Annual Report 1996

CUDIC™

Nova Scotia
Credit Union Deposit Insurance Corporation

Annual Report
1996

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Report of the Board of Directors

***Lloyd Coombs**,*
Chair

"The development of a system of monitoring the operations of our credit unions is progressing well and we expect it will be completed during the coming year."

We are pleased to report another year of success and progress for the Nova Scotia Credit Union Deposit Insurance Corporation (CUDIC).

The successes of the past year has been the removal of several credit unions from the Intervention System. This has come about as a result of the dedication of the Board and Management of each credit union in resolving the issues which placed them on the Intervention System. The staff of CUDIC and Credit Union Central of Nova Scotia (CUCNS) are to be congratulated as well for working closely with these credit unions to assist them in meeting their goals and objectives.

The progress referred to above is highlighted by the fact that equity in CUDIC has increased from approximately $3,300,000 at the end of 1995 to approximately $5,600,000 at the end of 1996. We are pleased that we have been able to increase equity to this degree, even though we have decreased assessments to our credit unions from 25 basis points to 20 basis points.

Claims will be in the area of $200,000 which is considerably less than the $500,000 that we had budgeted in 1996.

The Board of Directors held five regular meetings, one Telephone Conference Call and a special Board meeting during 1996, as well as a Planning Session. Also, all Committees met regularly during the year.

There were two changes to the make up of the Board during the year. Carol Ripley resigned after accepting a position with one of our credit unions and was replaced by Mary Boyd. We take this opportunity to thank Carol for her dedicated service to our Board. Her expertise and understanding of the credit union Movement was a great asset to us. Marina Russell was replaced by Janine Saulnier during the year. We thank Marina for the contribution she made to our Board during her term.

The Sound Business and Financial Practices Committee were active during the year and issued the Impaired Loans Standard, in response to the issuance of new guidelines for accounting for Impaired Loans from the Canadian Institute of Chartered Accountants.

The Executive Committee met several times with the Executive Committee of CUCNS to deal with issues of common concern, but mainly to develop an agreement on Roles and Responsibilities for both organizations. We are pleased to report that an agreement was signed by both Boards at a joint meeting held on December 4, 1996. Both Boards and staff are to be commended for the many hours of work and the spirit of co-operation shown during the negotiations of this important document.

The development of a system of monitoring the operations of our credit unions is progressing well and we expect it will be completed during the coming year. It has been, and will continue to be, time consuming, but the end product will be extremely beneficial to CUDIC in fulfilling our mandate. We extend thanks to our staff for the efficient manner in which they have carried out their responsibilities. Operating costs have consistently remained under budget, which has allowed us to reduce assessments and build equity at the same time.

Respectfully submitted on behalf of the Board of Directors.

Lloyd W. Coombs

Lloyd W. Coombs
Chair

Kay Chisholm,
Director

Mike MacNeil,
Vice–Chair

Gerard Thériault,
Director

Janine Saulnier,
Director

Mary Boyd,
Director

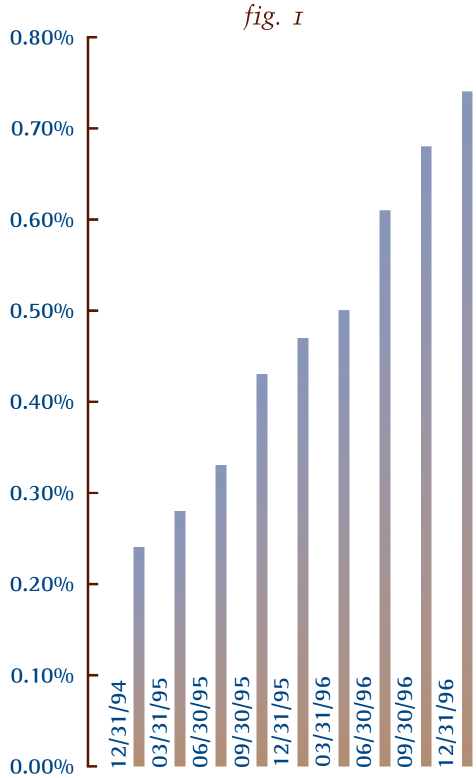
David Nunn,
Secretary

Report of the Chief Executive Officer

Barry Bennett*,*
Chief Executive Officer

"The results achieved by the credit unions for their efforts is very rewarding."

fig. 1



Equity/System Assets

I look back on 1996 with a sense of pride. Pride in the growth and progress made by the Nova Scotia Credit Union movement and knowing that in our own small way we have contributed to the overall well-being of credit union members.

