% straight line

No amortization is taken in the year of acquisition.

f) Future Income Tax

The Credit Union follows the asset and liability method for accounting for income taxes. Under this method, future income tax assets and liabilities are recognized for the expected future income tax consequences attributed to the difference between the financial statement carrying amount of existing assets and liabilities and their respective income tax bases. Future tax assets and liabilities are measured using tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

g) Revenue Recognition

Interest income is recognized using the effective interest method, unless the loan is classified as impaired. Recognition of interest income ceases when the carrying amount of the loan (including accrued interest) exceeds the estimated realizable amount of the underlying security.

The effective interest method is a method of calculating the amortized cost of the related loan based on its estimated fair value and allocating the interest income over the relevant period.

Loan negotiation fees and income recorded on prepayment or renegotiation of fixed term loans are recognized in the period in which they occur.

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

2. Significant Accounting Policies - continued

Mutual fund income is recognized as the services are rendered to the member, the price is fixed or determinable and collectability is reasonably assured when payment is received.

h) Financial Instruments

The Credit Union recognizes and measures financial assets and financial liabilities on the consolidated balance sheet when it becomes a party to the contractual provisions of a financial instrument. All financial instruments are measured at fair value on initial recognition. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for trading, loans and receivables, held to maturity, available for sale or other financial liabilities. Management determines the classification of financial assets and liabilities at initial recognition.

All transactions related to financial instruments are recorded on a settlement date basis.

Held-for-Trading

Financial instruments are classified under this category if they are:

- (i) acquired principally for the purpose of selling or repurchasing in the near term;
- (ii) part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short term profit-taking;
- (iii) a derivative, except for a derivative that is a financial guarantee contract or a designed effective hedging instrument; or
- (iv) designed at fair value using the fair value option ("FVO")

Financial instruments cannot be transferred into or out of the Held for Trading category after inception. For designation at fair value using the FVO option, reliable fair values must be readily available.

This category is comprised of cash. It is carried on the balance sheet at fair value with changes in fair value recognized in the statement of operations. Transaction costs related to instruments classified as held-for-trading are expensed as incurred.

Loans and Receivables

This category is comprised of accounts receivable and members' loans. These assets are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. They are initially recognized at fair value and subsequently carried at amortized cost, using the effective interest rate method, less any provision for impairment. Transaction costs related to loans and receivables are expensed as incurred.

Held-to-Maturity

This category is comprised of liquidity term deposits. These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the company's management has the positive intention and ability to hold to maturity and comprises certain investments in debt securities. These assets are initially recognized at fair value and subsequently carried at amortized cost, using the effective interest rate method, less any provision for impairment. Transaction costs related to held-to-maturity investments are expensed as incurred.

Continued ...

Salmon Arm Savings and Credit Union Notes to Consolidated Financial Statements

December 31, 2008

2. Significant Accounting Policies - continued

Available-For-Sale

Non-derivative financial assets not included in the above categories are classified as available-for-sale and comprises certain investments, including the Credit Union's investments in private companies. When they have a quoted market price in an active market, they are carried at fair value with changes in fair value recognized as a separate component of other comprehensive income. When they do not have a quoted market price in an active market, they are carried at cost. Where a decline in the fair value is determined to be other than temporary, the amount of the loss is removed from other comprehensive income and recognized in the income statement. Transaction costs related to available-for-sale investments are expensed as incurred.

Other Financial Liabilities

Other financial liabilities includes all financial liabilities other than those classified as held-for-trading and comprises accounts payable and accrued liabilities, members' deposits, equity shares and dividends payable. These liabilities are initially recognized at fair value and subsequently carried at amortized cost using the effective interest rate method. Transaction costs related to other financial liabilities are expensed as incurred.

Measuring Fair Value

The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arm's-length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values are determined by reference to quoted bid or asking prices as appropriate, in the most advantageous active market for that instrument to which the Credit Union has immediate access.

Fair values determined using valuation models require the use of assumptions concerning the amount and timing of estimated future cash flows and discounted rates. In determining those assumptions, external readily observable market inputs including interest rate yield curves, currency rates and price and rate volatilities are considered, as applicable.

