OUR BRANCH COMMUNITIES:

Bracebridge • Burk's Falls • Bancroft • Cobourg • Coe Hill • Emsdale

Huntsville • Kinmount • Keene • Lindsay • Little Britain

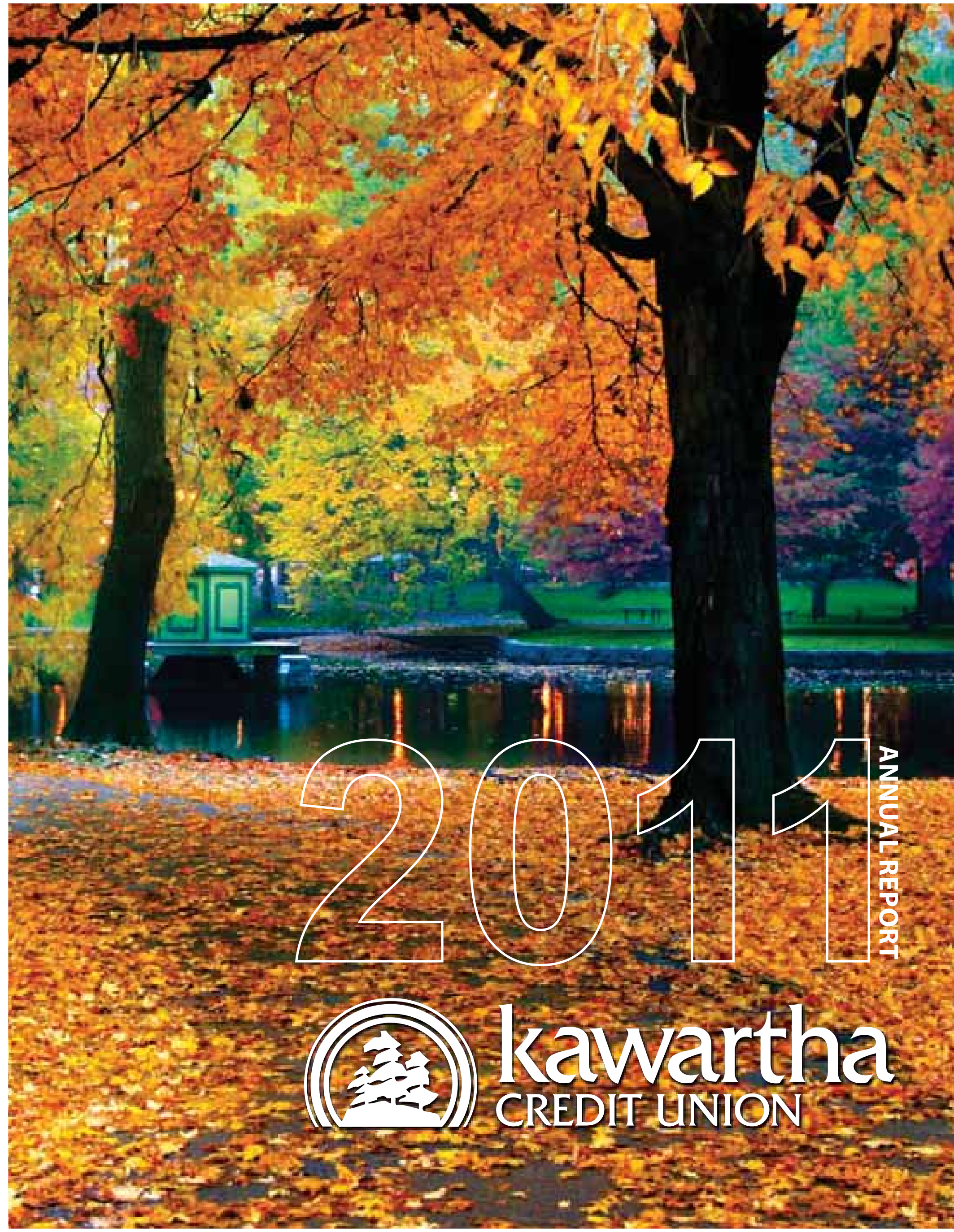
Magnetawan • Parry Sound • Peterborough • South River • Trenton

PHOTOS:

Huntsville, Ontario

kawartha
CREDIT UNION

www.kawarthacu.com



kawartha
CREDIT UNION

Annual Report 2011

Management Team

TABLE OF CONTENTS

REPORT TO THE MEMBERS

Your Board and management are pleased to provide this report on the activities of the past year along with the highlights of initiatives we are working on for the future. In a year that was noted for uncertainty and continuing economic challenges around the world, we have stayed true to our plan for Kawartha Credit Union. Our strategic focus on member and employee engagement paid dividends again last year. Despite a weak economy, we invested in new initiatives to improve member service and promoted a record number of employees to support the growth of the company. We completed a brand survey, with some surprising results and really put the Governance Committee to work. The financial results were solid with continuing growth and a modest increase in profit, allowing the Board to return over $2 million to members in the form of Affinity Shares and to declare over $1.2 million in cash dividends. As we look to the future, we have a continued emphasis on growth to provide the scale and resources we need to prosper in an increasingly competitive industry. We have a number of exciting initiatives underway to achieve this growth. We hope you find this report interesting and informative.

STRATEGIC DIRECTION

As regular readers of our annual reports may remember, Kawartha's overarching strategic direction is to leverage above average member and employee engagement to drive superior financial performance for the benefit of our members – the owners of the credit union. We have well-defined strategies which are monitored and reviewed regularly to achieve that objective. This strategic direction has served Kawartha well over the past several years, carrying the company through the recent recession and slow recovery with continuing above-average growth and profitability. At our strategic planning session earlier this year, the Board and management confirmed this direction, while revising some of the strategies to fit the current environment.

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

In the area of member engagement, we work to make you so proud to belong to Kawartha Credit Union that you will want to bring your friends and family to bank with us. Our primary strategy to achieve this is providing all members with financial advice and solutions that are suited to your personal needs – not the product of the month. We call this Member Service Excellence. With that in mind, we opened a member Contact Centre this year, staffed with experienced Kawartha employees, to better support members after our branches are closed or to visit you at your convenience. This has been well-received, with over $14 million of business booked by the Contact Centre within its first year of operations and has already received many member testimonials. We also upgraded our mobile banking service to allow full account access for bill payments and transfers in addition to account balance and activity information, for convenient anywhere, anytime banking using your smartphone. Another initiative to make you proud to belong to Kawartha is our Community Involvement Program, because members have told us it is important to them that we support their communities. Since inception, this program has invested over $1 million to improve the quality of life in the communities we serve. Please see page 8 for more details.