Following all the changes which incurred in 1995 with the new Act, introduction of Standards of Sound Business Practices, new policies and deposit insurance, 1996 was a year of reorganization and application of the new tools. The results achieved by the credit unions for their efforts is very rewarding. Credit union Boards, management and staff are commended for the herculean efforts that were needed to assimilate and apply all the new procedures which came at them in a very short time frame. I would like to thank each of you for your cooperation and patience during this transition period.

With the Nova Scotia Credit Union Deposit Insurance Corporation's (CUDIC) Board returning to full complement, it will put us in a position to work with credit unions to deal with the challenges we will be facing in 1997 and beyond. At the time of writing this, interest rates appear to have stabilized at a low rate. Initially, this helped financial institutions as the cost of deposits dropped more quickly than the repricing of the loans. However, as rates remain low, loans are repricing at significantly lower rates and for longer periods and this is creating significant pressure on the financial margins in credit unions. The longer the period of low interest rates, the greater the demand for longer term loans and mortgages becomes, because people begin to believe that rates must go up and try and lock in borrowing rates for the longest period possible. On the other side of the coin, members are not interested in committing to longer term deposits because they feel rates are going up. The combined pressure of these two natural tendencies will lead to even greater shrinking of the financial margins. Therefore, the shrinking financial revenues means credit unions must either reduce expenses or find alternative sources of revenues or a combination of the two. Historically speaking, credit unions have been reluctant to jump on the "service charge bandwagon", but Boards will be forced to address this with greater scrutiny in the next year. Cost cutting and rationalization of expenses is gaining prominence in many credit unions. More and more groups of credit unions have entered into discussions about amalgamating in order to preserve the availability of local credit union services to their members at reasonable costs. Currently, serious discussions are going on in the Clare District as well as preliminary discussions in several groups of credit unions in Cape Breton.

We have attempted to assist credit unions in cost cutting by

Credit Unions on the Intervention System in 1996

Intervention System	Total January 1996	Additions During 1996	Removal During 1996	Total December 1996
Early Warning List	9	5	5	9
Performance Improvement Plan	8	2	2	8
Supervision	1	-	-	1
Total	18	7	7	18

reducing our assessment rates in 1996 from ¼of 1% of assets to 20 basis points. With claims down significantly again this year to approximately $200,000, we have made significant progress in our equity building program. Not counting the $465,000 in the Directors Liability Shared Deductible Pool, we ended 1996 with equity of $5,563,000 which represents 0.73% of the system assets. (See Figure 1)

This is well on the way to achieving our target of 1%. This significant increase in equity should be maintained in 1997 because we are in the final year of the amortization of the settlement with Credit Union Central of Nova Scotia and therefore our income will recognize the final $700,000. However, the low interest rates are significantly affecting our interest income, although I am pleased to report that we have again been able to cover the costs of operations before grants from our interest income. Because of these factors, the Board will wait to see what progress is made in our equity building program before there are any decisions made with respect to the final assessment rate for 1997. At this point, we expect that the 1997 rate will again be 20 basis points; however, if we again have low claim experience, there may be an opportunity for some reconsideration prior to the final billing next November. Our current projections based upon annual claims in the $500,000 range indicate we should meet our minimum target of equity perhaps as early as the end of 1998 but definitely by the end of the amortization of the prepaid assessments in 1999.

During 1996, the Advisory Committee for Sound Business Practices developed a Standard relating to Impaired Loans in order to assist in the adaptation of the new Section 3025 of the Canadian Institute of Chartered Accountants Handbook. This was recommended to and adopted by our Board and became effective for the December 31, 1996 year end. The Board also adopted the Standard on Audit and Internal Control and one on Asset and Liability Management which had been previously circulated as Exposure drafts. As well, a model policy dealing with Asset and Liability Management was developed jointly with Central's staff and credit unions with assets in excess of $10 Million were asked to develop ALM policies and submit them to us for review.

