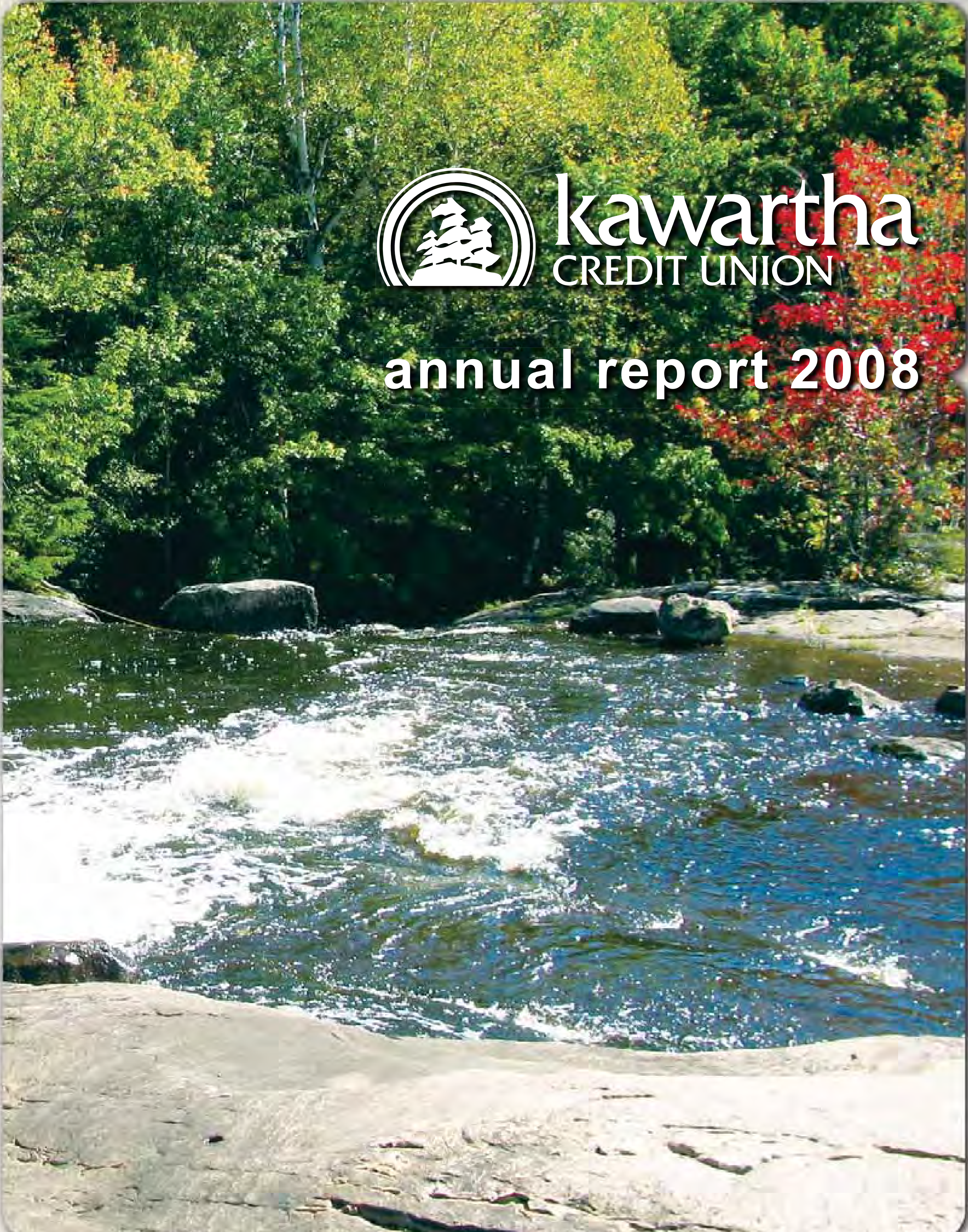

kawartha
CREDIT UNION

annual report 2008

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REPORT TO THE MEMBERS

The past year has been the most challenging we have faced in over a decade, for a number of reasons. However, we are pleased to report that despite these challenges, Kawartha Credit Union had another successful year, meeting most of our growth and profitability targets.

CHALLENGES

The global credit crisis, triggered by sub-prime mortgage lending in the United States, spread to Canadian financial markets in late 2007. We have witnessed a worldwide credit tightening, a restructuring of the U.S. financial industry on a scale not seen in decades and Canadian banks record huge write-downs. The implication for Kawartha has been a narrowing of our financial margin caused by wide credit spreads that have driven up the cost of funds while the Bank of Canada pushed down the Prime lending rate. In response, Kawartha made a concerted effort to raise deposits (successfully) and took advantage of rare opportunities to securitize mortgages in order to bolster our liquidity position. We also took action to reduce our interest rate risk exposure in these uncertain times.

Closer to home, the Credit Union Centrals of Ontario and British Columbia merged to form Central 1 Credit Union. After months of delays due to valuation issues with Ontario Central's Asset Backed Commercial Paper (ABCP) holdings, the merger was completed on July 1, 2008. To facilitate the merger, Ontario credit unions were required to participate in a plan to support Ontario Central by purchasing these troubled assets (ABCP) via a limited partnership. The implications for Kawartha are that we invested $3.5 million in limited partnership units. Although we expect to earn a return on that investment in time, the Montreal Accord restructuring has experienced repeated delays resulting in this being a non-performing asset to date. Additionally, the wide credit spreads symptomatic of the credit crisis have caused at least a temporary impairment in the value of the ABCP. In response, Kawartha has taken a write-down of $350,000 as a measure of prudence.

ACCOMPLISHMENTS

Despite these external distractions, Kawartha enjoyed a number of significant achievements in 2008.

PEOPLE

Most notably, in January we were thrilled to learn that Kawartha placed fifth in the Best Small-Medium Employers in Canada study. This is a national competition sponsored by Queen's School of Business, Hewitt Associates and the Globe & Mail. This year's study featured 250 participating companies and so ranking fifth in a program of this stature is truly an accomplishment. Briefly, the purpose of the study is to measure employee engagement. The benefits to Kawartha from participation are primarily threefold. With an 85% correlation between employee engagement and organizational results, measuring and learning how to increase employee engagement has real bottom line benefits. In addition, the publicity received from this program helps attract and retain

Board of Directors *– Left to Right (Back to Front): Ellen Menzies (Recording Secretary), Janice James, Carl Silvestri (Chair), Earl Robbins, Harvey Spry, Ken Stickle, Lloyd Churchill, Robert George, Robert Lake, Ellen Stewart*

REPORT TO THE MEMBERS (continued)

great employees as well as appeal to our members and non-members. And finally, improving as an employer has a positive impact on member service delivery.

MEMBER SERVICE

Late in the year we launched our new Affinity Share program, which has been very well received by the membership. Affinity Shares are a reward for doing business with Kawartha – the more business a member does with us, the more shares they receive. The program is also a means for Kawartha to demonstrate one of the benefits of membership. By distributing a portion of our retained earnings to members, we reaffirm that the Credit Union is owned by our members. This is a significant point of differentiation from our bank competitors, which is often overlooked. It is our intent that this will be an ongoing program with distributions to members every year, subject to financial constraints.

In response to member requests, we introduced enhancements to our flat fee service packages this year along with two new packages for both individuals and commercial members. Key additions were unlimited transactions on personal accounts and the inclusion of Kawartha Direct Internet and Telephone banking at no additional cost on all packages. We also introduced cross border debit card transactions through the ACCEL point-of-sale network, providing access to one of the largest POS networks in the United States with more than 1,000,000 merchant locations in the network. In conjunction with these enhancements, we also reviewed our service charges on personal and commercial accounts to ensure that our fees are competitive and cover our costs. As a result we increased a number of fees, including cheque clearing and most counter transactions, effective October 1, 2008. We recognize that service fee increases are always unpopular, so these changes were only made after careful review and consideration by the Board and management with the goal that our fees will still be equal to or less than fees for comparable services at the banks. For many of these fees, this was the first increase in over a decade. On the whole we are proud to confirm that our service fees represent better value than our competitors.

Senior Management Team *– Left to Right (Back to Front): Stuart Forsyth, Jennifer Mowry, Julian Sellers, Crystal Dayman, Laurianne Gruzas, Louise Coleman, Rob Wellstood, Cheryl Pearce*

During 2008 we continued to invest in a number of facilities upgrades to improve member service. As promised last year, we refurbished the branch inside the PepsiCo plant in Peterborough, adding an ATM for 24x7 access to cash, and a private office to support the provision of lending and investing services right in the plant. We have also created a new Commercial Services Centre attached to the Parry Sound branch to better serve our members in that area. Finally, while not a direct member service enhancement, we renovated the former Peterborough Industrial Credit Union office converting it into our Training Centre. Feedback from staff on the facility has been excellent.