At Kawartha we want every employee to be committed with their heart and their mind to the success of the credit union. We measure this through biannual participation in the Best Small & Medium Employer in Canada survey conducted by Queens University and AON Hewitt. Past participation has taught us a good deal about what it takes to achieve this goal. Recognition of employee contributions, both formally and informally, is a critical component and one we take seriously. Examples of formal recognition are the staff recognition awards found on page 24, and our service awards whereby we celebrate every employee's anniversary with the company every five years. This year we celebrated with thirty-six employees whose service ranged from five to thirty-five years. Career development is also an important driver of employee engagement and we are pleased to report that during the past year, forty employees were promoted while another forty-six participated in temporary short-term transfers to different positions as part of our employee development initiatives. We also had seven employees receive accreditations in their area of expertise. Through previous surveys our employees have told us we could do a better job of performance management, and in response we are implementing a new performance management system. In June 2011, almost all of our employees went online to complete the BSME survey. We are anxiously awaiting the results which will be released in February 2012.

REPORT TO THE MEMBERS (continued)

For many years, your Board and management have held the view that the public's perception of Kawartha Credit Union is critical to the success of the organization. This year, we engaged Ipsos ASI to conduct a Brand Equity research study to help direct future marketing initiatives. The results were pleasing in some respects, sobering in others, and will be very useful to us going forward. Familiarity, market share, brand health and brand equity of Kawartha Credit Union in the Peterborough region (our largest market) are very much aligned with the big five banks. A quarter of members surveyed reported themselves as exclusively using Kawartha, on par with the banks. As well, Kawartha had the lowest percentage of lapsed members when compared to the banks, suggesting that if you try us you will like us and probably stay. Ratings on all metrics are weaker for all other regions, indicating we still have considerable work to do in those markets. A key finding of the study was that encouraging people to try Kawartha is a significant opportunity for growth.

Senior Management Team *– Left to Right; Stuart Forsyth, Jennifer Mowry, Crystal Dayman, Louise Coleman, Laurianne Gruzas, Cheryl Pearce, Julian Sellers, Robert Wellstood*

The effective and efficient management of the business operations and all risks to which the credit union is exposed has long been considered a key success factor by the Board and management. Effective governance is the first step and as previously reported, your Board of Directors formed a Governance Committee in 2010 to assist the Board in providing the best governance possible. New this year, a Governance Committee Report is included in the Annual Report, providing a summary of the activities and outcomes. During the past year we reviewed and enhanced our Enterprise Risk Management processes based on learnings from our participation in a working group drawn from the credit union system looking at best practices in this area. We also completed our search for a new computer system, negotiated contracts and have commenced the implementation process. This is a major undertaking which we expect will produce efficiencies and improved member service as well as position the company solidly for the future. We will be communicating with our members about this initiative in 2012, as we get closer to completing the implementation.

FINANCIAL RESULTS

In 2011, total assets under management grew by $49 million or 6.9% to end the year at $766 million. Balance sheet assets grew by $27 million or 4% and off-balance sheet assets grew by $22 million as we securitized $38 million of residential mortgages during the year. Personal loans and lines of credit increased by $10 million or 7.5%, due in part to the introduction of the Contact Centre. The total residential mortgage portfolio grew by $27 million or 8.3%, with $5 million on the balance sheet and $22 million in the pool of securitized mortgages. Commercial lending growth slowed to $16 million or 8.9% bringing this portfolio to 28% of total loan portfolios under management. Deposit growth of $47 million or 8.4% was just $6 million less than loan growth this year. With net securitization proceeds of $35 million, we were able to fund the difference and pay down the borrowings from Central by $28 million. Members' Equity grew by $5.6 million or 12%, primarily due to earnings. Once again, Kawartha maintained its healthy financial position with regulatory capital of 7.5% on a leverage basis or 12.9% on a risk adjusted basis and liquidity of 9.3% at year end, both well in excess of statutory and Board policy requirements.

Net income of $6.2 million or 0.91% of average assets was up 14% from 2010. This provided a return on average equity of 12.6%, close to our target range of 13% - 16% and supported the payment of a 7% dividend on Class A Investment Shares totalling $887,000 and a 6% dividend on Class B Affinity Shares of $345,000, in November 2011. As the interest rate environment in 2011 remained low and fairly stable, the 5.1% increase in the interest margin was primarily due to growth. The 14% increase in other income was primarily due to securitization income. The 11% increase in the operating expenses was primarily due to increases in salaries, benefits and other staff-related expenses as we added the equivalent of 16 full time employees to the staff complement. Due to the restructuring of one of our investments, we were able to change accounting classifications of that investment and recognize a $0.5 million increase in fair value. Loan loss expenses were up 8% from 2010, reflecting the ongoing high unemployment rate and an increase in the number of bankruptcies and resultant losses.

During fiscal 2011 Kawartha shared over $2 million of profit with our members in the form of Affinity Shares, as a reward for doing business with Kawartha, bringing the total outstanding to $5.7 million. This is an ongoing program with distributions to members every year, subject to financial constraints. The more business a member does with Kawartha, the more shares they receive.

Overall, the Board and management are pleased with the financial results of 2011, particularly within the context of the slow economic recovery and low interest rate environment. Asset growth was about half that of our long term target of 15% as we sought to balance risk and return with growth. Profitability was up slightly over 2010, providing a return on equity at the low end of our target range, contributing to a strengthening of our capital level.

LOOKING AHEAD

There is no question that the events of the past few years have permanently changed the financial services industry and the pace of change is increasing. For your Board of Directors and management this confirms our view that Kawartha Credit Union needs to continue to grow quickly. We have a number of initiatives underway to lay the foundation for that growth in addition to those mentioned earlier in this report, with the following two important examples.

Firstly, we are very pleased that as we write this report we have just announced that Kawartha Credit Union and Unity Savings and Credit Union have entered into negotiations to merge the two operations. Headquartered in Kingston, Unity is the largest credit union along the 401 corridor east of Kawartha's territory. In discussions to date, we have been struck by the similarities; especially our shared values and commitment to member service excellence. We believe this merger will be good for the members of both credit unions because it means additional locations throughout the province and access to enhanced products and services. The amalgamation is subject to regulatory approval as well as approval by the members of both credit unions. We look forward to explaining all the benefits of this combination to you at a special membership meeting planned for March, 2012.

Secondly, we are in the process of preparing for another offering of Class A Investment Shares to go on sale in early 2012. These uninsured shares add to the capital of the credit union and have been very popular with our members because of the premium return they have provided. The purpose of this offering is to increase the capital of the credit union in anticipation of continued growth.

On behalf of the Board and management team, we offer our sincere thanks to our employees for their dedication to Kawartha's success. Through their efforts the company has enjoyed another strong year. To our members, we thank you for your ongoing support. We will continue to do our best to earn your business and to make you proud to be a member of Kawartha.

