

**ANNUAL REPORT OF THE AUDIT AND OPERATIONAL RISK
COMMITTEE**

It is my pleasure to present the annual report of the Audit and Operational Risk Committee of Community Credit Union of Cumberland Colchester Limited for the 2017 fiscal year. The Committee's mandate is outlined in considerable detail in provincial legislation, (*Credit Unions Act – Audit Committee*) and is further documented in the credit union's By-Laws and Board Policy.

The purpose and objectives of the Audit and Operational Risk Committee are outlined in Board-approved Terms of Reference and is summarized as follows:

"Purpose

The Audit and Operational Risk Committee's principal role is to ensure that due diligence is directed towards gaining assurance that an effective risk management and control framework, has been implemented by management. This framework is to provide reasonable assurance that the financial, operational and regulatory objectives of the Credit Union are achieved and that the governance and accountability responsibilities of the Board and management are met.

The Audit and Operational Risk Committee undertakes responsibility for the oversight of the design and implementation of internal controls to support the risk management framework, the integrity of financial reporting, and compliance with regulatory matters.

Objectives

The objectives of the Audit and Operational Risk Committee are:

- *To assist the Board to fulfill its oversight responsibilities, including accountable management of funds, efficiency and effectiveness of controls, safeguarding of assets and member deposits;*
- *To gain assurance that there is compliance with laws, regulations and policies;*
- *To gain assurance regarding the reliability of external financial reporting;*
- *To provide for independence of the internal audit function;*
- *To communicate concerns of the Board to the internal and external auditors and to have input into the overall direction of all audit efforts;*
- *To engage external auditors and provide appropriate oversight of their work; and*
- *To promote effective and timely resolution of audit issues."*

The Committee's mandate during the year included financial and risk management oversight to the credit union. Throughout the 2017 fiscal year, the Committee met on a minimum quarterly basis, to assess the financial and risk management activities and results. The findings and subsequent action plans and activities were reported to the Board of Directors.

2017 Activities:

- Loan Interest Income – As reported in previous years, we continue to offset our low personal lending results, with the purchase of Concentra mortgage pools. As a direct result, we maintained our net interest income performance in 2017 to that of 2016. With this pool reducing on a monthly basis, we were able to continue to purchase an additional mortgage pools from our system partner Concentra Financial. With the increasing challenge in growing our personal lending portfolio, and in addition to purchasing mortgage pools, we have increased our participation in small business regional loan syndications. Both of these initiatives, are the primary drivers of lending growth again this year.
- Deposit Interest Expense – Throughout 2017 our net deposit position was virtually the same as that of 2016. As a result of this position, our interest expense has remained relatively consistent with a nominal impact on our gross financial margin.
- Financial Margin – We are pleased with our continued Gross Margin position, which has remained strong throughout the past several years and again in 2017 at **4.47%** compared to 2016 at 4.45%. We will continue our due diligence to maintain our Gross Margin above the 4.00% level by managing our excess liquidity in a prudent manner.
- Operating Expense – Our operating expenses, at 4.18% in 2017, increased slightly over the 2016 performance of 4.08%. Overall expenses remained consistent year over year with only a nominal 0.10% increase in 2017 over 2016. This is an important financial area, which will require continued oversight and effective management, particularly during a low interest rate environment. We will continue to monitor this area very closely to ensure we experience financial stability.
- Operating Surplus – Our pre-tax operating surplus decreased from 0.38% in 2016 to **0.29%** in 2017, which remains above the minimum benchmark set by our Regulator at 0.25%. This reduction is primarily due to an unexpected loan loss in 2017. In a low interest rate environment, achieving this level of operating surplus requires continued investment diligence, alternative income sources as well as a very diligent expense management. These three important areas will continue to be addressed in 2018 and beyond in an effort to maintain our operational surplus well above the regulatory benchmark and our strategic objective of 0.50%.

We are pleased with the satisfactory and stable financial performance during 2017 and we are confident continued improvement in our revenue opportunities and our expense management mandate will again be evident throughout the 2018 fiscal year and beyond. Our performance to date is directly attributed to the effectiveness of our ongoing financial management activities, which will continue to evolve in 2018 and beyond. A more detailed analysis will be provided by our President & CEO.

In 2017, the Committee, through the Board, was directly involved in continued '*governance development*' sessions, intended to establish further oversight practices to financial and operational risk.



The Committee is comfortable that the 2017 Financial Statements present fairly, in all material respects and free from material misstatement, the financial position of Community Credit Union and the results of its operations were in accordance with International Financial Reporting Standards.

I would like to take this opportunity to express my appreciation to the committee members for their diligence and attention and the significant work completed throughout the past year. As well, on behalf of the committee, I would like to extend our sincere appreciation to our President & CEO, Darrell Kuhn, our Vice President, Corporate and Lending Services, Edith Doyle and Phemie Horvath, our Financial Services Clerk for their continued financial management activities.

*Respectfully submitted by
Darrell Jones, Committee Chair
April 25, 2018*