FINANCIAL RESULTS

In 2007, your Board and Management set another ambitious goal to double the asset size of your Credit Union: to reach $1 billion in assets by September 30, 2012 by staying true to our values and our purpose. We set that goal because we remain convinced that principled and member focussed growth is essential to ensure the continuing success of Kawartha Credit Union.

In 2008, total assets under management grew by $63 million or 12% to end the year at $580 million. Balance sheet assets grew by $43 million or 9%, lower than the total because we completed two securitization transactions through CMHC's Canada Mortgage Bond program. As the economy cooled through 2008, so did consumer loan demand, and $28 million of residential mortgage growth was securitized, leaving the consumer portfolios essentially unchanged over the year. We had another record year in commercial lending, with growth of 28%, moving our asset mix in the desired direction. Deposit growth of $74 million or 18% allowed us to eliminate our loans from Central and build liquidity. Capital grew by $3.5 million or 10%, primarily due to continuing strong profitability. In 2008 Kawartha distributed $1.4 million in Affinity Shares to members, based on the volume of business done with the Credit Union. Net income of $3.8 million or 0.75% of average assets was down 14% from 2007 but operating income of $5.0 million was right on budget. This provided a return on average equity of 10.3%, below our target range of 13% - 16% but supporting the payment of a 7% dividend on Class A Investment Shares totalling $889,000 and a 6% dividend on Class B Affinity Shares of $86,000. Once again, Kawartha maintained its healthy financial position with regulatory capital of 7.4% on a leverage basis or 13.3% on a risk weighted basis and liquidity of 15.3% at year end, both well in excess of statutory requirements and providing a prudent cushion against the current market turbulence and economic slowdown.

2009 AND BEYOND

At the time of writing, we are in the midst of a global credit crisis which shows no signs of relenting. The Canadian economy is in a significant slowdown, with Ontario particularly hard hit. In setting our plans we have scaled back our growth targets accordingly and forecast lower profitability as a result of the current interest rate environment. Nevertheless, we fully expect to continue to grow and prosper in this difficult business environment. The credit crisis will subside and the economic cycle will turn around.

On behalf of the Board and Management team, we want to thank all Kawartha employees for their dedication to service excellence. Through their efforts, we have completed another very successful year under difficult business conditions. We also want to thank our members for rewarding us with your support. We will continue to do our best to earn your trust and your business.

Finally, we want to take this opportunity to extend our sincere thanks to Wanda Byrne, whose retirement we celebrated with mixed emotions at the end of June. Wanda started with Kawartha Credit Union over twenty-nine years ago and worked her way up through a variety of positions to that of Vice President, Consumer Credit. During that time she made a tremendous contribution to the company through her unflagging work ethic and unwavering dedication to member service. She is a leader, a mentor, and a friend. Thank you Wanda.

Respectfully,

Carl Silvestri
Chair of the Board

Robert Wellstood
Chief Executive Officer

CREDIT STATISTICS

Total applications for credit	**6678**		
Rejected requests	**1021**		
Accounts in arrears greater than 90 days	**202**	**$**	**3,752,470**

APPROVED CREDIT

Consumer Loans	1890	$	25,794,939
Consumer Lines of Credit	1804	$	36,607,525
Consumer Overdraft Agreements	218	$	115,200
Residential Mortgages	501	$	73,691,233
Commercial Loans	7	$	532,328
Commercial Lines of Credit	20	$	705,000
Commercial Overdraft Agreements	15	$	37,400
Commercial Mortgages	72	$	38,868,649
Total Approved Credit	**4527**	**$**	**176,352,274**

COMMERCIAL DEVELOPMENT 2008

COMMERCIAL LOANS BY TYPE OF BUSINESS

Type of Business	# of Loans	Disbursed
Agriculture, Forestry, Fishing & Hunting	1	$ 800
Construction	14	596,178
Manufacturing	4	433,271
Retail Trade	11	2,080,050
Transportation & Warehousing	1	1,355,250
Finance & Insurance	2	85,000
Real Estate - Rental & Leasing	27	8,582,863
Administrative, Support, Waste Management	3	56,500
Health Care & Social Assistance	5	2,414,586
Arts, Entertainment & Recreation	6	4,173,947
Accomodation & Food Services	27	18,012,508
Other Services	12	2,172,332
TOTAL	**113**	**39,963,285**

COMMERCIAL LOANS BY SIZE

Size		
Less than $25,000	31	$ 220,180
$25,000 to $99,999	15	833,782
$100,000 to $499,999	35	8,976,158
over $500,000	32	29,933,165
TOTAL	**113**	**39,963,285**

2008 COMMUNITY INVOLVEMENT PROGRAM

Kawartha Credit Union has a proud tradition of giving back to the communities we serve to make them vibrant and strong. We support causes that matter most to our members, including hospitals, health-care programs, youth, education, community development, and the environment. In 2008, we invested $100,000 (roughly 2% of our pre-tax earnings) in important causes in the regions that encompass our 19 branches. Our support is provided in the form of donations, sponsorships, gifts-in-kind and the various ways our employees volunteer their time and talents. Our community investments, whether in the form of corporate donations or staff participation, make a difference.


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Representing Kawartha Credit Union's 2008 Community Involvement Program, Cathy Martin, Monaghan Road Branch Manager, presents a $2000 cheque to Tricia Clarkson of Homegrown Homes.

Kawartha Credit Union Makes a $2000 Donation to Homegrown Homes

Through its Community Involvement Program, Kawartha Credit Union continues to give back to the communities we serve with a $2000 donation to Homegrown Homes to help provide affordable housing to those in need.

Tricia Clarkson, Research and Resource Development Coordinator for Homegrown Homes, was pleased to accept the donation. "As a non-profit organization, Homegrown Homes depends on the community and our fundraisers to support our efforts. This gift from Kawartha Credit Union is very much appreciated and will be used to help provide affordable, accessible and sustainable housing for those in need, which will improve the quality of life in our community."

www.kawarthacu.com

EMPLOYEE INVOLVEMENT

Kawartha Credit Union's amazing employees provide important leadership to a variety of community organizations, campaigns and events. Our enthusiastic volunteers build strong relationships with our community partners, and many Kawartha Credit Union staff help drive community fundraising efforts, while others contribute their energy and enthusiasm to organized events. Our branches/departments have participated in almost 50 initiatives in 2008 – above and beyond our formal Community Involvement Program.

HEALTHCARE

From local health centers to broader health concerns, Kawartha Credit Union supports healthcare initiatives that benefit the greatest number of people in the communities we serve. We also lend a hand to community programs that encourage physical activity and healthy lifestyles, and we help to set an example by participating in a number of events that promote staying active and healthy. Our 2008 initiatives in this area include (see left):

- Peterborough Dragon Boat Festival (Platinum Sponsor)
- Parry Sound Dragon Boat Festival (Gold Sponsor)
- Huntsville District Memorial Hospital Foundation
- Burk's Falls & District Health Centre (Miles for Coins)
- Northumberland Hills Hospital Foundation
- Trenton Memorial Hospital Foundation
- South Muskoka Hospital Foundation
- North Hastings Hospital Foundation
- Peterborough Regional Health Centre
- Ross Memorial Hospital (Lindsay)
- West Parry Sound Health Centre
- Peterborough Aids Resource Network (P.A.R.N.)
- Hospice North Hastings
- Victoria's Quilts

AIDS Walk for Life

Dragon Boat Festival

YOUTH AND EDUCATION

Literacy and learning are a powerful force in improving the quality of life and enhancing prosperity in the communities we serve. They are equally powerful in encouraging the development of a skilled and well-educated workforce for Kawartha Credit Union. The following initiatives were funded by Kawartha Credit Union during the 2008 fiscal year (see right):

- City of Kawartha Lakes Boys & Girls Club
- Kawartha Haliburton Childrens' Foundation
- Quinte Childrens' Foundation
- Food For Kids, Peterborough
- Food For Kids, City of Kawartha Lakes
- Food For Learning, Prince Charles School
- Northumberland Food For Thought
- Breakfast Club, North Hastings High School
- Risk Watch


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CREDIT UNION

Representing Kawartha Credit Union's 2008 Community Involvement Program, Rob Wellstood, CEO, presents a $5,000 cheque to Julie Davis, President & CEO of the PRHC Foundation, and Sheila Hamilton, VP Clinical and Chief Nursing Officer, of PRHC.