Respectfully,

Robert Wellstood
Chief Executive Officer

Ken Stickle
Chair of the Board

REPORT FROM THE GOVERNANCE COMMITTEE

One of the goals of the Board of Directors is to provide the best governance possible for Kawartha Credit Union. In 2010, your Board formed a standing Governance Committee to assist in achieving that goal. More specifically, the purpose of the Governance Committee is to assist the Board in fulfilling its responsibility to create, promote and enhance policies and programs for:

a. Corporate governance
b. Board and committee composition
c. Director education, knowledge, skills and abilities

The Governance Committee met seven times in 2011. Key activities included:

1. Completed a review of all existing governance policies and made recommendations for improvement.
2. Recommended to the Board of Directors the appropriate qualifications and selection criteria for Directors.
3. Recommended Audit Committee member qualifications and training/continuing education requirements.
4. Recommended a new annual Committee member selection process.
5. Recommended a process for Board, Committee and Individual Director performance evaluation and worked with a consultant to develop and deliver the assessment.
6. Reviewed the draft DICO Guidance Note: Director Training and Qualifications.
7. Reviewed and made a recommendation to the Board regarding the adequacy of Director compensation.
8. Monitored compliance with the mandatory Director education program.

The Board has approved all Committee recommendations.

Respectfully submitted,

Earl Robbins

Earl Robbins, Committee Chair
Committee: Carl Silvestri, Janice James, Lloyd Churchill

CREDIT STATISTICS 2011

Total interviews for consumer and commercial credit:			
Consumer	**5354**		
Commercial	**771**		
Total declined requests for consumer and commercial credit:	**1159**		
Accounts in arrears greater than 90 days:	**117**	**$**	**4,430,996**

APPROVED CREDIT

Consumer Loans	1782	$	28,397,774
Consumer Lines of Credit	1501	$	38,336,844
Consumer Overdrafts	209	$	108,980
Residential Mortgages	620	$	99, 581, 761
Commercial Mortgages	78	$	36,451,038
Agricultural Mortgages	10	$	3,620,000
Commercial Loans	9	$	296,015
Agricultural Loans	3	$	123,000
Commercial Lines of Credit	22	$	2,612,500
Commercial Overdrafts	8	$	24,500
Total Approved Credit	**4242**	**$**	**209, 552, 412**

COMMERCIAL DEVELOPMENT 2011

COMMERCIAL LOANS BY TYPE OF BUSINESS

Type of Business	# of Loans		Disbursed
Agriculture, Forestry, Fishing & Hunting	13	$	4,606,854
Utilities	2		1,768,077
Construction	6		961,361
Manufacturing	4		91,437
Retail Trade	13		4,517,134
Transportation & Warehousing	3		212,000
Real Estate - Rental & Leasing	32		11,158,199
Administrative, Support, Waste Management	1		18,700
Education Services	1		2,000
Health Care & Social Assistance	3		4,519,706
Arts, Entertainment & Recreation	5		788,595
Accomodation & Food Services	25		11,252,875
Other Services	10		1,406,741
TOTAL	**118**		**41,303,679**

COMMERCIAL LOANS BY SIZE

Size	# of Loans		Disbursed
Less than $25,000	21	$	196,464
$25,000 to $99,999	16		1,096,885
$100,000 to $499,999	46		10,946,176
Over $500,000	35		29,064,154
TOTAL	**118**	**$**	**41,303,679**

2011 COMMUNITY INVOLVEMENT PROGRAM

Supporting the well-being of the communities we serve is a guiding principle at Kawartha Credit Union. We strive to remain a vital contributor through donations and sponsorships, and by our employees lending their time and talents to a variety of causes. We help to sustain important initiatives in the areas of healthcare, youth and education, community development, and the environment. In addition, we assist global concerns like Helping Haiti, and crisis relief efforts in our own backyards - such as the tornado in Goderich.

In 2011, we invested $140,000 (2.25% of our net income) to causes that matter most to our members in the regions that encompass our 19 branches. Kawartha Credit Union also distributes funds and gifts-in-kind throughout the year to causes that affect the most positive community advantage.

Our dedicated employees make important contributions to a number of organizations, campaigns and events. They build solid relationships with our community partners, and this year they participated in over 50 initiatives above and beyond those we support through our corporate Community Involvement Program.

The following initiatives were funded by our Community Involvement Program during the 2011 fiscal year:

COMMUNITY SUPPORT AND DEVELOPMENT

From shelters to community centres, our contributions help to strengthen the infrastructures that support sustainability and independence.

- Peterborough YMCA
- Peterborough & Victoria County YWCA/Crossroads Shelter
- Maggie's Resource Centre (Bancroft)
- Victoria County Womens' Resources Services
- Northumberland Services For Women (Transitional Housing)
- Womens' Own Resource Centre – Rural Outreach (South River)
- Esprit Place Family Resource Centre–Transitional Support (Parry Sound)
- Peterborough AIDS Resource Network
- Kawartha Lakes Food Source
- Kawartha Food Share
- Homegrown Homes
- Chrysalis Womens' Shelter (Huntsville)
- Burk's Falls Community Centre
- North Hastings Children's Services
- Community Counselling and Resource Centre

YOUTH AND EDUCATION

Literacy and learning improve quality of life, enhance prosperity and encourage the development of a skilled and well-educated workforce.

- Risk Watch
- Learning Disabilities Association
- Food For Kids Peterborough
- City of Kawartha Lakes "Food For Kids"
- Kawartha Haliburton Childrens' Foundation
- City of Kawartha Lakes Boys and Girls Club
- Food For Learning, Hastings/Prince Edward
- Northumberland "Food For Thought"
- Junior Achievement
- Festival of the Sound (Childrens' Music Scores Program)
- Bracebridge Community Theatre Campaign
- The Rene M. Caisse Memorial Theatre Campaign
- Academy Theatre Foundation – Childrens' Workshops
- 4th Line Theatre – Youth Workshops
- Fleming College Bursary
- Trent University Bursary
- Loyalist College Bursary (Bancroft Campus)
- Community Counseling and Resource Centre
- Five Counties Childrens' Centre
- Childrens' Foundation of Muskoka
- Quinte Childrens' Foundation – Playing for Keeps

ENVIRONMENT

Educating children about environmental sustainability enables them to take an active and knowledgeable role in protecting and preserving their future.

- Peterborough Childrens' Water Festival
- Haliburton/Muskoka Water Festival
- Adventures in Green Industry
- Camp Kawartha Environment Centre


kawartha CREDIT UNION

Representing Kawartha Credit Union's 2011 Community Involvement Program, Crystal Dayman V.P. Marketing & Corporate Communications, presents a $1,500 cheque to John McNutt, Regional Manager of the Kawartha Lakeland Region Junior Achievement program.

Kawartha Credit Union Makes a $1,500 Donation to Junior Achievement

Through its Community Involvement Program, Kawartha Credit Union strives to support education initiatives with a $1,500 donation to Kawartha Lakeland Region Junior Achievement program.

"Junior Achievement of Kawartha Lakeland Muskoka region is very pleased to receive an increase in financial commitment for the school year 2010-2011 from Kawartha Credit Union. There has been a steady increase in KCU involvement not only with funds but with volunteers to deliver the programs in the schools for the past three years. The extra funds will help to sponsor at least one more classroom and expose students to entrepreneurship and business as a career choice. Thanks to the staff and members of Kawartha Credit Union" states John McNutt, Junior Achievement Regional Manager for Kawartha Lakeland Region.

www.kawarthacu.com

HEALTHCARE

Kawartha Credit Union strives to benefit the greatest number of people in the communities we serve by supporting health centres and broader health concerns.