Impairment of Financial Assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it has been impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar risk characteristics. All impairment losses are recognized in the income statement.

Change in Accounting Policy

On January 1, 2008, the Credit Union adopted CICA Handbook Section 3862, "Financial Instruments - Disclosure", Section 3863, "Financial Instruments - Presentation" and Section 1535, "Capital Disclosures".

Continued ...

Salmon Arm Savings and Credit Union Notes to Consolidated Financial Statements

December 31, 2008

2. Significant Accounting Policies - continued

Section 3862 increases the disclosures currently required to include the extent to which an entity is exposed to risks arising from financial instruments, the nature of those risks and a description of management's objectives, policies and processes for dealing with them. Section 3863 replaces the existing requirements on the presentation of financial instruments, which have been carried forward unchanged. Section 1535 requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance.

The adoption of these new standards required additional note disclosure as contained primarily in Notes 4, 12 and 15. There was no material impact on the Credit Union's Consolidated Statement of Operations.

i) Derivative Financial Instruments

The Credit Union enters into equity linked option contracts to manage its exposure to fluctuations in interest rates for specific financial instruments. Premiums paid to enter into these contracts are recorded in other assets and are amortized over the contract life. Expenses associated with equity linked (TSX linked products) option contracts are accounted for on an accrual basis and recognized over the life of the contract as an adjustment to financial expenses.

j) Use of Estimates

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The precise determination of many assets and liabilities is dependent on future events. As a result, the preparation of consolidated financial statements for a period involves the use of estimates and approximations which have been made using careful judgement. Actual results could differ from those estimates and approximations.

k) Foreign Currency Translation

Foreign currency accounts are translated into Canadian dollars as follows:

At the year end date, monetary assets, liabilities, revenues and expenses are translated into Canadian dollars by using the exchange rate in effect at that date. The resulting foreign exchange gains and losses are included in income in the current period.

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

2. Significant Accounting Policies - continued

I) New Accounting Pronouncements

Recent accounting pronouncements that have been issued but are not yet effective, and have a potential implication for the Credit Union, are as follows:

Financial Statement Concepts

CICA Handbook Section 1000, Financial Statement Concepts, has been amended to focus on the capitalization of costs that truly meet the definition of an asset and de-emphasize the matching principle. The reviewed requirements are effective for annual financial statements relating to fiscal years beginning on or after October 1, 2008. The Credit Union is currently evaluating the impact of the adoption of this change on the disclosure within its financial statements.

Goodwill and Intangible Assets

Section 3064 incorporates guidance to clarify the recognition of intangible assets and address recognition and measurement of internally developed intangible assets. The new standards are effective for annual financial statements relating to fiscal years beginning on or after October 1, 2008. The Credit Union is currently evaluating the impact of the new standard.

International Financial Reporting Standards

In February 2008, the Canadian Standards Board announced that Canadian generally accepted accounting principles for publicly accountable enterprises will be replaced by International Financial Reporting Standards (IFRS) for fiscal years beginning on or after January 1, 2011. As a credit union we are specifically scoped into the definition of a publicly accountable enterprise. As such, we will be required to prepare our December 31, 2011 financial statements including comparative information in compliance with IFRS. We are currently assessing the potential impact of the transition to IFRS on our financial statements, disclosures, and broader financial reporting systems and controls.

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

3. Cash Resources

	2008	2007
Cash	\$ 7,351,626	\$ 6,666,872
Central 1 Credit Union	36,819,305	29,008,081
Accrued interest on deposits	506,961	421,407
	44,677,892	36,096,360
Central 1 Credit Union demand loan (Note 9)	-	1,500,000
	\$ 44,677,892	\$ 34,596,360

Cash with Central 1 Credit Union in term deposits as at December 31, 2008 totals \$36,819,305 (2007 - \$29,008,081) and bears interest at 0.21% to 4.84% with maturities from January 2, 2009 to April 8, 2013.