Kawartha Credit Union Makes a $5,000 Donation to Peterborough Regional Health Centre Foundation

Through its Community Involvement Program, Kawartha Credit Union continues to make our community a better place to live with a $5,000 donation to Peterborough Regional Health Centre Foundation.

PRHC Foundation President and CEO Julie Davis was pleased to accept the donation. "We look to our community to assist our efforts and Kawartha Credit Union's continued support is generous and very much appreciated. Like KCU we are dedicated to making a difference. This contribution will help to transform health care for our community with new equipment and technology."

In keeping with their Mission Statement, Kawartha Credit Union strives to improve the quality of life within the communities they serve.

www.kawarthacu.com

ENVIRONMENT

Ensuring that our children understand the importance of a healthy, sustainable environment is of paramount importance to us. Causes and initiatives that support education and awareness are key to our program.

- Peterborough Childrens' Water Festival

COMMUNITY SUPPORT AND DEVELOPMENT

We have a responsibility to support programs and projects that contribute to the well-being, development, prosperity, and quality of life in our communities. From festivals to the arts, from shelters to community centers, we believe that our contributions help to strengthen the infrastructures that support independence (see left).

- Peterborough YMCA
- Peterborough & Victoria County YWCA
- Bracebridge Arts Council
- Victoria Womens' Resource Centre
- Northumberland Services For Women
- Womens' Own Resource Centre (South River)
- Esprit Place (Parry Sound)
- Homegrown Homes (Peterborough)
- Chrysalis Womens' Shelter (Huntsville)
- Maggie's Resource Centre (Bancroft)
- North Hastings Community Trust

In addition to the organizations mentioned here, Kawartha Credit Union contributes to a variety of causes throughout the year. These opportunities are often community-based, and we carefully disburse funds to affect the greatest and most positive community advantage.

"Support the Shorts" Food Drive

AUDITORS' REPORT

To the Members
Kawartha Credit Union Limited

We have audited the balance sheet of Kawartha Credit Union Limited as at September 30, 2008 and the statements of income, comprehensive income, members equity and cash flows for the year then ended. These financial statements are the responsibility of the Credit Union's management. 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 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 Credit Union as at September 30, 2008 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

BDO Dunwoody LLP

Chartered Accountants, Licensed Public Accountants

Peterborough, Ontario
October 24, 2008

REPORT FROM THE AUDIT COMMITTEE

The Audit Committee's function is to assist the Board of Directors in fulfilling its oversight responsibilities by reviewing the financial information and reporting processes including the risks and controls related to those processes which management and the Board have established.

The Audit Committee is composed of four directors and has adopted a mandate that includes all of the tasks specified for Audit Committees in the Credit Unions and Caisse Populaires Act, 1994 and the associated regulations.

The Audit Committee met five times during the 2008 fiscal year to complete its responsibilities. Key activities included:

- Review the financial statements and the results of the year end audit with the external auditor;
- Review the performance of the Auditors and their proposed engagement letter;
- Ensure that regulatory filings were submitted on time;
- Review the Credit Union's policies, procedures, and controls for legislative compliance;
- Review the disaster recovery plan;
- Monitor the adherence of Directors, Officers, and employees with the Credit Union's policies and code of conduct;
- Review outstanding legal issues;
- Review accounting issues;
- Review risk management issues; and
- Review director and officer expense claims.

Management has implemented all Committee recommendations and there are no matters which the Committee believes should be reported to the members or which are required to be disclosed pursuant to the Act or the regulations.

Respectfully submitted,

Ken Stickle

Ken Stickle, Committee Chair
Committee: Lloyd Churchill, Robert George, Harvey Spry, Robert Lake

BALANCE SHEET

At September 30

	2008	2007
Assets		
Cash resources (Note 1b)	$ 33,900,361	$ 22,906,217
Liquidity deposits (Note 1b)	35,822,871	32,595,365
Loans to members (Note 4a)	439,500,630	415,870,019
Investments (Note 5)	7,351,765	2,576,618
Other assets	4,046,618	3,505,866
Capital assets (Note 6)	5,537,266	5,856,043
Derivative financial instruments (Note 17)	27,318	112,993
	$ 526,186,829	**$ 483,423,121**
Liabilities		
Term loans (Note 9a)	$ -	$ 35,000,000
Members' deposits (Note 7a)	482,245,925	407,841,166
Accounts payable and accrued liabilities	5,276,439	5,154,898
Derivative financial instruments (Note 17)	459	260,490
	487,522,823	**448,256,554**
Members' Equity		
Class A Investment Shares (Note 14)	12,494,685	12,494,685
Class B Affinity Shares (Note 14)	1,438,014	-
Membership Shares (Note 14)	825,453	820,023
Contributed surplus	169,301	169,301
Retained earnings	24,065,094	21,800,556
Accumulated other comprehensive income	(328,541)	(117,998)
	38,664,006	35,166,567
	$ 526,186,829	**$ 483,423,121**

Approved by the Board:

Carl J. Silvestri | Ken Stickle

Director | Director

The accompanying notes are an integral part of these financial statements

STATEMENT OF INCOME

For the year ended September 30

	2008	2007
Financial Revenue		
Interest on loans to members (Note 4c)	$ 27,324,121	$ 25,171,028
Investment income	1,584,941	1,190,748
	28,909,062	26,361,776
Financial Expense		
Interest on deposits (Note 7b)	13,040,882	10,012,158
Interest on borrowings (Note 9a)	903,606	1,087,320
	13,944,488	11,099,478
Financial Margin	14,964,574	15,262,298
Other Income	5,422,169	4,103,703
	20,386,743	19,366,001
Operating Expenses		
Salaries and employee benefits	8,100,922	7,078,729
Loan loss expense (Note 4d)	937,485	695,992
Occupancy	1,744,967	1,659,047
Banking costs	544,797	571,448
Other expenses (Note 13)	1,864,899	1,689,597
Data costs	915,216	841,933
Deposit insurance	294,663	280,675
Promotion	852,530	720,159
Directors' expenses	109,755	61,650
	15,365,234	13,599,230
Operating Income	5,021,509	5,766,771
Other Items		
Write down of investments (Note 5)	100,000	-
Vault cash program (recovery) loss	(43,000)	(104,000)
	57,000	(104,000)
Income before income taxes	4,964,509	5,870,771
Income tax expense (Note 21)	1,170,000	1,445,000
Net Income	**$ 3,794,509**	**$ 4,425,771**

The accompanying notes are an integral part of these financial statements

CASH FLOW STATEMENT

For the year ended September 30

		2008		2007
Cash Provided by Operations (Note 15)				
Net Income	$	3,794,509	$	4,425,771
Adjustments to Cash Basis of Accounting				
Amortization of Capital Assets		997,047		928,511
Changes in Liquidity Deposits		(3,227,506)		(12,821,799)
Changes in Other Assets		(540,752)		(761,545)
Changes in Accounts Payable		121,541		640,159
Changes in Allowance for Loan Losses		479,975		302,286
Changes in Tax Effect Related to Derivative Financial Instruments		(34,899)		29,499
Net Mortgage Securitization Premium		(138,455)		-
Write Down of Investments		100,000		-
		1,551,460		(7,257,118)
Cash Provided by (Advanced to) Members				
Increase in Members' Deposits		74,404,759		46,244,418
Increase in Shares		1,443,444		64,360
Dividends Paid to Members, Net of Tax		(626,957)		(701,957)
Class B Affinity Share Issuance, Net of Tax		(903,014)		-
(Increase) Decrease in Loans to Members		(52,265,078)		(59,049,758)
		22,053,154		(13,442,937)
Financing Activities				
Term Loans Advanced (Repaid)		(35,000,000)		26,500,000
Proceeds of Mortgage Securitization		28,292,948		-
		(6,707,052)		26,500,000
Investment Activities				
Purchases of Fixed Assets (net of disposals)		(678,271)		(1,871,647)
(Increase) Decrease in Investments		(5,225,147)		(186,230)
		(5,903,418)		(2,057,877)
Increase in Cash Resources During the Year		10,994,144		3,742,068
Cash Resources - Beginning of the Year		22,906,217		19,164,149
Cash Resources - End of the Year	**$**	**33,900,361**	**$**	**22,906,217**