The development of our monitoring system is progressing and starting to show positive results. For example, we are monitoring delinquency on a monthly basis and following up on unacceptable trends. The result has been a significant reduction in system delinquency (Figure 2) due to the additional attention and efforts by credit union managers to keep delinquency within acceptable parameters.

We have been able to download financial data from League Data directly into our system and are developing a monthly base of financial information which we will utilize to implement trend analysis which will allow us to hopefully detect undesirable trends at an earlier stage.

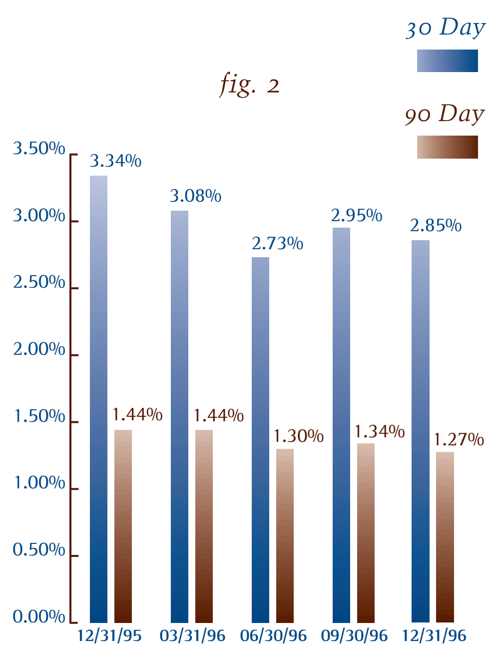
All in all, I am pleased with the progress the system has made in 1996. It appears that 1997 will also bring significant challenges to the credit union movement and as a result to us. We will be working with credit unions to deal with problems as they arise.

As well, we will be striving to improve our service to credit unions and their members. We are developing an Internet site and hope to use this to provide guidance to credit unions and to answer questions members may have on deposit insurance coverage. You can contact us at www.nscudic.org. We are working on the development of a newsletter to address emerging issues and provide clarification on existing issues. Our overall objective in 1997 is to provide friendly, efficient service and to work with Credit Union Central and credit unions to ensure that credit union members have a safe and sound financial institution to meet their ever changing needs.

Respectfully submitted,

Barry C. Bennett, C.A.
Chief Executive Officer

fig. 2



System Delinquency

Staff

*CEO **Barry Bennett** (right) meets with Accountant **Joyce Clarke** and Credit Union Analysts **Norbert Gagnon** (left) and **Vernon MacNeill** (centre)*

*Accountant **Joyce Clarke** (left) & Secretary **Beverly O'Quinn** (right).*

*Secretary, **Karen Conrad***

*Credit Union Analysts: **Vernon MacNeill** (top), **Bernie Beaton** (centre) & **Norbert Gagnon** (above).*

Auditors' Report

To the Members of
Nova Scotia Credit Union Deposit Insurance Corporation

We have audited the balance sheet of Nova Scotia Credit Union Deposit Insurance Corporation as at December 31, 1996 and the statements of earnings and retained earnings, and changes in cash resources for the year then ended. These financial statements are the responsibility of the corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the 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 financial statements present fairly, in all material respects, the financial position of the corporation as at December 31, 1996 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Doane Raymond

Halifax, Nova Scotia
January 16, 1997

Chartered Accountants

Statements of Earnings and Retained Earnings

Year Ended December 31

	1996	1995
Earnings		
Investment income	$ 740,374	$ 845,826
Assessments and recoveries (Note 10)	2,449,241	2,590,621
	3,189,615	3,436,447
Expenses		
Operating		
Board and committees	67,238	91,254
Depreciation	26,952	22,245
Insurance	21,998	17,487
Legal	1,331	5,881
Office	23,752	29,771
Occupancy costs	50,770	50,023
Professional fees	34,337	36,113
Salaries and employee benefits	392,147	333,937
Telephone	13,428	10,993
Travel	89,142	69,915
	721,095	667,619
Financing		
Interest on long term debt		66,000
Conditional grants and loan purchases (Note 11)	201,091	520,830
	922,186	1,254,449
Net earnings	$ 2,267,429	$ 2,181,998