Under governing legislation, the Credit Union must maintain, for liquidity purposes, deposits with Central 1 Credit Union of at least 8% of deposits and borrowings. At December 31, 2008, the Credit Union liquidity deposits exceeded the minimum requirement.

4. Members' Loans

	Residential Mortgages	Personal Loans	Commercial Loans	Total 2008	Total 2007
Loans	\$226,188,869	\$ 82,746,354	\$ 95,613,745	\$404,548,968	\$378,195,987
Accrued interest	842,169	27,695	8,264	878,128	962,179
	227,031,038	82,774,049	95,622,009	405,427,096	379,158,166
Allowance for impaired loans	811,467	181,918	303,633	1,297,018	1,097,571
	\$226,219,571	\$ 82,592,131	\$ 95,318,376	\$404,130,078	\$378,060,595

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

4. Members' Loans - continued

	Residential Mortgages	Personal Loans	Commercial Loans	Total 2008	Total 2007
Impaired loans	\$ -	\$ 387,115	\$ 28,250	\$ 415,365	\$ 6,554
Less: unsatisfactory loans where loss is not expected	-	335,508	16,092	351,600	2,663
Specific provision	-	51,607	12,158	63,765	3,891
General provision	811,467	130,311	291,475	1,233,253	1,093,680
	<u>\$ 811,467</u>	<u>\$ 181,918</u>	<u>\$ 303,633</u>	<u>\$ 1,297,018</u>	<u>\$ 1,097,571</u>

The activity in the allowance for impaired loans has been as follows:

	Personal Loans	Commercial Loans	Total 2008	Total 2007
Balance, opening	\$ 855,325	\$ 242,246	\$ 1,097,571	\$ 937,552
Recoveries on loans previously written off	6,112	-	6,112	767
Current year provision	172,334	45,145	217,479	176,979
	<u>1,033,771</u>	<u>287,391</u>	<u>1,321,162</u>	<u>1,115,298</u>
Loans written off	(24,144)	-	(24,144)	(17,727)
Balance, ending	<u>\$ 1,009,627</u>	<u>\$ 287,391</u>	<u>\$ 1,297,018</u>	<u>\$ 1,097,571</u>

Member loans can either have a variable rate or fixed rate of interest with terms of up to 10 years.

Variable rate loans are based on an increment or decrement to the prime rate, ranging from prime minus 0.25% to prime plus 9.00%. The applicable rate is determined by the member's credit worthiness, security, and whether the member is defined as a full service member (FSM). A FSM is defined as a member who has all significant dealings with the Salmon Arm Savings and Credit Union. The Credit Union's prime rate at December 31, 2008 is 3.50% (2007 - 6.00%).

The interest rate offered on fixed rate loans being advanced as at December 31, 2008 range from 4.79% to 13.50% (2007 - 6.54% to 16.00%). The rate offered to a member varies with the term of the loan, type of security offered, the member's credit worthiness and whether the member is defined as a full service member (described above).

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

4. Members' Loans - continued

Personal loans consist of term loans, lines of credit and residential mortgages and, as such, have various repayment terms.

Commercial loans consist of mortgages, term loans and lines of credit and, as such, have various repayment terms.

Residential and commercial mortgages are secured by real property and generally are repayable on monthly blended payments of principal and interest.

At December 31, 2008, the Credit Union has committed to certain loans which, if they had been fully advanced, would amount to \$1,678,181 (2007 - \$4,676,148).

The Credit Union has guaranteed letters of credit for several companies in the amount of \$2,610,207 (2007 - \$2,512,526).

5. Other Assets

	2008	2007
ICBC Insurance License	\$ 608,532	\$ -
Other Assets	576,618	773,733
	<u>\$ 1,185,150</u>	<u>\$ 773,733</u>

6. Investments

	2008	2007
Shares and Trust Units		
Central 1 Credit Union	\$ 1,125,594	\$ 1,042,286
CUPP Services Ltd.	110,250	92,194
Stabilization Central Credit Union	386	386
GrowthStart: A Local Business Development Fund	-	1,000,000
	<u>\$ 1,236,230</u>	<u>\$ 2,134,866</u>

Shares in Central 1 Credit Union (Central 1) are required investments as a condition of membership in Central 1 and also required by provincial legislation. These investments, which are determined by formula based on Credit Union membership and assets, are realizable only on withdrawal from membership. As there is no market for these instruments, their fair value is assumed to approximate their carrying value.