The accompanying notes are an integral part of these financial statements

STATEMENT OF MEMBERS' EQUITY

For the year ended September 30

	2008	2007
Class A Investment Shares		
Opening Balance	$ 12,494,685	$ 12,494,685
Net change during the year	-	-
Ending Balance	12,494,685	12,494,685
Class B Affinity Shares		
Opening Balance	-	-
Share issuance	1,438,014	-
Ending Balance	1,438,014	-
Membership Shares		
Opening Balance	820,023	755,663
Net change during the year	5,430	64,360
Ending Balance	825,453	820,023
Contributed Surplus		
Opening Balance	169,301	169,301
Net change during the year	-	-
Ending Balance	169,301	169,301
Retained Earnings		
Opening Balance	21,800,556	18,076,742
Add: Net Income	3,794,509	4,425,771
	25,595,065	22,502,513
Less: Class B Affinity Shares Issued	(1,438,014)	-
Related Tax Savings	535,000	-
Less: Dividends Paid on Class A Investment Shares	(886,957)	(886,957)
Related Tax Savings	260,000	185,000
Ending Balance	24,065,094	21,800,556
Accumulated Other Comprehensive Income		
Opening Balance	(117,998)	-
Other Comprehensive Income (loss)	(210,543)	(117,998)
Ending Balance	(328,541)	(117,998)
Total Equity	**$ 38,664,006**	**$ 35,166,567**

STATEMENT OF COMPREHENSIVE INCOME

For the year ended September 30

	2008	2007
Net Income (Page 12)	$ 3,794,509	$ 4,425,771
Other Comprehensive Income		
Gains (Losses) on Financial Derivatives Designated as Cash Flow Hedges, Net of Tax Effect	139,457	(117,998)
Fair Value Adjustment on the Investment in ABCP 2008 Limited Partnership (Note 5)	(350,000)	-
	(210,543)	(117,998)
Comprehensive Income	**$ 3,583,966**	**$ 4,307,773**

The accompanying notes are an integral part of these financial statements

1. SIGNIFICANT ACCOUNTING POLICIES

a) Nature of Business
Kawartha Credit Union Limited is incorporated under the Credit Unions and Caisses Populaires Act and is a member of the Deposit Insurance Corporation of Ontario and of Central 1 Credit Union Limited.

b) Cash Resources and Liquidity Deposits
The term "cash resources" as used in these financial statements consists of cash on hand and fixed rate term investments which are issued by Central 1 or are government backed. Carrying value of investments approximates market value. Investments mature within three years and provide a yield of 3.28%.

c) Capital Assets and Amortization
Capital assets are recorded at acquisition cost. The Credit Union provides amortization on substantially all its property and equipment using the straight line method at the rates set out below, designed to amortize costs over the expected useful life of the respective assets.

Parking lot		25 years
Building		25 - 50 years
Building	- interior renovations	10 years
Equipment	- computer	3 - 5 years
	- furniture & other	5 - 10 years
Leasehold improvements		Remaining term of the lease
Member files		5 – 10 years

d) Income Taxes
The Credit Union follows the asset and liability method of accounting for income taxes, whereby future tax assets and liabilities are recognized for the expected future tax consequences attributable to temporary differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases.

e) Allowance for Impaired Loans
All loan assets are subject to recurring review and assessed for possible impairments. The Credit Union considers evidence of impairment at both a specific loan and a non-specific collective level. The specific portion of the allowance for impaired loans is calculated in accordance with generally accepted accounting principles as interpreted by By-law No. 6 of the Deposit Insurance Corporation of Ontario. The non-specific portion of the allowance is estimated based on historical loan losses incurred along with management's best estimate of future losses.

Loans are written off in the period in which they are identified. If an allowance for impairment has been recognized in relation to a loan, write-offs are made against the allowance. If no allowance for impairment has been previously recognized, write-offs are recognised as an expense in the statement of income.

f) Employee Future Benefits
The Credit Union sponsors a defined contribution pension plan. Contributions to the plan during the year were $305,830 (2007 - $281,231).

The Credit Union also provides health and dental benefits for retired employees who were employed on a full time basis prior to November 1, 2003. The Credit Union recognizes these post retirement costs in the period in which the employees render their services. The cost of employee future benefits earned by employees is actuarially determined using the Projected Unit Credit actuarial cost method prorated on services and management's best estimate of retirement ages of employees, employee turnover and expected health care costs. The most recent actuarial valuation of the obligation was performed as at October 1, 2005.

g) Mortgage Securitization
The Credit Union occasionally securitizes mortgages by selling them to Central 1 Credit Union Limited. Transfers of mortgages to Central are treated as sales provided that control over the transferred mortgages has been surrendered and consideration other than beneficial interests in the transferred mortgages has been received in exchange. Gains on these transactions are reported as other income on the statement of income. The amount of these gains are based on the present value of expected future cash flows using management's best estimates and key assumptions such as prepayment rates, excess spread, credit losses and discount rates. The Credit Union has a contractual obligation to service the loans on behalf of the transferee.

h) Revenue Recognition
Interest income on member loans and investments is recorded as revenue using the accrual method based on the number of days the loan or investment is outstanding.

Other income includes service charges and various fees. Service charges are generally for monthly services and are charged and recorded as revenue on a monthly basis. Fees are recorded as revenue when the service generating the fee has been provided.

i) Use of Estimates
The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management's best estimates as additional information becomes available in the future.

j) Financial Instruments - Recognition and Measurement
Financial assets and financial liabilities are initially recognized at fair value and are subsequently accounted for based on their classification as described below. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Except in very limited circumstances, the classification is not changed subsequent to initial recognition. Financial assets purchased and sold, where the contract requires the asset to be delivered within an established time frame, are recognized on a trade-date basis. Transaction costs are recognized immediately in income or are capitalized, depending upon the nature of the transaction and the associated product.

Held for trading financial instruments continue to be recorded on the balance sheet at fair value with the change in fair value being reported in income under other income for the period. Under Section 3855, any financial asset or liability whose fair value can be readily measured may be classified on initial recognition as being held for trading. This designation is then irrevocable. Kawartha Credit Union has classified it's cash resources, securitization assets, accounts payable and derivative financial instruments as held for trading.

Available for sale financial instruments continue to be recorded on the balance sheet at fair value unless they are not quoted on an active market, in which case they are recorded at cost. The change in fair value is reported in other comprehensive income until they are derecognized. Kawartha Credit Union has classified it's investments as available for sale.

Financial instruments that have a fixed maturity date, where the Credit Union intends and has the ability to hold to maturity, are classified as held to maturity and are accounted for at amortized cost using the effective interest rate method. Kawartha Credit Union has classified it's liquidity deposits as held to maturity.

Loans and receivables and other liabilities are accounted for at amortized cost using the effective interest rate method. Kawartha Credit Union has classified it's loans to members as loans and receivables and it's term loans and members' deposits as other liabilities.

Fair value is based on the market price when an active market exists. Otherwise, it is estimated using valuation methods and techniques such as discounted cash flow analysis or option pricing models, based on observable market factors.

k) Derivative Financial Instruments and Hedges
The Credit Union periodically enters into derivative contracts to manage financial risks associated with movements in interest rates and other financial indices. The Credit Union does not enter into derivative financial instruments for speculative purposes.

Derivative financial instruments, including embedded derivatives which are required to be accounted for separately, are recorded on the balance sheet at fair value. Derivatives forming part of a hedging relationship can be designated as part of a fair value hedge or a cash flow hedge. In a fair value hedge, the hedging instrument and the impact of the designated risk on the hedged item are measured at fair value. When such changes in fair value are not completely offset, the resulting gain or loss is recognized under other income. For a cash flow hedge, gains or losses resulting from changes in the fair value of the effective portion of the derivative instrument will be recorded in other comprehensive income until the hedged item is recognized in income, at which time such change is recognized under interest income. The ineffective portion will be recognized immediately in income under other income. For derivative financial instruments that are not part of a hedging relationship, changes in fair value are recognized under other income.

Note 17 to the financial statements for the year ending September 30, 2008 describes the Credit Union's derivative financial instruments including those eligible for hedge accounting and the risk management policy relative to derivative financial instruments.

l) Comprehensive Income
Other comprehensive income includes, in particular, unrealized gains and losses on available-for-sale financial assets and the change in the effective portion of a cash flow hedge transaction. The financial statements include a Statement of Comprehensive Income and Accumulated Other Comprehensive Income which is presented as an equity item on the balance sheet.