- Peterborough Dragon Boat Festival - Platinum Sponsor
- Parry Sound Cardiac Biosphere "Do It For Life" Walk, Run, Pole (Naming 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)
- Kinmount District Health Services
- West Parry Sound Health Centre
- Hospice North Hastings
- Hospice Peterborough

Kawartha Food Share: *Kawartha CEO Rob Wellstood presents a cheque to Warehouse Manager John Alleyne. Employees volunteer to sort food several times a year at Kawartha Food Share.*

Habitat For Humanity: *Mike Sullivan (Investment Specialist), Chemong Road Branch), Nicole Wickett (Receptionist, Monaghan Road Branch), Ryan Crowley (Branch Manager, Keene) and Al Mackay (Branch Manager, Lansdowne Place) offer a helping hand at a Habitat For Humanity building site.*

Biosphere Run: *Parry Sound Branch Manager Debbie McMurray (left) and Member Service Representative Angela Jeffery (right) join CEO Rob Wellstood (centre) at the Parry Sound Biosphere "Do It For Life" Walk, Run, Pole. Kawartha is a naming sponsor of the event.*

Dragon Boat Festival: *Kawartha Credit Union is the Platinum Sponsor of the event, and our employees participate in the races.*

Northumberland Hills Hospital: *Cobourg Branch Manager Dana Farrell (centre) presents a $3500 cheque to Ward Clerk Kathleen McDonald (left) and Registered Nurse Lorelei Kenny of Northumberland Hills Hospital Foundation. Kawartha's total donation to the hospital to date is $30,800.*

Ross Memorial Hospital: *John Fox, Chair of the Ross Memorial Hospital Foundation's "Imagine the Future" campaign, accepts a donation from Lindsay Branch Manager, Karen Munro. From left to right: Tasha Bonnar, Carol Davis, John Fox, Karen Munro, Rose Joudrie, Erin Coons (Executive Director, Ross Memorial Hospital Foundation), and Dawn Coombs.*

INDEPENDENT AUDITORS' REPORT

To the Members of Kawartha Credit Union Limited

We have audited the accompanying financial statements of Kawartha Credit Union Limited, which comprise the balance sheet as at September 30, 2011, and the statements of income, cash flows, members' equity and comprehensive income for the year then ended, along with a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Credit Union as at September 30, 2011 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

BDO Canada LLP

Chartered Accountants, Licensed Public Accountants

Peterborough, Ontario
November 2, 2011

REPORT FROM THE AUDIT COMMITTEE

The Audit Committee's function is to assist the Board of Directors fulfill its oversight responsibilities. It does this 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 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 2011 fiscal year to complete its responsibilities. Key activities included:

- Review the financial statements and 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 internal audit activities.

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,

Harvey Spry

Harvey Spry, Committee Chair
Committee: Carl Silvestri, Robert George, Bob Lake

BALANCE SHEET

At September 30

	2011	2010
Assets		
Cash resources (Note 1b)	$ 16,810,816	$ 18,570,299
Liquidity deposits	40,771,291	45,939,417
Loans to members (Note 3a)	615,900,979	585,792,750
Investments (Note 4)	6,610,793	6,009,429
Other assets	6,958,547	4,407,409
Capital assets (Note 5)	4,740,386	4,938,471
Derivative financial instruments (Note 15)	1,693,927	1,007,432
	$ 693,486,739	**$ 666,665,207**
Liabilities		
Term loans (Note 8a)	$ 25,000,000	$ 53,000,000
Members' deposits (Note 6a)	604,912,196	557,834,528
Accounts payable and accrued liabilities	5,247,349	4,458,405
Employee future benefits (Note 7)	4,088,709	3,576,323
Derivative financial instruments (Note 15)	2,055,338	1,165,568
	641,303,592	**620,034,824**
Members' Equity		
Class A Investment shares (Note 12)	12,494,685	12,494,685
Class B Affinity shares (Note 12)	5,746,179	3,757,239
Membership shares (Note 12)	865,808	844,781
Contributed surplus	230,243	209,533
Retained earnings	33,384,083	29,330,595
Accumulated other comprehensive income	(537,851)	(6,450)
	52,183,147	46,630,383
	$ 693,486,739	**$ 666,665,207**

Approved by the Board:

Ken Stickle

Director

Director

The accompanying notes are an integral part of these financial statements

STATEMENT OF INCOME

For the year ended September 30

	2011	2010
Financial Revenue		
Interest on loans to members (Note 3c)	$ 32,249,464	$ 30,850,765
Investment income	786,616	880,561
	33,036,080	31,731,326
Financial Expense		
Interest on deposits (Note 6b)	10,726,171	10,546,782
Interest on borrowings	537,885	463,826
	11,264,056	11,010,608
Financial Margin	21,772,024	20,720,718
Other Income	5,262,567	4,609,384
	27,034,591	25,330,102
Operating Expenses		
Salaries and employee benefits	11,003,102	9,797,605
Loan loss expense (Note 3d)	767,458	708,065
Occupancy	2,066,762	1,982,228
Banking costs	741,453	585,879
Other expenses (Note 11)	2,427,589	2,178,391
Data costs	1,144,750	1,070,676
Deposit insurance	462,228	440,364
Promotion	1,207,214	1,148,716
Directors' expenses	135,535	124,263
	19,956,091	18,036,187
Operating Income	7,078,500	7,293,915
Other Items		
Increase in fair value of investments	540,734	-
Income before income taxes	7,619,234	7,293,915
Income tax expense (Note 19)	1,397,000	1,856,000
Net Income	**$ 6,222,234**	**$ 5,437,915**

The accompanying notes are an integral part of these financial statements

STATEMENT OF CASH FLOWS

For the year ended September 30

	2011	2010
Cash Provided by Operations (Note 13)		
Net income	$ 6,222,234	$ 5,437,915
Adjustments to cash basis of accounting		
Amortization of capital assets	861,154	927,535
Changes in other assets	(2,551,138)	(150,136)
Changes in fair value of derivative financial instruments	(328,129)	87,792
Changes in accounts payable	788,944	2,582,478
Change in employee future benefits	512,386	306,237
Changes in allowance for loan losses	201,263	(88,516)
Net mortgage securitization premium	(203,784)	(186,834)
Increase in fair value of investments	(540,734)	-
	4,962,196	8,916,471
Cash Provided by (Advanced to) Members		
Increase in members' deposits	47,077,670	31,565,505
Increase in shares	2,009,967	967,755
Dividends paid to members net of tax savings	(758,183)	(881,661)
Class B Affinity share issuance net of tax savings	(1,410,563)	(851,644)
Increase in contributed surplus	20,710	28,065
(Increase) decrease in loans to members	(64,734,241)	(78,908,749)
	(17,794,640)	(48,080,729)
Financing Activities		
Changes in liquidity deposits	5,168,126	(6,126,638)
Term loans advanced (repaid)	(28,000,000)	24,000,000
Proceeds of mortgage securitization	34,628,533	21,011,228
	11,796,659	38,884,590
Investment Activities		
Purchases of capital assets	(663,069)	(499,231)
(Increase) decrease in investments	(60,629)	59,385
	(723,698)	(439,846)
Increase (Decrease) in Cash Resources During the Year	(1,759,483)	(719,514)
Cash Resources - Beginning of the Year	18,570,299	19,289,813
Cash Resources - End of the Year	**$ 16,810,816**	**$ 18,570,299**