The GrowthStart units were redeemed on October 31, 2008 at their carrying value, plus interest.

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

7. Property, Buildings and Equipment

	2008		2007	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Land	\$ 656,380	\$ -	\$ 656,380	\$ -
Buildings	7,104,511	1,788,393	5,230,977	1,655,651
Furniture and equipment	3,867,150	2,392,765	3,341,759	2,412,971
Leasehold improvements	684,435	620,563	684,435	562,254
Pavement	243,960	86,568	243,960	65,312
	\$ 12,556,436	\$ 4,888,289	\$ 10,157,511	\$ 4,696,188
Net book value		\$ 7,668,147		\$ 5,461,323

8. Members' Deposits

	2008	2007
Demand	\$226,520,779	\$207,858,366
Term	156,048,706	143,196,746
Registered savings plans	45,820,458	40,763,797
Non-equity shares	89,829	50,039
Accrued interest - demand and term	2,419,893	2,253,601
- registered savings plans	1,180,845	1,068,558
	\$432,080,510	\$395,191,107

All deposits and non-equity shares of the Credit Union are guaranteed by the Credit Union Deposit Insurance Corporation, a government corporation, as set out in the Financial Institutions Act.

Demand deposits are variable rate and may be withdrawn at any time. The interest rates offered on demand deposits at December 31, 2008 range from 0% to 2.25% (2007 - 0% to 3.75%). Interest on demand deposits is either calculated daily and paid monthly or compounded daily and paid monthly.

Term deposits bear fixed rates of interest for terms up to five years. Interest is calculated daily and can be paid annually, semi-annually, monthly or upon maturity. The interest rates offered on term deposits issued on December 31, 2008 range from 0.25% to 2.95% (2007 - 2.025% to 4.25%).

Registered Savings Plans consist of Registered Retirement Savings Plans (RRSP's), Registered Retirement Income Funds (RRIF's), and Registered Education Savings Plans (RESP's). Registered accounts may be fixed or variable rate. The fixed rate registered plans have terms and rates similar to the term deposit accounts described above. The interest rates offered on variable rate registered plans bear interest at 0.25% to 2.25% at December 31, 2008 (2007 - 0.25% to 3.75%). Interest on the variable rate registered plans are calculated daily and paid monthly or semi-annually.

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

8. Members' Deposits - continued

Included in the Registered Retirement Savings Plan deposits are \$183,098 (2007 - \$183,098) of Index Linked Deposits. The Credit Union pays a fixed rate premium to Central 1 Credit Union on each of the deposits. At the end of the term, Central 1 Credit Union pays interest to the depositor based on the performance of the Index.

Members' contributions to registered savings plans are deposited with the Credit Union and held at Central 1 Credit Union under a trust agreement.

9. Term Loans and Accrued Interest

The Credit Union has available to it, through Central 1 Credit Union, a basic credit facility of \$20,000,000 secured by a demand debenture and the general assignment of book debts. The balance outstanding as at December 31, 2008 was \$ Nil (2007 - \$1,500,000).

10. Equity Shares

All members are required to hold a prescribed number of equity shares. The Credit Union has one class of equity shares, having a par value of \$1.00. Funds invested in these shares are not guaranteed by the Credit Union Deposit Insurance Corporation of British Columbia. Redemption of equity shares may be subject to certain restrictions.