2. NEW ACCOUNTING POLICIES

On October 1, 2007, Kawartha Credit Union adopted the new standards of the Canadian Institute of Chartered Accountants (CICA) entitled "Capital Disclosures" (Section 1535), "Financial Instruments - Disclosures" (Section 3862) and "Financial Instruments - Presentation" (Section 3863). The main requirements of these standards are set out below.

a) Capital Disclosures
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.

b) Financial Instruments - Disclosures and Presentation
CICA Handbook Section 3862, Financial Instruments - Disclosures increases the disclosures currently required to enable users to evaluate (i) the significance of financial instruments for an entity's financial position and performance and (ii) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and how the entity manages those risks. CICA Handbook Section 3863, Financial Instruments - Presentation, replaces the existing requirements on the presentation of financial instruments, which have been carried forward unchanged. These two Handbook sections replaced Handbook Section 3861, Financial Instruments - Disclosure and Presentation.

3. 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:

International Financial Reporting Standards
The CICA plans to converge Canadian GAAP with International Financial Reporting Standards ("IFRS") over a transition period expected to end in 2011. The impact of the transition to IFRS on the Credit Union's financial statements has yet to be determined.

4. LOANS TO MEMBERS

a) Summary

	2008	2007
Personal loans	$ 120,486,693	$ 118,040,808
Residential mortgages	209,637,944	212,644,458
Commercial loans	111,218,755	86,625,604
	441,343,392	417,310,870
Accrued interest receivable	766,605	688,541
	442,109,997	417,999,411
Allowance for impaired loans	(2,609,367)	(2,129,392)
Net loans to members	**$ 439,500,630**	**$ 415,870,019**

b) Fair Value Information

Variable rate loans are based on a "prime rate plus" formula. The rate above prime is determined by the type of security offered and the borrowers' credit worthiness. The Credit Union's prime rate at September 30, 2008 is 4.75% and fluctuates with the market. The net carrying value of variable rate loans to members approximates their fair value. Fixed rate loans are offered at rates which are determined by the level of market rates, the type of security offered and the borrowers' credit worthiness. The fair values of fixed rate loans are estimated by discounted cash flow techniques using interest rates currently offered for loans with similar risk characteristics and terms to maturity.

Accordingly, the estimated fair values of member loans at September 30, are as follows:

	2008	2007
Personal loans	$ 120,225,000	$ 117,945,000
Residential mortgages	209,520,000	209,801,000
Commercial loans	109,922,000	86,302,000
	$ 439,667,000	**$ 414,048,000**

The key economic assumptions used in measuring the fair value of member loans at September 30, 2008 were as follows:

	Personal Loans	Residential Mortgages	Commercial Loans
Prepayment rate	10%	8%	5%
Weighted-average life	2.14 years	2.74 years	2.60 years
Market rate	6.50%	5.51%	6.25%

c) Interest Income

	2008	2007
Personal loans	$ 8,641,290	$ 9,085,716
Residential mortgages	11,794,110	10,342,521
Commercial loans	6,888,721	5,742,791
	$ 27,324,121	**$ 25,171,028**

Personal loans are comprised of term loans, which account for 51% of the portfolio, and lines of credit which account for the remaining 49% of the portfolio. Repayment terms vary with the term length and loan type. Security may include collateral mortgages on real property, lodgement of title documents, investments, personal property and wage assignments. All personal loans are open for prepayment without penalty. Mortgage loans are secured by residential properties. Repayment is in the form of blended payments, with amortization periods ranging up to 40 years.

Loans to members had the following average yields at September 30, 2008:

	Principal	Yield
Variable rate loans	$ 158,316,710	6.24%
Fixed rate loans with maturities within one year	48,563,220	5.96%
Fixed rate loans with maturities beyond one year	234,463,462	6.18%
	$ 441,343,392	

d) Activity in the allowance for impaired loans has been as follows

	Personal Loans	Residential Mortgages	Commercial Loans	Total
2008				
Opening	$ 1,208,681	$ 212,985	$ 707,726	$ 2,129,392
Recoveries	49,020	-	-	49,020
Loan loss expense	785,231	28,394	123,860	937,485
	2,042,932	241,379	831,586	$ 3,115,897
Write-offs	(482,220)	(1,298)	(23,012)	(506,530)
Ending	**$ 1,560,712**	**$ 240,081**	**$ 808,574**	**$ 2,609,367**
Principal balance of impaired loans	**$ 1,440,275**	**$ 1,662,121**	**$ 650,074**	**$ 3,752,470**
2007				
Opening	$ 1,014,964	$ 209,263	$ 602,879	$ 1,827,106
Recoveries	40,859	-	-	40,859
Loan loss expense	579,611	3,722	112,659	695,992
	1,635,434	212,985	715,538	2,563,957
Write-offs	(426,753)	-	(7,812)	(434,565)
Ending	**$ 1,208,681**	**$ 212,985**	**$ 707,726**	**$ 2,129,392**
Principal balance of impaired loans	**$ 963,351**	**$ 1,431,338**	**$ 324,985**	**$ 2,719,674**

The allowance for impaired loans consists of an allowance for specific impaired loans and an allowance for non-specific groups of loans. The allowance for non-specific loans amounts to $1,228,000 (2007 – $1,335,000). At September 30, 2008, there were no formally restructured loans outstanding (2007 - none).

5. Investments

	2008	2007
Credit Union Central of Ontario, Membership	$ 4,207,359	$ 2,559,061
Central 1 Credit Union Limited, Membership	101	-
ABCP 2008 Limited Partnership	3,126,748	-
Co-operators General Insurance, Class A Series A	12,557	12,557
Credential Securities Inc., Debenture	5,000	5,000
	$ 7,351,765	**$ 2,576,618**

As a result of the merger of Credit Union Central of Ontario Limited (CUCO) with Credit Union Central of British Columbia (see below), the Credit Union's Membership shares in CUCO are to be exchanged for Membership shares in Central 1 Credit Union Limited (Central 1). CUCO membership shares must be maintained as determined by their Board of Directors from time to time and are currently at 0.82% of the Credit Union's total assets. The shares are redeemable at cost only if there is a reduction in the Credit Union's total assets at December 31 each year or upon withdrawal of membership. Accordingly, there is no separately quoted market value. Dividends on these shares are at the discretion of the Board of Directors of CUCO. Dividends received on these shares in 2008 amounted to $196 (2007 - $99,000). The fair values of the shares in Central 1 and the Co-operators are not readily determinable because of the lack of a resale market for them and accordingly, they are carried at cost. The June 30, 2008 audited financial statement for CUCO indicates that CUCO was in deficit immediately prior to the merger. Management believes that there has been an impairment in the value of the CUCO Membership shares and has estimated the Credit Union's loss to be $100,000, which has been provided for.

At a special general meeting held on May 31, 2008, members of Credit Union Central of Ontario Limited approved a resolution to facilitate the merger of CUCO and Credit Union Central of British Columbia (CUCBC) to form a new national financial services entity named Central 1.

As a pre-condition of this merger, CUCO was required to divest itself of investments in certain third-party asset-backed commercial paper (ABCP). The resolution approved the creation of ABCP 2008 Limited Partnership (ABCP LP) to acquire these investments funded by member credit unions in proportion to their share investment in CUCO. As a result, on June 30, 2008, immediately prior to the merger of CUCO and CUCBC, the excluded ABCP with a total par value of $186,916,000 was acquired by the ABCP LP at its estimated fair value of $133,564,000 including accrued interest, net of expenses, and other assets. As there was no liquid market in these ABCP investments, the fair values used to determine the acquisition price were provided by Edenbrook Hill Capital Ltd., a firm engaged by CUCO to provide an independent valuation of the assets underlying the ABCP investments. The valuation for each credit union's share of the ABCP LP was provided to them before closing and the Credit Union recorded the investment in ABCP LP units at a fair value of $3,476,748.

The ABCP LP is governed by a Board of Directors that was elected by Ontario member credit unions and each limited partner will record its proportionate share of net income or loss in the ABCP LP as determined by Canadian generally accepted accounting principals and subject to an annual external audit.

The ABCP holdings of the ABCP LP did not settle at their scheduled maturity dates and there has been no active trading of the ABCP since mid-August 2007. In December 2007, a group of participants in the ABCP market, including CUCO, banks, liquidity providers and major investors, known as the Pan-Canadian Investors Committee, proposed a restructuring for $32 billion of ABCP. Under this proposal, the underlying assets of the ABCP would be segregated between those eligible for the restructuring process and those which are ineligible. Separate classes of notes would be issued to investors representing their respective holdings of eligible assets in each of the ABCP conduits based on the relative fair value of those assets. Class A-1 and A-2 notes would be interest bearing, and the repayment of principal on these notes would be required before interest and principal payments could be made to Class B and C note holders. Investors may also receive Ineligible Asset Tracking Notes (IATN's) in respect of their ineligible assets. The payment of interest and principal on all classes would be subject to certain conditions.