The accompanying notes are an integral part of these financial statements

STATEMENT OF MEMBERS' EQUITY

For the year ended September 30

	2011	2010
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	3,757,239	2,797,335
Net share issuance	2,009,650	987,969
Shares forfeited	(20,710)	(28,065)
Ending balance	5,746,179	3,757,239
Membership Shares		
Opening balance	844,781	836,930
Net change during the year	21,027	7,851
Ending balance	865,808	844,781
Contributed Surplus		
Opening balance	209,533	181,468
Net change during the year	20,710	28,065
Ending balance	230,243	209,533
Retained Earnings		
Opening balance	29,330,595	25,625,985
Add: net income	6,222,234	5,437,915
	35,552,829	31,063,900
Less: Class B Affinity share issuance	(2,070,563)	(1,019,644)
Related tax savings	660,000	168,000
Less: Dividends paid to members	(1,112,183)	(1,055,661)
Related tax savings	354,000	174,000
Ending balance	33,384,083	29,330,595
Accumulated Other Comprehensive Income		
Opening balance	(6,450)	(18,814)
Other comprehensive income (loss)	(531,401)	12,364
Ending balance	(537,851)	(6,450)
Total Equity	**$ 52,183,147**	**$ 46,630,383**

STATEMENT OF COMPREHENSIVE INCOME

For the year ended September 30

	2011	2010
Net Income (Page 12)	$ 6,222,234	$ 5,437,915
Other Comprehensive Income		
Gains (losses) on financial derivatives designated as cash flow hedges net of tax effect	(531,400)	12,364
Comprehensive Income	**$ 5,690,834**	**$ 5,450,279**

The accompanying notes are an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS At September 30, 2011

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 (Central).

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 or are government backed. Carrying value of investments approximates market value. Investments mature within two years and provide an average yield of 1.56%.

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 Canadian 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 recognized 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 $429,434 (2010 - $402,285).

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 benefit 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, 2010.

g) Mortgage Securitization
The Credit Union occasionally securitizes mortgages through Central 1 Credit Union Limited or Concentra Financial. Securitizations of mortgages 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. The principal estimates used in the preparation of these financial statements are the determination of the liability for post-retirement benefits, the non-specific allowance for impaired loans, the estimated useful life of capital assets, future tax assets and liabilities and the fair value of financial instruments. 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 for the period. Under Section 3855 of the Canadian Institute of Chartered Accountants accounting standards, 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 its cash resources, securitization assets, accounts payable, derivative financial instruments and the investment in CUCO Cooperative Association Class B investment shares 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 unless it has been determined that an other than temporary decline in fair value exists. Any other than temporary declines in value are reported as a charge to income. With the exception of the aforementioned investment classified as held for trading, Kawartha Credit Union has classified its 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 its 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 its loans to members as loans and receivables and its 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 15 to the financial statements for the year ending September 30, 2011 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 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:

a) International Financial Reporting Standards

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

3. LOANS TO MEMBERS

a) Summary

	2011	2010
Personal loans	$ 139,602,993	$ 129,860,867
Residential mortgages	288,460,087	283,439,460
Commercial loans	190,174,509	174,604,624
	618,237,589	587,904,951
Accrued interest receivable	979,264	1,002,411
	619,216,853	588,907,362
Allowance for impaired loans	(3,315,874)	(3,114,612)
Net loans to members	**$ 615,900,979**	**$ 585,792,750**

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, 2011 is 4.00% and fluctuates with the market, subject to management's discretion. 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:

	2011	2010
Personal loans	$ 139,513,000	$ 129,325,000
Residential mortgages	302,183,000	300,805,000
Commercial loans	183,016,000	168,615,000
	$ 624,712,000	**$ 598,745,000**

The key economic assumptions used in measuring the fair value of member loans at September 30, 2011 were as follows:

	Personal Loans	Residential Mortgages	Commercial Loans
Prepayment rate	10%	6%	5%
Weighted-average term to maturity	2.11years	2.49years	1.81years
Market rate	7.00%	3.60%	6.00%

c) Interest Income

	2011	2010
Personal loans	$ 7,909,897	$ 7,546,656
Residential mortgages	13,282,565	13,193,247
Commercial loans	11,057,002	10,110,862
	$ 32,249,464	**$ 30,850,765**

Personal loans are comprised of term loans, which account for 46% of the portfolio, and lines of credit which account for the remaining 54% of the portfolio. Repayment terms vary with the term length and loan type. Security may include collateral mortgages on real property, 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, 2011:

	Principal	Yield
Variable rate loans	$ 199,022,429	5.75%
Fixed rate loans with maturities within one year	72,407,113	5.43%
Fixed rate loans with maturities beyond one year	346,808,047	5.38%
	$ 618,237,589	

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

	Personal Loans	Residential Mortgages	Commercial Loans	Total
2011				
Opening	$ 1,712,442	$ 315,268	$ 1,086,902	$ 3,114,612
Recoveries	71,841	-	-	71,841
Loan loss expense	492,049	64,502	210,907	767,458
	2,276,332	379,770	1,297,809	3,953,911
Write-offs	(577,185)	(4,730)	(56,122)	(638,037)
Ending	**$ 1,699,147**	**$ 375,040**	**$ 1,241,687**	**$ 3,315,874**
Principal balance of impaired loans	**$ 2,411,834**	**$ 4,940,206**	**$ 2,344,532**	**$ 9,696,572**
2010				
Opening	$ 2,024,750	$ 273,576	$ 904,802	$ 3,203,128
Recoveries	44,780	-	-	44,780
Loan loss expense	429,366	86,707	191,992	708,065
	2,498,896	360,283	1,096,794	3,955,973
Write-offs	(786,454)	(45,015)	(9,892)	(841,361)
Ending	**$ 1,712,442**	**$ 315,268**	**$ 1,086,902**	**$ 3,114,612**
Principal balance of impaired loans	**$ 1,946,207**	**$ 2,986,742**	**$ 1,545,802**	**$ 6,478,751**

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 $1,399,700 (2010 – $1,499,700). At September 30, 2011, there were no formally restructured loans outstanding (2010 – none).