Authorized and Issued

	2008	2007
Class A membership equity shares	\$ 996,038	\$ 1,046,592

11. Income Taxes

	2008	2007
The major components of future income tax payable are:		
Temporary differences relating to property, buildings and equipment (primarily due to differences between tax treatment and accounting treatment of property, buildings and equipment)	\$ (85,741)	\$ (80,211)
Temporary differences relating to allowance for impaired loans	173,548	175,051
Future income taxes receivable	\$ 87,807	\$ 94,840

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

11. Income Taxes - continued

The effective rate of income tax varies from the statutory rates as follows:

	<u>2008</u>	<u>2007</u>
Combined tax rates	31 %	34 %
Income tax expense at the applicable rate	\$ 422,734	\$ 523,311
Preferred rate deduction for credit unions	(228,102)	(235,662)
Items not deductible for tax purposes	692,919	591,585
Items not taxable for tax purposes	(609,591)	(595,022)
Future income tax	7,033	19,824
Income tax expense	<u>\$ 284,993</u>	<u>\$ 304,036</u>

12. Capital Management

As a provincially incorporated Credit Union, Salmon Arm Savings and Credit Union is required to measure its capital adequacy based on the Financial Institutions Commission of British Columbia (FICOM) regulations. Regulatory capital must have the following fundamental characteristics: i) permanency; ii) free of fixed charges against earnings; and iii) subordinate in its priority on liquidation to the rights of deposits and other creditors of the credit union. Primary or secondary capital allocations are based on whether items meet all or only some of the fundamental characteristics. Also, other items may need to be deducted from capital to arrive at the Total Capital Base (TCB).

Based primarily on the credit risk of each type of asset, the book value of each asset is multiplied by a risk weight factor ranging from 0.00% to 150.00%. The regulatory ratio is then computed by dividing the TCB by the Credit Union's risk weighted assets, including off balance sheet commitments. Regulation currently requires that Credit Unions maintain a minimum capital to risk-weighted assets ratio of 8.00%. As at December 31, 2008 the Credit Union met the capital requirements of the Act.

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

12. Capital Management - continued

The capital ratio over the past 5 years is as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Capital Adequacy Ratio	12.13 %	12.26 %	13.25 %	14.66 %	13.56 %

Capital in the Credit Union is comprised of :

	<u>2008</u>	<u>2007</u>
Capital		
Primary Capital		
Retained Earnings	\$ 20,643,606	\$ 19,772,903
Membership Equity Shares including Dividends	1,015,395	1,086,924
	<u>21,659,001</u>	20,859,827
Secondary Capital		
Share of System Retained Earnings	2,431,881	2,272,995
	<u>24,090,882</u>	23,132,822
Deductions from Capital		
Future Income Taxes	87,807	94,840
Total Capital Base	<u>\$ 24,003,075</u>	<u>\$ 23,037,982</u>

Salmon Arm Savings and Credit Union manages its capital and its composition based on its statutory requirements. The ratio is reviewed monthly and is addressed in short and long-term planning to review the impact of strategic decisions, growth rates and other trends. The Board of Directors maintains overall responsibility for an effective capital management process, including policy review, and regulatory adherence. It has delegated certain of its specific responsibilities to the Investment and Lending Committee. There have been no changes in what the Credit Union considers to be capital since the previous period.

13. Commitments

- a) The Credit Union has entered into a contract with CDSL Canada Limited for data processing and transaction switching services for the period June 28, 2002 to December 31, 2013. Data processing costs vary with the level of usage and the number of members. Costs in 2008 were \$401,178 (2007 - \$395,121).
- b) The Credit Union has entered into an agreement with Impress Digital for electronic output distribution services for the period January 1, 2004 to May 31, 2009. Subsequent to implementation, costs are based on the volume of transactions and follow a preset pricing matrix. Costs in 2008 were \$102,015 (2007 - \$103,025).

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

13. Commitments - continued

- c) Leases
- i) Effective June 1, 2005 the Credit Union has entered into a five year lease for its Sorrento premises, at an annual cost of \$28,908 plus operating costs.
 - ii) Effective December 1, 2007 the Credit Union has entered into a five year lease for its Sicamous premises, at an annual cost of \$66,525 plus operating costs.