ABCP LP units with a carrying value of $3,126,748 are net of a $350,000 fair value adjustment. The Credit Union has estimated the fair value of the ABCP LP units by discounting the expected future cash flows on the underlying Class A-1, A-2, B and C notes the ABCP LP expects to receive under the restructuring plan. In forecasting the expected future cash flows the Credit Union has made assumptions as to the timing and amount of cash flows expected to be received as well as market yield expectations on those instruments. Additionally, the Credit Union has made assumptions as to the fair value of IATN's that it expects the ABCP LP to receive as part of the restructuring process.

Uncertainty remains with respect to the timing and amount of future cash flows on the ABCP that could give rise to a material change in the value of ABCP LP's ABCP holdings and thus the value of the units. The Credit Union performed a sensitivity analysis of certain fair value assumptions. Based on a 5% favourable and a 5% unfavourable change in the discount rate and the expected cash flows, the Credit Union determined that the fair value adjustment could range from approximately $288,000 to $465,000.

6. CAPITAL ASSETS

	2008		2007	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Land and parking lot	$ 1,156,962	$ 48,905	$ 1,156,962	$ 48,770
Building	3,700,363	1,918,777	3,566,511	1,717,267
Equipment	5,818,435	4,541,258	5,370,808	4,107,390
Leasehold improvements	2,005,162	815,964	1,908,371	636,458
Member files	1,368,860	1,187,612	1,368,860	1,005,584
	$14,049,782	**$ 8,512,516**	**$13,371,512**	**$ 7,515,469**
Net book value		**$ 5,537,266**		**$ 5,856,043**
Amortization expense		**$ 997,047**		**$ 928,511**

7. MEMBERS' DEPOSITS

a)

	2008	2007
Chequing accounts	$ 101,250,173	$ 101,658,203
Demand savings accounts	36,562,135	36,900,538
Term deposits	232,828,373	174,718,460
Registered savings plans	84,692,716	68,690,971
Registered retirement income funds	17,601,314	18,000,852
Accrued interest on member deposits	9,311,214	7,872,142
	$ 482,245,925	**$ 407,841,166**

b) Interest on Deposits

	2008	2007
Chequing accounts	$ 547,658	$ 554,387
Demand savings accounts	267,855	261,789
Term deposits	8,405,829	6,077,208
Registered savings plans	3,070,293	2,435,457
Registered retirement income funds	749,247	683,317
	$ 13,040,882	**$ 10,012,158**

Chequing accounts and demand savings accounts are due on demand and bear interest at variable rates which depend upon the type of account and the balance maintained. Term deposits bear fixed rates of interest for terms up to five years. Interest can be paid monthly, annually or at maturity. Certain types of term deposits are callable by the depositor and account for 73% of the portfolio (2007- 73%).

Registered savings plans consist of fixed rate deposits which account for 97% (2007 - 97%) of the portfolio and variable rate deposits which comprise the remaining 3% (2007 - 3%) of the portfolio. Deposits which are callable by the depositor account for 62% of the portfolio (2007 - 65%), with the remaining 38% (2007 - 35%) being fixed for terms up to five years. The registered retirement income funds (RRIFs) are almost entirely fixed rate deposits for terms ranging up to five years. Members may make withdrawals from a RRIF on a regular schedule ranging from monthly to annually at amounts which vary according to individual needs.

Members' deposits have the following average yields at September 30, 2008:

		Principal	Yield
Variable rate deposits due on demand	$	140,056,513	0.63%
Fixed rate deposits with maturities within one year		174,285,975	3.80%
Fixed rate deposits with maturities beyond one year		158,592,223	4.27%
	$	**472,934,711**	

c) Fair Value Information

The carrying value of all variable rate deposits approximates their fair values. The fair values of fixed rate deposits are estimated by discounted cash flow techniques using interest rates currently offered for deposits with similar terms to maturity and assuming callable deposits are held to maturity. The estimated fair values of member deposits at September 30, are as follows:

		2008		2007
Chequing and demand savings accounts	$	137,812,000	$	138,559,000
Term deposits		231,931,000		180,919,000
Registered plans		102,530,000		90,495,000
	$	**472,273,000**	**$**	**409,973,000**

The key economic assumptions used in measuring the fair value of member deposits at September 30, 2008 were as follows:

	Non Registered Deposits	Registered Deposits
Weighted-average life	1.29 years	1.89 years
Market rate	4.01%	4.07%

8. EMPLOYEE FUTURE BENEFITS

The Credit Union pays certain post retirement benefits of its retired employees. The Credit Union recognizes these post retirement costs in the period in which the employees render the services. The accrued benefit obligation at September 30, 2008 of $3,130,700 (2007 - $2,892,200) and the net periodic benefit cost for the year ending September 30, 2008 was determined by actuarial valuation using a discount rate of 5.0% (2007 - 5.0%).

Information about the Credit Union's defined benefit plans is as follows:

		2008		2007
Accrued benefit obligation				
Balance at the beginning of the period	$	2,892,200	$	2,841,900
Service cost for the period		120,300		94,400
Interest cost for the period		149,900		130,300
Benefits cost for the period		(31,700)		(29,100)
Actuarial gain recognized in the period		-		(145,300)
Projected accrued benefit obligation at the end of the period as determined by actuarial valuation		3,130,700		2,892,200
Unamortized transitional obligation		(752,400)		(1,010,500)
Unamortized actuarial gain		600,800		663,100
Accrued liability	**$**	**2,979,100**	**$**	**2,544,800**

Components of net periodic benefit cost

		2008		2007
Service cost for the period	$	120,300	$	94,400
Interest cost for the period		149,900		130,300
Amortization of transitional obligation		258,100		258,200
Amortization of actuarial gain		(62,300)		(91,400)
Net periodic benefit cost	**$**	**466,000**	**$**	**391,500**

The main actuarial assumptions employed for the valuations are as follows:

General Inflation (CPI rate)	2.1%
Interest (discount) rate	5.0%

Medical costs were assumed to increase at the CPI rate plus a further increase of 4.9% in 2008, then graded down by one percentage point each year until reaching the CPI rate plus 2.9% in 2010 and thereafter.

Dental costs were assumed to increase at the CPI rate plus 2.9% in 2008 and thereafter.

9. COMMITMENTS

a) Credit Facilities

The Credit Union has authorized line of credit and term loan facilities with Central 1 Credit Union Limited totalling $49,750,000. There are no outstanding term loans at year end. The authorized line of credit bears interest at prime. Security given is an assignment of loans receivable and a general security agreement covering all assets of the Credit Union.

b) Loan Commitments

At September 30, 2008, the Credit Union is committed to advance approximately $3,431,221 on mortgage loans and $8,788,779 on commercial loans. In addition, lines of credit which had been approved but not used at year-end totalled approximately $53,513,954.

c) Lease Agreements

The Credit Union has entered into lease agreements for branch offices, with minimum future payments in each of the next five years as follows: 2009 - $772,520; 2010 - $758,214; 2011 - $676,056, 2012 - $628,048; 2013 – $606,038 and $3,440,876 in the aggregate.

d) Contingencies

The nature of the Credit Union's activities are such that there is usually litigation pending or in progress at any time. There were no claims at September 30, 2008.

10. CAPITAL ADEQUACY

The Credit Unions and Caisses Populaires Act, 1994, requires the Credit Union to maintain adequate regulatory capital, consisting of membership shares, any other class of qualifying share capital that may be issued and retained earnings. Adequate capital is defined as 4.25% of total assets and 8.0% of risk-weighted assets. At September 30, 2008, the Credit Union is in compliance with the Act and regulation.