4. INVESTMENTS

	2011	2010
Central 1 Credit Union Limited, Membership	$ 4,081,852	$ 3,896,277
CUCO Cooperative Association		
- Class A membership shares	15,759	14,549
- Class B investment shares	2,495,625	-
ABCP 2008 Limited Partnership	-	2,081,046
Co-operators General Insurance, Class A Series A	11,250	11,250
Credential Securities Inc., Debenture	5,000	5,000
Concentra Financial	1,307	1,307
	$ 6,610,793	**$ 6,009,429**

The membership share requirement in Central 1 Credit Union (Central) is determined based on the percentage of the Credit Union's assets to the total member credit unions' assets. Central has a policy designed to ensure its capital is sufficient to support its operations and to comply with regulatory requirements. Each year Central rebalances the membership shareholdings based on the proportion of each credit union's assets to the total assets of all Central's member credit unions as reported in their most recent audited financial statements. Dividends on these shares are at the discretion of the Board of Directors of Central. The Credit Union received dividends amounting to 2% of the membership shares in 2011 (2010 - 2%). The fair values of the shares in Central, the Co-operators and Credential Securities are not readily determinable because of the lack of a resale market for them and accordingly, they are carried at cost. Management believes that there has been no impairment in any of these investments.

On August 17, 2011 Credit Union Central of Ontario Limited (CUCO) discontinued as a regulated financial institution and continued as a co-operative known as CUCO Cooperative Association (CUCO Co-op). On August 31, 2011 CUCO Co-op purchased the investment portfolio of long term notes from ABCP LP in exchange for Class B investment shares which were distributed to the ABCP LP unit holders. The Credit Union received 908,029,893 Class B investment shares. This combination of steps restructured the Credit Union's holding in the assets, created a new investment, and unlocked a potential tax shelter on any future gains in the value. On October 24, 2011 the Board of ABCP LP approved a resolution to dissolve the limited partnership as it had ceased operations and disposed of all assets.

As the investment in CUCO Co-op Class B investment shares represents a new investment, the Credit Union has elected to classify it as "Held for Trading" requiring the investment to be carried at fair value and all gains and losses in value to be recorded in income. At September 30, 2011 CUCO Co-op provided an estimate of fair value of the investment of $2,495,625, an increase in value of $539,525.

Uncertainty remains with respect to the timing and amount of future cash flows on the notes held by CUCO Co-op that could give rise to a material change in the value of the holdings and thus the value of the Class B investment shares. The Credit Union performed a sensitivity analysis on the fair value assumptions and based on a 10% favourable and a 10% unfavourable change in the valuation, the Credit Union determined that the fair value could increase or decrease by $36,000.

CUCO Co-op membership shares were written up by $1,210.

5. CAPITAL ASSETS

	2011 Cost	2011 Accumulated Amortization	2010 Cost	2010 Accumulated Amortization
Land and parking lot	$ 1,108,800	$ 1,354	$ 1,156,962	$ 49,516
Building	4,028,061	2,465,214	3,863,992	2,309,011
Equipment	5,147,057	4,034,601	6,665,791	5,522,015
Leasehold improvements	2,122,075	1,177,449	2,329,941	1,226,296
Member files	1,368,860	1,355,849	1,368,860	1,340,237
	$13,774,853	**$ 9,034,467**	**$15,385,546**	**$10,447,075**
Net book value		**$ 4,740,386**		**$ 4,938,471**
Amortization expense		**$ 861,154**		**$ 927,535**

6. MEMBERS' DEPOSITS

a)

	2011	2010
Chequing accounts	$ 122,614,434	$ 116,759,863
Demand savings accounts	51,291,776	46,740,018
Term deposits	269,339,922	252,298,594
Registered savings plans	105,337,270	99,624,462
Registered retirement income funds	24,160,851	21,124,849
Tax-free savings accounts	24,119,203	14,393,292
Accrued interest on member deposits	8,048,740	6,893,450
	$ 604,912,196	**$ 557,834,528**

b) Interest on Deposits

	2011	2010
Chequing accounts	$ 404,913	$ 391,469
Demand savings accounts	269,747	251,577
Term deposits	5,830,035	5,905,615
Registered savings plans	3,033,503	3,043,625
Registered retirement income funds	711,547	698,050
Tax-free savings accounts	476,426	256,446
	$ 10,726,171	**$ 10,546,782**

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 57% of the portfolio (2010 - 67%).

Registered savings plans consist of fixed rate deposits which account for 98% (2010 - 98%) of the portfolio and variable rate deposits which comprise the remaining 2% (2010 - 2%) of the portfolio. Deposits which are callable by the depositor account for 51% of the portfolio (2010 - 58%), with the remaining 49% (2010 - 42%) being fixed for terms up to five years. Tax-free savings accounts and 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, 2011:

	Principal	Yield
Variable rate deposits due on demand	$ 176,725,456	0.43%
Fixed rate deposits with maturities within one year	213,702,505	2.14%
Fixed rate deposits with maturities beyond one year	206,435,495	3.24%
	$ 596,863,456	

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:

	2011	2010
Chequing and demand savings accounts	$ 176,725,000	$ 163,363,000
Term deposits	272,373,000	255,882,000
Registered plans	155,998,000	134,340,000
	$ 605,096,000	**$ 553,585,000**

The key economic assumptions used in measuring the fair value of member deposits at September 30, 2011 were as follows:

	Non Registered Deposits	Registered Deposits
Weighted-average term to maturity	1.39years	1.46years
Market rate	2.54%	2.94%

7. 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, 2011 of $4,054,776 (2010 - $2,778,120) and the net periodic benefit cost for the year ending September 30, 2011 was determined by actuarial valuation using a discount rate of 4.75% (2010 - 5.5%).

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

	2011	2010
Accrued benefit obligation		
Balance at the beginning of the period	$ 2,778,120	$ 2,600,704
Service cost for the period	108,694	64,917
Interest cost for the period	184,791	144,623
Benefits cost for the period	(40,976)	(32,124)
Loss on A.B.O. recognized in the period	1,024,147	-
Projected accrued benefit obligation at the end of the period as determined by actuarial valuation	4,054,776	2,778,120
Unamortized transitional obligation	-	(236,192)
Unamortized past service cost	(118,425)	(142,110)
Unamortized actuarial gain	152,358	1,176,505
Accrued liability	**$ 4,088,709**	**$ 3,576,323**
Components of net periodic benefit cost		
Service cost for the period	$ 108,694	$ 64,917
Interest cost for the period	184,791	144,623
Amortization of transitional obligation	236,192	258,104
Past service cost	23,685	23,685
Amortization of actuarial gain	-	(152,938)
Net periodic benefit cost	**$ 553,362**	**$ 338,391**

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

General Inflation (CPI rate) 2.00%
Interest (discount) rate 4.75%

Medical costs were assumed to increase at the CPI rate plus a further increase of 6.0% in 2011, then graded down by 0.37% each year until reaching the CPI rate plus 3.0% in 2020 and thereafter.