The minimum annual lease payments excluding operating costs to the expiry of the leases are as follows:

2009	\$	95,433
2010		78,570
2011		66,525
2012		60,981
	<u>\$</u>	<u>301,509</u>

14. Related Party Transactions and Transactions with Others

The following information, for the year ended December 31, 2008, is disclosed for the benefit of the members:

- a) Outstanding loans to directors, officers, employees and members of any committee of the Credit Union amounted to \$15,252,973 (2007 - \$11,461,361). All such loans were granted in accordance with normal lending terms at regular member rates.
- b) Directors, in their capacity as directors, received remuneration totalling \$63,350 (2007 - \$73,700).
- c) Annual dues paid to Central 1 Credit Union totalled \$97,725 (2007 - \$92,748).

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

15. Risk Management Related to Financial Instruments

The Credit Union is exposed to various types of risks as a result of the nature of its business activities. This note describes the Credit Union's objectives, policies and processes for managing the risk arising from financial instruments and the methods used to measure them. Further quantitative information in respect of these risks is presented throughout these financial statements.

The following table presents the principal financial instruments used by the Credit Union, and their classification:

Class of Financial Instrument	<u>Categories of Financial Assets and Financial Liabilities</u>			
	Held to Maturity	Available for Sale	Loans & Receivables	Other Financial Liabilities
Deposits with financial institutions				
Liquidity deposits	\$ 31,818,965	\$ -	\$ -	\$ -
Other deposits	-	5,000,340	-	-
Members' loans	-	-	404,130,078	-
Investments				
Central 1 Credit Union	-	1,125,565	-	-
Other Investments	-	110,636	-	-
Members' deposits	-	-	-	432,080,510
Accounts payable and other liabilities	-	-	-	5,265,150

Risk Management

Senior management is responsible for identifying risks and developing appropriate and prudent risk management policies. The Board of Directors (the Board), through various committees, reviews and approves all risk management policies and provides oversight to the risk management framework and processes.

Within the various risks inherent in business activities, those related to financial instruments are: credit risk, market risk, liquidity and funding risk.

a) Credit Risk

Credit risk is the risk that a financial loss will be incurred if a counterparty fails to meet its contractual obligations to the Credit Union. This risk can relate to balance sheet assets such as loans, as well as off balance sheet assets such as commitments and letters of credit.

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

15. Risk Management Related to Financial Instruments - continued

i) Risk Measurement

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

ii) Objectives, Policies and Processes

The Credit Union's credit risk management principles are guided by its overall risk management principles. The Board ensures that management has a framework, policies, and processes in place to manage credit risks and that the overall credit risk policies are complied with at the business and transaction level. The Investment and Lending Committee (ILC), comprised of members of the Board and Senior Management, approves and regularly reviews lending policies, establishes lending limits for the Credit Union, delegates lending limits and reviews quarterly reports prepared by management on watch list loans, impaired loans, diversification of the portfolio and other policy compliance requirements. The Audit Committee reviews the adequacy of the allowance for impaired loans.

Credit risk policies and principles used to manage credit risk exposure include the following:

- Lending policy statements including approval of lending policies, eligibility for loans, exceptions to policy and policy administration;
- Delegated lending authorities, which are clearly communicated to personnel engaged in the credit granting process and a defined approval process for loans in excess of those limits;
- Loan collateral security classifications which set loans classifications, advance ratios and amortization periods;
- Procedures outlining loan overdrafts, release or substitution of collateral, temporary suspension of payments and loan renegotiations;
- Early recognition of problem accounts, loan delinquency controls and procedures for loans in arrears;
- Appointment of personnel engaged in credit granting who are qualified;
- Management of growth within quality objectives; and
- Audit procedures and processes are in existence for all levels of Credit Union lending activities.

Continued ...