Retained earnings, beginning of year	$ 3,319,787	$1,163,980
Net earnings	2,267,429	2,181,998
Transfer to shared deductible pool reserve (Note 8)	(23,536)	(26,191)
Retained earnings, end of year	$ 5,563,680	$ 3,319,787

See accompanying notes to the financial statements.

Balance Sheet

December 31

	1996	1995
Assets		
Cash	$ 5,726	$ 658,183
Receivables (Note 3)	443,351	449,966
Prepaids	5,732	3,974
Investments (Note 4)	9,427,709	9,043,107
Furniture and equipment (Note 5)	75,042	60,481
	$ 9,957,560	$10,215,711
Liabilities		
Payables and accruals (Note 6)	$ 834,834	$ 1,753,811
Unearned revenue (Note 7)	3,093,510	4,700,000
	3,928,344	6,453,811
Equity		
Shared deductible pool reserve (Note 8)	465,536	442,113
Retained earnings	5,563,680	3,319,787
	6,029,216	3,761,900
	$ 9,957,560	$10,215,711

Commitments and contingent liabilities (Note 12)
Lease commitments (Note 14)

On behalf of the Corporation

Director

Director

See accompanying notes to the financial statements.

Statement of Changes in Cash Resources

Year Ended December 31

	1996	1995
Cash derived from (applied to)		
Operating		
Net earnings	$ 2,267,429	$ 2,181,998
Depreciation	26,952	22,245
	2,294,381	2,204,243
Change in non-cash operating working capital (Note 9)	(2,520,610)	2,303,621
	(226,229)	4,507,864
Financing		
Repayment of long term debt		(1,100,000)
Investing		
Redemption (purchase) of investments (net)	(384,602)	(2,701,374)
Purchase of property and equipment	(41,626)	(63,314)
	(426,228)	(2,764,688)
Net increase (decrease) in cash	(652,457)	643,176
Cash		
Beginning of year	658,183	15,007
End of year	$ 5,726	$ 658,183

See accompanying notes to the financial statements.

Notes to the Financial Statements

December 31, 1996

1. Nature of operations

The Nova Scotia Credit Union Deposit Insurance Corporation is a body corporate established under the Credit Union Act to provide deposit insurance to members of credit unions and to ensure the financial stability of credit unions.

2. Summary of significant accounting policies

Investments
Investments are recorded at face value. Premiums or discounts on the acquisition of investments are recorded as investment income in the year of disposal.

Gains or losses realized on investments within the managed investment portfolio are reported as investment income during the year.

Depreciation
Furniture, equipment and leasehold improvements are depreciated over their useful lives as follows:

Furniture	20% declining balance
Computer equipment	40% declining balance
Leasehold improvements	5 years straight line

3. Receivables

	1996	1995
Credit Union assessments	$ 10,177	$ 5,368
Accrued interest	428,178	439,090
Other	4,996	5,508
	$ 443,351	$ 449,966

4. Investments

	Weighted Average Interest Rate	Duration (Years)	1996 Cost	1996 Market Value	1995 Cost	1995 Market Value
Credit Union Movement	4.79%	.33	$ 4,077,699	$ 4,077,699	$ 2,868,097	$ 2,868,097
Managed portfolio	7.82%	3.45	5,000,000	5,380,853	5,000,000	5,261,237
Provincial bonds and others	8.16%	2.26	350,010	359,320	1,175,010	1,192,578
			$ 9,427,709	$ 9,817,872	$ 9,043,107	$ 9,321,912

5. Furniture and equipment

	Cost	Accumulated Depreciation	1996 Net Book Value	1995 Net Book Value
Furniture and equipment	$ 109,940	$ 51,672	$ 58,268	$ 38,118
Leasehold improvements	27,954	11,180	16,774	22,363
	$ 137,894	$ 62,852	$ 75,042	$ 60,481