	2008	2007
Total regulatory capital is composed of Tier 1 and Tier 2 capital as follows:		
Tier 1 Capital		
Class A Investment Shares	$ 12,494,685	$ 12,494,685
Less Redeemable Portion of Class A Shares	(769,000)	(769,000)
Class B Affinity Shares	1,438,014	-
Membership Shares	825,453	820,023
Contributed Surplus	169,301	169,301
Retained Earnings	24,065,094	21,800,556
Total Tier 1 Capital	38,223,547	34,515,565
Tier 2 Capital		
Redeemable Portion of Class A Shares	769,000	769,000
General Provisions	1,228,000	1,335,000
Other Comprehensive Income	(328,541)	(117,998)
Total Tier 2 Capital	1,668,459	1,986,002
Tier 1 and Tier 2 Capital	39,892,006	36,501,567
Future Income Taxes	(1,168,126)	(1,016,213)
Total Regulatory Capital	**$ 38,723,880**	**$ 35,485,354**

Total assets are adjusted for credit risk, market risk and operational risk factors to come up with the total risk adjusted assets as follows:

Credit Risk	257,416,589	224,971,308
Market Risk	1,050,000	675,000
Operational Risk	32,545,927	28,780,610
	$ 291,012,516	**$ 254,426,918**

The applicable capital ratios are as follows:

Tier 1 Capital to Risk Adjusted Assets	13.13%	13.57%
Total Regulatory Capital to Risk Adjusted Assets	13.31%	13.95%
Total Regulatory Capital to Total Assets	7.36%	7.34%

11. RESTRICTED PARTY TRANSACTIONS

The Credit Union has enacted a policy requiring disclosure and Board approval of all restricted party transactions. Restricted parties have been defined in the policy to include anyone who is, or has been within the preceding twelve months, a Director or Officer of the Credit Union, their spouse or relatives residing within the same house. The Credit Unions and Caisses Populaires Act, 1994, provides a broader definition of restricted parties which includes all relatives of Directors and Officers. There were 5 loans advanced to restricted parties as defined by policy during the year, and there are 24 loans outstanding to such parties with an aggregate value of $948,791 at September 30, 2008.

12. OTHER STATUTORY INFORMATION

Pursuant to the requirements of the Credit Unions and Caisses Populaires Act, 1994, the following information is provided:

	2008	2007
Director remuneration in the year	$ 75,600	$ 47,200
Deposit insurance premium paid in the year	$ 294,663	$ 280,675

13. OTHER EXPENSES

	2008	2007
Other supplies and postage	$ 409,032	$ 327,064
Equipment costs	248,711	254,010
Central dues & regulatory assessments	119,858	114,306
Amortization of member files	182,028	172,412
Savings and loan life insurance	73,779	74,702
Education and staff development	379,498	275,096
Bonding insurance	114,829	82,621
Professional services	95,090	135,523
Collection costs	65,555	53,213
Telephone	102,645	76,412
Miscellaneous	62,064	113,752
Central annual meeting	11,810	10,486
	$ 1,864,899	**$ 1,689,597**

14. SHARE CAPITAL

The Credit Union is authorized to issue an unlimited number of Membership shares with an issue price of $5 each. As a condition of membership, each member is required to hold $25 in membership shares. These shares are redeemable at cost only when membership is withdrawn, subject to certain statutory restrictions.

The Credit Union is authorized to issue an unlimited number of Class A shares, in series, with rights, privileges, restrictions and conditions to be determined by the Board of Directors, subject to statutory restrictions. The Credit Union has issued and outstanding 12,670,779 Non-Cumulative, Non-Voting, Non-Participating, Class A Series 1 Special Shares (Class A Investment Shares). The Class A Series 1 shares pay dividends at the discretion of the Board of Directors in the form of cash or additional shares. These shares are redeemable at the sole and absolute discretion of the Board of Directors and are subject to a maximum of 10% of the shares outstanding at the end of the previous fiscal year. The Credit Union has the option to redeem 7,675,391 of these shares in whole or in part at any time, and to redeem the remaining 4,995,388 shares in whole or in part after March 31, 2009.

The Credit Union is authorized to issue an unlimited number of Non-Cumulative Redeemable Non-Voting Non-Participating Class B Affinity shares. The Class B shares pay dividends at the discretion of the Board of Directors in the form of cash or additional shares. These shares are redeemable at the sole and absolute discretion of the Board of Directors on a date commencing five years after the issue date, subject to a maximum of 10% of the shares outstanding at the end of the previous fiscal year. On September 29, 2008 the Credit Union issued 1,438,014 Class B Series 2 Affinity Shares. The Credit Union has the option to redeem 1,438,014 of these shares in whole or in part after September 29, 2013.

15. CASH FLOW STATEMENT

The following amounts are included in the cash provided by operations:

		2008		2007
Cash paid for interest	$	11,555,964	$	8,795,327
Cash paid for income taxes	$	1,143,436	$	943,424

16. SEGMENT DISCLOSURES

The Credit Union operates in the loans and deposit-taking industry in Central Ontario and, based on the Credit Union's internal management reporting structure, only has one operating segment. Products and services offered to its members include personal and commercial loans, lines of credit and mortgages, chequing and savings accounts, registered and non-registered term deposits, registered retirement income funds, mutual funds and financial planning services.

17. DERIVATIVE FINANCIAL INSTRUMENTS

The Credit Union does not hold or issue derivative financial instruments for speculative purposes and controls are in place to prevent and detect these activities.

The Credit Union has outstanding $39,000 (2007 - $240,000) in Index-Linked Term Deposits to its members. The Index-Linked Term Deposits are three and five year deposits that pay interest at the end of the term, based on the performance of a variety of indices. The Credit Union has entered into hedge agreements with Central 1 to offset the exposure to the indices associated with this product, whereby the Credit Union pays a fixed rate of interest annually for the term of each Index-Linked Term Deposit on the face value of the deposits sold. At the end of the term, the Credit Union receives an amount equal to the amount that will be paid to the depositors, based on the performance of the indices.

The Credit Union enters from time to time into Interest Rate Swap contracts with Central 1 to hedge the Credit Union's exposure to interest rate risks. As at September 30, 2008 the Credit Union had entered into Interest Rate Swap contracts for a total of $140,000,000 of notional principal whereby it has agreed to pay at variable interest rates based on Bankers' Acceptance rates for 30 days and receive at fixed interest rates. These swap contracts have fixed interest rates ranging from 2.85% to 4.34% and will mature from December 2008 to September 2009. The agreements are secured by a general security agreement covering all assets of the Credit Union.

18. NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS

We are exposed to the following risks as a result of holding financial instruments: credit risk, market risk and liquidity risk. The following is a description of those risks and how we manage our exposure to them.

a) Credit Risk

Credit risk is the risk of financial loss to the Credit Union if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Credit Union's member loans.

Risk Measurement

Credit risk rating systems are designed to assess and quantify the risk inherent in credit activities in an accurate and consistent manner. Credit scoring is the primary risk rating system for assessing obligor and transaction risk for retail exposures.

Objectives, Policies, and Processes

Our credit risk management principals are guided by our overall risk management principles. The Board of Directors is involved in the management of credit risks. The Board ensures that management has a framework, and policies, processes and procedures in place to manage credit risks and that the overall credit risk policies are complied with at the business and transaction level.

Our credit risk policies set out the minimum requirements for management of credit risk in a variety of transactional and portfolio management contexts. Our credit risk policies comprise the following:

i) Loan general policy statements including approval of lending policies, eligibility for loans, exceptions to policy, policy violations, liquidity, and loan administration.
ii) Loan lending limits, including schedule of assigned limits.
iii) Loan collateral security classifications which set loan classifications, advance ratios and amortization periods.
iv) Procedures outlining loan overdrafts, release or substitution of collateral, temporary suspension of payments and loans renegotiation.
v) Loan delinquency controls regarding procedures followed for loans in arrears.
vi) Internal controls policy regarding audit procedures for lending activities.

The Credit Union's maximum exposure to credit risk in relation to each class of recognised financial asset is the carrying amount of those assets as indicated on the balance sheet. The maximum credit risk exposure does not take into account the value of any collateral or other security held. The Credit Union's maximum exposure to credit risk related to member loans as at September 30, 2008 was as follows

Loans that are not past due	$ 432,426,589
Loans that are past due	
under 30 days	3,695,168
30 to 89 days	2,772,981
90 -179 days	1,239,099
180 - 365 days	908,951
over 365 days	300,604
	$ 441,343,392

At a minimum all loans that are over 90 days past due are considered impaired. There are 202 loans with a combined principal of $3,752,470 considered to be impaired. The security held on these loans totalled $2,849,236

Our credit risk policies, processes and methodologies have not changed materially in the past year.

b) Market Risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, equity or commodity prices, and credit spreads. We are exposed to market risk in our asset/liability management activities. The level of market risk to which we are exposed varies depending on market conditions and expectations of future price and yield movements.

Asset/Liability Management
Traditional banking activities, such as deposit taking and lending, expose us to market risk, of which interest rate risk is the largest component. Our goal is to manage the interest rate risk of the balance sheet within established limits. We continually monitor the effectiveness of our interest rate risk mitigation activity.