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

15. Risk Management Related to Financial Instruments - continued

iii) Maximum Exposure to Credit Risk

The Credit Union's maximum exposure to credit risk at December 31, 2008 without taking account of any collateral or other credit enhancements is as follows:

	Carrying Value	Maximum exposure
Deposits with Financial Institutions	\$ 36,819,305	\$ 36,819,305
Member Loans	404,130,078	404,130,078
Unfunded loans and lines of credit	-	1,678,181
Letters of credit	-	2,610,207
	<u>\$440,949,383</u>	<u>\$445,237,771</u>

The principal collateral and other credit enhancement we hold as security for loans include i) insurance, mortgages over residential lots and properties, ii) recourse to business assets such as real estate, equipment, inventory and accounts receivable, iii) recourse to the commercial real estate properties being financed, and iv) recourse to liquid assets, guarantees and securities.

Our credit risk objectives, policies and processes have not changed materially from 2007.

b) Market Risk

Market risk is the risk of a loss that may arise from financial market factors such as interest rates, foreign exchange rates, and equity or commodity prices. The credit union is exposed to market risk when making loans, taking deposits and making investments, all part of its asset/liability management activities. The level of market risk to which the Credit Union is exposed varies depending on market conditions and expectation of future price and yield movements. The Credit Union's material market risks are confined to interest rates and to a limited extent, foreign exchange, as discussed below.

i) Interest Rate Risk

Interest rate risk arises mainly from the different re-pricing dates of cash flows associated with interest sensitive assets and liabilities. Certain products with embedded options such as loan prepayment and deposit redemption impact interest rate risk.

1) Risk Measurement

The Credit union measures its interest rate risk on a monthly basis. Measures include the sensitivity of net interest income and equity value to changes in rates, duration parameters, as well as simulation modeling.

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**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

15. Risk Management Related to Financial Instruments - continued

2) Objectives, Policies and Processes

The Asset Liability Committee (ALCO), made up of senior management, meets regularly to monitor the Credit Union's position as set by Board policy and ALCO operational guidelines, and decide future strategy. These policies and guidelines define the standards and limits within which risk to net interest income and the value of equity are to be contained. An asset/liability risk report is reviewed by ALCO monthly and on a quarterly basis by the ILC. Interest Rate Risk policies are reviewed annually by the Board.

The Credit Union's potential risk due to changes in interest rates at December 31, 2008 is provided below. All interest rate risk measures are based upon interest rate exposures at a specific time and continuously change as a result of business activities and our risk management initiatives.

100 basis point increase in interest rates Impact on net interest income (for the next 12 months)	\$ 709,000
100 basis point decrease in interest rates Impact on net interest income (for the next 12 months)	\$ (559,000)

The maturity of interest-sensitive items is disclosed in Note 16 to the financial statements.

ii) Foreign Exchange Risk

Foreign exchange risk arises when there is a difference between assets and liabilities denominated in a foreign currency. In providing services to its members, the Credit Union has assets and liabilities denominated in U.S. dollars.

1) Risk Measurement

The Credit Union's position is measured daily by determining the net foreign exchange position of the Credit Union.

2) Objectives, Policies and Processes

The Credit Union's foreign exchange exposure is managed by a limit on the maximum allowable difference between U.S. dollar assets and liabilities. Policy with respect to foreign exchange exposure is reviewed and approved at least annually by the Board of Directors.

At December 31, 2008, the Credit Union's exposure to foreign exchange risk was not material.

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**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

15. Risk Management Related to Financial Instruments - continued

c) Liquidity and Funding Risk

Liquidity risk is the risk that the Credit Union may not be able to gather sufficient cash resources in a timely and cost effective manner to meet its financial obligations as they become due.

i) Risk Measurement

The Credit Union measures and manages risk from different perspectives. We monitor cash resources daily in order to address our normal day-to-day funding requirements and ensuring regulatory compliance, as well as measure overall maturity of assets and liabilities, longer-term cash and funding needs and contingency planning. The assessment of the Credit Union's liquidity position reflects management's estimates, assumptions and judgments pertaining to current and prospective conditions of the Credit Union, the markets and the related behavior of members and counterparties.

ii) Objectives, Policies and Processes

The Credit Union's liquidity management framework is monitored by ALCO and policies are approved by the ILC and Board. This framework is in place to ensure that the Credit Union has sufficient cash resources to meet its current and future financial obligations under both normal and unusual conditions. Maintenance of a prudent liquidity base also provides flexibility to fund loan growth and react to other market opportunities.