Dental costs were assumed to increase at the CPI rate plus 3.0% in 2011 and thereafter.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects for 2011:

	Increase	Decrease
Total of service and interest cost	$ 72,000	$ (55,000)
Accrued benefit obligation	$ 778,000	$ (624,000)

8. COMMITMENTS

a) Credit Facilities
The Credit Union has authorized line of credit and term loan facilities with Central 1 Credit Union Limited totalling $50,570,000. As of September 30, 2011 the Credit Union had unused credit facilities totalling $25,570,000. The authorized lines of credit bear interest at 1.46%. 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, 2011, the Credit Union is committed to advance approximately $2,158,537 on mortgage loans and $10,873,080 on commercial loans. In addition, lines of credit which had been approved but not used at year-end totalled approximately $64,707,933.

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: 2012 - $1,192,966; 2013 - $1,148,129; 2014 - $1,106,223, 2015 - $738,984; 2016 – $581,654 and $4,767,956 in the aggregate.

d) Contingencies
The nature of the Credit Union's activities are such that there may be litigation pending or in progress at any time. There were no claims at September 30, 2011.

9. REGULATORY REPORTING

a) 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 4.00% of total assets and 8.0% of risk-weighted assets. At September 30, 2011, the Credit Union is in compliance with the Act and regulation.

	2011	2010
Total regulatory capital is composed of Tier 1 and Tier 2 capital as follows:		
Tier 1 Capital, otherwise known as core capital, is the highest quality. It is comprised of the following:		
Class A Investment Shares	$ 12,494,685	$ 12,494,685
Less Redeemable Portion of Class A Shares	(1,267,000)	(769,000)
Class B Affinity Shares	5,746,179	3,757,239
Membership Shares	865,808	844,781
Contributed Surplus	230,243	209,533
Retained Earnings	33,384,083	29,330,595
Total Tier 1 Capital	51,453,998	45,867,833
Tier 2 Capital, otherwise known as supplementary capital, contributes to the overall strength of a financial institution as a going concern, but is of a lesser quality than Tier 1 capital relative to both permanence and freedom from charges. It is comprised of the following:		
Redeemable Portion of Class A Shares	1,267,000	769,000
General Provisions	1,399,700	1,499,700
Other Comprehensive Income	(537,851)	(6,450)
Total Tier 2 Capital	2,128,849	2,262,250
Tier 1 and Tier 2 Capital	53,582,847	48,130,083
Future Income Taxes	(1,480,813)	(1,145,813)
Total Regulatory Capital	**$ 52,102,034**	**$ 46,984,270**

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	360,815,584	340,925,747
Market Risk	46,875	892,500
Operational Risk	42,154,241	38,426,678
	$ 403,016,700	**$ 380,244,925**

The applicable capital ratios are as follows:

Tier 1 Capital to Risk Adjusted Assets	12.77%	12.06%
Total Regulatory Capital to Risk Adjusted Assets	12.93%	12.36%
Total Regulatory Capital to Total Assets	7.51%	7.05%

b) Remuneration of Officers and Employees
The Credit Unions and Caisses Populaires Act, 1994, requires credit unions to disclose remuneration paid during the year to the officers and employees of a credit union whose total remuneration for the year exceeded $150,000. If there are more than five officers and employees of a credit union whose total remuneration for the year was over $150,000, the five officers and employees with the highest total remuneration for the year are disclosed. The table below provides this information for the 2010 calendar year:

	Total Salary Received	Monetary Value of Benefits Received
Robert Wellstood, CEO	$ 216,744	$ 11,225
Julian Sellers, CFO	$ 151,170	$ 10,525

c) Other Statutory Information
Pursuant to the requirements of the Credit Unions and Caisses Populaires Act, 1994, the following information is provided:

	2011	2010
Director remuneration in the year	$ 110,450	$ 100,200
Deposit insurance premium paid in the year	$ 462,228	$ 440,364

10. 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 4 loans advanced to restricted parties as defined by policy during the year, and there are 34 loans outstanding to such parties with an aggregate value of $1,666,190 at September 30, 2011.

11. OTHER EXPENSES

	2011	2010
Other supplies and postage	$ 473,052	$ 438,650
Equipment costs	335,695	314,675
Central dues & regulatory assessments	117,840	124,740
Amortization of member files	15,612	15,612
Savings and loan life insurance	59,346	105,195
Education and staff development	608,761	509,209
Bonding insurance	238,300	194,711
Professional services	255,722	219,626
Collection costs	81,848	70,352
Telephone	128,042	120,528
Miscellaneous	110,774	61,662
Central annual meeting	2,597	3,431
	$ 2,427,589	**$ 2,178,391**

12. 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, subject to a maximum of 10% of the shares outstanding at the end of the previous fiscal year.

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 March 15, 2011 the Credit Union issued 2,024,990 Class B Series 2 Affinity Shares.

13. CASH FLOW STATEMENT

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

	2011	2010
Cash paid for interest	$ 9,570,881	$ 12,437,411
Cash paid for income taxes	$ 1,307,491	$ 553,219
Cash received for income taxes	$ -	$ 17,035

14. 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.

15. 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 tables below provide an overview of the Credit Union's derivative portfolio.

2011

	Maturities of Derivatives (Notional Amounts)			Fair Value	
	Within 1 year	1 to 5 years	Total	Asset	Liability
Interest rate swaps:					
Receive fixed	$ 80,000,000	$ 50,000,000	$ 130,000,000	$ 1,533,970	$ -
Pay fixed	20,000,000	42,050,920	62,050,920	-	1,895,380
Index-linked options	-	4,353,626	4,353,626	159,957	159,957
Total	**$100,000,000**	**$ 96,404,546**	**$196,404,546**	**$ 1,693,927**	**$ 2,055,337**

2010

	Maturities of Derivatives (Notional Amounts)			Fair Value	
	Within 1 year	1 to 5 years	Total	Asset	Liability
Interest rate swaps:					
Receive fixed	$ 25,000,000	$ 80,000,000	$ 105,000,000	$ 754,930	$ -
Pay fixed	10,000,000	56,218,464	66,218,464	-	913,066
Index-linked options	-	3,347,742	3,347,742	252,502	252,502
Total	**$ 35,000,000**	**$139,566,206**	**$174,566,206**	**$ 1,007,432**	**$ 1,165,568**

Notional amounts are the contract amounts used to calculate the cash flows to be exchanged. They are a common measure of the volume of outstanding transactions, but do not represent credit or market risk exposure. Notional amounts are not exchanged.

The Credit Union has credit risk which arises from the possibility that a counterparty to a derivative contract could default on their obligation to the Credit Union. However, credit risk associated with derivative contracts is normally a small fraction of the notional principal amount of the contract. Derivative contracts expose the Credit Union to loss where there is a favourable change in market rates from the Credit Union's perspective and the counterparty fails to perform. The Credit Union only enters into derivative contracts with a counterparty that the Credit Union has determined to be creditworthy.