Risk Measurement
Our risk position is measured monthly. Measurement of risk is based on rates charged to members as well as funds transfer pricing rates.

Objectives, Policies, and Processes
Management is responsible for managing our interest rate risk, monitoring approved limits and compliance with policies and operating standards. The Credit Union has established policies and related reporting to manage its exposure to fluctuating interest rates (referred to as interest rate risk). Without these policies, the Credit Union's earnings would be impacted, either positively or negatively, as interest rates change.

The Credit Union's major source of income is financial margin, the difference between interest earned on investments and member loans and interest paid on member deposits.

The objective of "interest rate sensitivity" management is to match interest-sensitive assets with interest-sensitive liabilities as to amount and as to term to their interest rate repricing dates, thus minimizing fluctuations of income during periods of changing interest rates.

The following schedule shows the Credit Union's sensitivity to interest rate changes, after including the effect of interest rate swap agreements:

(in thousands)	Assets	Liabilities and Equity	Gap
Maturities			
Current	$ 157,802	$ 137,697	$ 20,105
< 6 months	66,863	148,633	(81,770)
1 year	57,635	33,213	24,422
2 years	67,347	82,047	(14,700)
3 years	67,946	44,740	23,206
4 years	58,027	28,395	29,632
5 years	43,053	32,966	10,087
> 5 years	247	-	247
	518,920	507,691	11,229
Non-interest sensitive items	7,267	18,496	(11,229)
	$ 526,187	**$ 526,187**	**$ -**

Amounts with floating (including adjustable) interest rates, or due on demand, are classified as variable rate products maturing in under one year, regardless of maturity. Amounts that are not interest sensitive are grouped together, regardless of maturity.

A significant amount of loans and deposits can be settled before maturity on payment of a penalty. No adjustment has been made for repayments that may occur prior to maturity.

As at September 30, 2008, the weighted average rate for interest-bearing assets is 5.92% and for interest-bearing liabilities is 3.23%.

Based on the Credit Union's interest rate positions at September 30, 2008 the following table shows the potential before tax impact of 100 basis points (bps) increase or decrease in interest rates on the Credit Union's net income.

	2008	2007
100 bps increase	$ 279,000	$ 305,000
100 bps decrease	$ (278,000)	$ (305,000)

The interest rate risk policy has been approved by the board of directors and for the year ended September 30, 2008 the Credit Union was in compliance with the policy.

Our overall market risk policies and procedures have not changed materially in the past year.

c) Liquidity Risk
Liquidity risk is the risk that we may be unable to generate or obtain sufficient cash or its equivalent in a timely and cost effective manner to meet our commitments as they come due.

Risk Measurement
The assessment of our liquidity position reflects management's estimates, assumptions and judgments pertaining to current and prospective firm-specific and market conditions and the related behaviour of our members and counterparties.

Objectives, Policies and Processes
Our liquidity and funding management framework is designed to ensure that adequate sources of reliable and cost-effective cash or its equivalents are continually available to satisfy our current and prospective financial commitments under normal and contemplated stress conditions.

We monitor and mange our liquidity position and consider regulatory, operational and any other applicable restrictions. The Board of Directors is responsible for oversight of our liquidity framework.

The Credit Unions and Caisses Populaires Act, 1994 requires that the Credit Union maintain adequate liquidity, defined as a minimum of 8% of borrowings and member deposits, in certain classes of short term or liquid assets as defined in the regulations. The Credit Union complies with requirements regarding adequate liquidity at September 30, 2008.

As at September 30, 2008 the position of the Credit Union is as follows:

Qualifying liquid assets on hand	$ 69,721,494
Total liquidity requirement	37,913,558
Excess of liquidity requirement	**$ 31,807,936**

The table below summarizes the contractual maturities of the Credit Union's member deposits and existing loan commitments as at September 30, 2008

	on demand	less than one year	one to five years
Member deposits (Note 7)	$ 140,056,513	$ 174,285,975	$ 158,892,223
Loan commitments (Note 9)	53,513,954	12,220,000	-
	$ 193,570,467	**$ 186,505,975**	**$ 158,892,223**

There have been no material changes to our liquidity and funding management framework or levels of liquidity and funding risk in the past year.

19. SUBSEQUENT EVENT

On October 22, 2008, the Board of Directors of the Credit Union passed a resolution to declare a dividend of 7% on the Class A Investment Shares, payable to the shareholders of record at September 30, 2008. The amount of the dividend will be $889,387, with a corresponding tax saving of $185,000.

On October 22, 2008, the Board of Directors of the Credit Union passed a resolution to declare a dividend of 6% on the Class B Affinity Shares, payable to the shareholders of record at September 30, 2008. The amount of the dividend will be $86,450, with a corresponding tax saving of $17,000.

20. MORTGAGE SECURITIZATIONS

During the year Kawartha Credit Union securitized residential mortgages of $28,154,493 (2007 - $nil). The Credit Union retains mortgage servicing responsibilities but does not receive an explicit servicing fee for its servicing responsibilities.

The total amount of securitized mortgages under administration as at September 30, 2008 was $53,780,165 (2007 – $33,532,637)

The following table summarizes the Credit Union's securitization activity for the period ended September 30.

	2008	2007
Net cash proceeds received	$ 28,292,948	$ -
Premium	262,981	-

The key economic assumptions used in measuring the fair value of retained interests at the date of securitization were as follows:

	2008	2007
Prepayment rate	10%	-
Weighted-average life	4.5 years	-
Expected annual credit losses	-	-
Residual cash flow discount rate	5.710%	-

At year end the key economic assumptions and the sensitivity of the current fair value of residual cash flows of two different adverse changes in those assumptions are shown below:

	2008	2007
Carrying value of retained interests	$ 1,630,598	$ 331,551
Weighted-average life	3.682 years	2.75 years
Prepayment rate assumption	8%	8%
Impact of a 10% prepayment	$ (55,000)	$ (5,000)
Impact of a 20% prepayment	$ (109,000)	$ (11,000)
Residual cash flow discount rate	5.563%	5.096%
Impact of a 1% point adverse change	$ (14,000)	$ (3,000)
Impact of a 2% point adverse change	$ (29,000)	$ (9,000)

These sensitivities are hypothetical and should be used with caution. Changes in fair value based on a variation of assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of retained interests is calculated without changing any other assumption; generally, changes in one factor may result in changes in another, which may magnify or counteract the sensitivities.

21. INCOME TAXES

The effects of temporary differences, which give rise to the future income tax assets reported in other assets on the balance sheet, are as follows:

	2008	2007
Employee future benefits	$ 655,000	$ 746,000
Allowance for impaired loans	233,000	415,000
Capital assets	133,000	144,000
Other	39,000	40,000
	$ 1,060,000	**$ 1,345,000**

The provision for income taxes differs from the result which would be obtained by applying the combined Canadian Federal and Provincial Statutory income tax rates to income before income taxes. This difference results from the following items:

	2008	2007
Income before income taxes	$ 4,964,509	$ 5,870,771
Statutory income tax rate	34.16%	36.12%
Expected income tax expense	1,695,876	2,120,522
Increase(decrease) in taxes resulting from:		
Available credit union small business deduction	(1,205,613)	(756,377)
General tax reduction unavailable	387,911	216,108
Non-deductible expenses and other reconciling items	291,826	(135,253)
Income tax expense	**$ 1,170,000**	**$ 1,445,000**

The income tax expense consists of the following:

	2008	2007
Current provision	$ 885,000	$ 1,973,000
Future provision	285,000	(528,000)
	$ 1,170,000	**$ 1,445,000**

KAWARTHA CREDIT UNION STAFF RECOGNITION AWARDS

	2004	2005	2006	2007	2008
BRANCH AWARDS					
Highest Overall Growth %	Cobourg	Emsdale	Huntsville	Huntsville	Little Britain
Highest Overall Growth $	Lansdowne	Lansdowne	Trenton	Monaghan	Monaghan
100% Club	South River	Emsdale	South River	Kinmount	*No Entry*
INDIVIDUAL AWARDS					
Manager of the Year	Therese Touchette	Cathy Martin	Connie White	Dana Farrell	Connie White
Extra Mile Award	Kathy Warner	Shirley Davis	Eon Dalzell	Janice Barber Francine Currie	Carol Davis Linden Gage Lana Koch
Glen Davies Award	Susan Maloney	Donna Fuller	Janice O'Neill	Steve Olmstead	Kristy Tremblett

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