Legislation requires that the Credit Union maintain liquid assets at Central 1 Credit Union at least equal to 8% of our deposit and other debt liabilities. Regulatory liquidity is reported to the Board monthly and the ILC receives regular reporting of available cash resources and utilization rates. The Credit Union strives to maintain a stable volume of base deposits originating from its members, as well as diversified funding sources such as asset sale or securitization and wholesale borrowings. The Credit Union was in compliance with the regulatory liquidity requirements throughout the year. At December 31, 2008, the Credit Union's liquidity ratio was 10.22%.

The maturities of the Credit Union financial liabilities are disclosed in Note 16 in the notes to the financial statements.

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

16. Interest Rate Sensitivity

Financial margin is the Credit Union's primary source of revenue, which is defined as the difference between interest earned on assets and interest paid on liabilities. The term "mismatch" is commonly used when the terms of the asset and liability instruments are different. The assessment of the interest rate exposure requires an analysis of the Credit Union's mismatched position. The following table sets out the scheduled maturities or re-pricing dates, whichever occurs earlier, of the financial assets and liabilities as at December 31, 2008, together with the weighted average interest rate earned on the respective financial assets and liabilities and the net mismatched position.

	Within 1 Year	%	1-5 Years	%	Over 5 Years	%	2008 Total	2007 Total
Assets (000's)								
Non-interest sensitive	\$ 18,394	-	\$ -	-	\$ -	-	\$ 18,394	\$ 12,170
Variable rate	174,902	7.06	-	-	-	-	174,902	132,253
Fixed rate	49,949	4.98	181,857	5.82	33,883	5.89	265,689	276,820
	243,245		181,857		33,883		458,985	421,243
Liabilities and Members' Equity (000's)								
Non-interest sensitive	79,747	-	-	-	-	-	79,747	75,655
Variable rate	181,176	2.35	-	-	-	-	181,176	163,545
Fixed rate sensitive liabilities	64,180	3.95	133,882	3.56	-	-	198,062	182,043
	325,103		133,882		-		458,985	421,243
Balance Sheet Mismatch	(81,858)		47,975		33,883		-	-
Interest Rate Swaps	-		-		-		-	-
Net Mismatch	\$ (81,858)		\$ 47,975		\$ 33,883		\$ -	\$ -

**Salmon Arm Savings and Credit Union
Notes to Consolidated Financial Statements**

December 31, 2008

17. Fair Value of Financial Instruments

The following represents the fair values of on and off balance sheet financial instruments of the Credit Union.

While the fair value amounts are intended to represent estimates of the amounts at which these instruments could be exchanged in a current transaction between willing parties, many of the Credit Union's financial instruments lack an available trading market. Consequently, the fair values presented are estimates derived using present value and other valuation techniques and may not be indicative of the net realizable values.

Due to the judgement used in applying a wide range of acceptable valuation techniques in calculating fair value amounts, fair values are not necessarily comparable among financial institutions. The calculation of estimated fair values is based on market conditions at a specific point in time and may not be reflective of future fair values.

Interest rate sensitivity is the main cause of changes in the fair value of the Credit Union's financial instruments. The book values are generally not adjusted to reflect the fair value, as it is the Credit Union's intention to realize their value over time by holding them to maturity.

Balance Sheet	2008		2007	
	Book value	Fair Value	Book Value	Fair Value
Assets (000's)				
Cash resources	\$ 44,678	\$ 46,489	\$ 34,596	\$ 35,008
Loans	404,130	409,188	378,061	379,737
Investments	1,236	1,236	2,135	2,135
Other assets	8,941	8,941	6,451	6,451
Liabilities and Members' Equity (000's)				
Members' and municipal deposits	\$ 432,081	\$ 434,848	\$ 395,191	\$ 385,895
Other liabilities	1,887	1,887	1,557	1,557
Dividend on equity shares	3,378	3,378	3,674	3,674
Equity shares	996	1,183	1,047	1,651