Notes to the Financial Statements

December 31, 1996

6. Payables and accruals

	1996	1995
Grants and loan purchases	$	$ 242,161
Trade	12,195	14,012
Unclaimed shares and deposits	47,639	47,639
Accrual for claims under commitments	625,000	854,999
Accrual for deficit funding	150,000	595,000
	$ 834,834	$ 1,753,811

7. Unearned revenue

	1996	1995
Unearned portion of Credit Union Central of Nova Scotia's settlement for its obligations under Financial Plan 1984	$ 700,000	$ 1,500,000
Prepaid assessment fees	2,393,510	3,200,000
	$ 3,093,510	$ 4,700,000

In accordance with agreements with the Central and the Credit Unions, the amount will be amortized to income on the following basis:

1997	$ 1,497,837
1998	797,836
1999	797,837
	$ 3,093,510

8. Shared deductible pool reserve

The reserve was established to fund a shared deductible pool for director's liability insurance. The first $5,000 of the claim will be paid by the credit union and any residual, up to a maximum of $95,000, will be paid from the reserve. Income earned on the funds will be credited to the reserve. The Corporation's liability is limited to funds available in the reserve.

During the year, interest income in the amount of $23,536 was transferred to the reserve.

9. Change in non-cash operating working capital

	1996	1995
Receivables	$ 6,615	$ 215,239
Prepaids	(1,758)	4,742
Payables and accruals	(918,977)	(216,360)
Unearned revenue	(1,606,490)	2,300,000
	$ (2,520,610)	$ 2,303,621

10. Assessments and recoveries

	1996	1995
Special assessments		
Credit Union Central of Nova Scotia	$800,000	$900,000
Credit unions' assessments - regular	1,456,679	1,577,271
Recovery of conditional grants	192,562	113,350
	$ 2,449,241	$ 2,590,621

11. Conditional grants and loan purchases

	1996	1995
Conditional grants paid and accrued in the year		
North Isle Madame	$ 137,091	$ 4,373
Strait Area Credit Union	17,106	
Valley Credit Union	225,817	
	380,014	4,373
Loan purchases made during the year		
Bergengren re: Canso		5,260
Credit Union Atlantic re: Eastern Passage	56,866	30,181
Credit Union Atlantic re: Russell	123,467	197,160
Heritage re: Tidal		72,947
Heritage re: St. Albans	1,269	
Margaree Credit Union re: St. Columba	202	
Strait Area Credit Union	41,288	22,752
Sydney re: Louisbourg		5,891
Valley Credit Union	272,985	619,400
	496,077	953,591
Total conditional grants and loans purchases	876,091	957,964
Decrease in accruals for claims considered likely under commitments	(675,000)	(437,134)
	$ 201,091	$ 520,830

12. Commitments and contingent liabilities

(i) Commitments in effect at December 31, 1996

The Corporation has provided protection to credit unions so they will not suffer losses on loans acquired in certain amalgamations, or as part of a deficit funding agreement. As at December 31, 1996, the Corporation has outstanding commitments in the amount of $1,085,000. Of this amount, $625,000 has been accrued in these financial statements and represents management's best estimate of the likely liability under these commitments. The liability, if any, associated with the remaining identified problem accounts of $460,000 are not determinable at this time.

(ii) Deficit funding

To provide estimated funding for identified problems in certain credit unions, the Corporation has accrued an amount of $150,000 in these financial statements.

Notes to the Financial Statements

December 31, 1996

13. Income taxes

The loss carry-forward for income tax purposes amounts to $1,751,293 and expires as follows:

December 31, 1997	$ 131,771
December 31, 1998	571,750
December 31, 1999	532,890
December 31, 2000	310,406
December 31, 2001	204,476

Any tax benefits of this loss carry-forward have not been recognized in the financial statements.

14. Lease commitments

The Corporation is committed to pay annual lease payments for its premises and vehicles for the next three years as follows:

1997	$ 68,779
1998	68,779
1999	57,304
	$ 194,862