Interest Rate Swaps

As part of its interest rate risk management process, the Credit Union utilizes interest rate contracts in the form of interest rate swaps to maintain its interest rate exposure within the preset limits defined by the Board approved policy.

As at September 30, 2011, the Credit Union had entered into 5 receive fixed interest rate swaps, 1 of which is delayed start, with a total notional amount of $130,000,000 and maturing between October 2011 and January 2013. Under the terms of these agreements, the counterparty to the swap is obligated to pay the Credit Union a fixed rate and the Credit Union is obligated to pay the counterparty a variable rate, with both payments based upon the notional amount of the underlying swap. The variable rate paid by the Credit Union is equivalent to the one month bankers' acceptance rate and is repriced monthly. The Credit Union is currently receiving or will receive fixed rates on these swaps ranging from 2.125% to 2.480% and is paying variable rates as at September 30, 2011 of 1.197%.

As at September 30, 2011, the Credit Union had 8 pay fixed interest rate swaps outstanding with a notional amount of $62,050,920 and maturing from January 2012 to June 2016. Under the terms of these agreements, the counterparty to the swap is obligated to pay the Credit Union a variable rate and the Credit Union is obligated to pay the counterparty a fixed rate, with both payments based upon the notional amount of the underlying swap. The variable rate received by the Credit Union is equivalent to the one month bankers' acceptance rate and is repriced monthly. The Credit Union is currently paying a fixed rate on these swaps ranging from 1.34% to 3.03% and is receiving a variable rate as at September 30, 2011 ranging from 1.197% to 1.279%.

Equity Index-Linked Deposits
The Credit Union has $4,353,626 (2010 - $3,347,742) of equity index-linked deposit products outstanding to its Members. These term deposits have maturities of 3 and 5 years and pay interest to depositors, at the end of the term, based on the performance of various market indices. The Credit Union has purchased equity index-linked option agreements with Central 1 to offset the exposure to the indices associated with these products. The Credit Union pays a fixed amount based on the notional amount at the inception of the equity index-linked purchase option contract. At the end of the term the Credit Union receives from Central 1 payments equal to the amount that will be paid to the depositors based on the performance of the respective indices.

The purpose of these agreements is to provide an economic hedge against market fluctuations. These agreements have fair values that vary based on the particular contract and changes in equity indices. Although hedge accounting is not applied, these agreements continue to be effective as economic hedges.

16. NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS

The Credit Union is 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 the Credit Union manages its 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
The Credit Union's credit risk management principals are guided by its 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.

The Credit Union's credit risk policies set out the minimum requirements for management of credit risk in a variety of transactional and portfolio management contexts. The Credit Union's 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, 2011 was as follows:

	2011
Loans that are not past due	$ 602,948,239
Loans that are past due	
under 30 days	5,408,012
30 to 89 days	5,381,815
90 -179 days	1,846,950
180 - 365 days	971,249
over 365 days	1,681,324
	$ 618,237,589

At a minimum all loans that are over 90 days past due are considered impaired. There are 302 loans with a combined principal of $9,696,572 considered to be impaired. The security shortfall on these loans totalled $1,784,201.

The Credit Union's 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. The Credit Union is exposed to market risk in our asset/liability management activities. The level of market risk to which the Credit Union is 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 the Credit Union to market risk, of which interest rate risk is the largest component. The Credit Union's goal is to manage the interest rate risk within established limits. The Credit Union manages both long term interest rate risk (equity risk) and short term interest rate risk (earnings risk). The Credit Union continually monitors the effectiveness of its interest rate mitigation activity.

Risk Measurement
The Credit Union's risk position is measured monthly. Measurement of risk is based on rates charged to clients as well as funds transfer pricing rates.

Objectives, Policies, and Processes
Management is responsible for managing the Credit Union's 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	$ 215,034	$ 52,672	$ 162,362
< 6 months	78,093	115,930	(37,837)
1 year	64,180	131,423	(67,243)
2 years	99,971	142,219	(42,248)
3 years	95,381	91,871	3,510
4 years	58,806	80,854	(22,048)
5 years	63,403	57,443	5,960
> 5 years	-	-	-
	674,868	672,412	2,456
Non-interest sensitive items	18,619	21,075	(2,456)
	$ 693,487	**$ 693,487**	**$ -**

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. An adjustment has been made for repayments that may occur prior to maturity based on recent member activity.

As at September 30, 2011, the weighted average rate for interest-bearing assets is 5.23% and for interest-bearing liabilities is 1.99%.

Based on the Credit Union's interest rate positions at September 30, 2011 the following table shows the potential before tax impact of an increase or decrease in interest rates on the Credit Union's net income.

	2011	2010
100 bp increase	$ (25,000)	$ (457,000)
50 bp decrease	$ 172,000	$ 378,000

The interest rate risk policy has been approved by the board of directors and for the year ended September 30, 2011 the Credit Union was in compliance with the policy.

The Credit Union's overall market risk policies and procedures have not changed materially in the past year.

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

Risk Measurement
The assessment of the Credit Union's 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 clients and counterparties.

Objectives, Policies and Processes
The Credit Union's 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 its current and prospective financial commitments under normal and contemplated stress conditions.

The Credit Unions and Caisses Populaires Act, 1994 and Regulation 237/09 requires the Credit Union to establish and maintain prudent levels and forms of liquidity that are sufficient to meet its cash flow needs, including depositor withdrawals and all other obligations as they come due.

The Credit Union monitors and manages its liquidity position and considers regulatory, operational and any other applicable restrictions. The Board of Directors is responsible for oversight of its liquidity framework.

The table below summarizes the contractual maturities of the Credit Union's member deposits and existing loan commitments as at September 30, 2011:

	on demand	less than one year	one to five years
Member deposits (Note 6)	$ 176,725,457	$ 213,702,505	$ 206,435,495
Loan commitments (Note 8)	13,031,617	64,707,933	-
	$ 189,757,074	**$ 278,410,438**	**$ 206,435,495**

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

17. SUBSEQUENT EVENTS

On October 26, 2011, 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, 2011. The amount of the dividend will be $886,957, with a corresponding tax saving of $195,000.

On October 26, 2011, 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, 2011. The amount of the dividend will be $327,434, with a corresponding tax saving of $72,000.

On October 31, 2011, Kawartha Credit Union Limited and Unity Savings and Credit Union Limited signed a non-binding letter of intent to amalgamate the companies subject to satisfactory due diligence and required regulatory and membership approvals. Management has yet to determine the financial impact of the transaction.

18. MORTGAGE SECURITIZATIONS

During the year Kawartha Credit Union securitized residential mortgages of $37,897,859 (2010 - $20,910,998). 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, 2011 was $72,815,915 (2010 – $50,182,898)

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

	2011	2010
Net cash proceeds received	$ 34,628,533	$ 21,011,228
Premium	203,784	186,834

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

	2011	2010
Prepayment rate	8 - 17%	8%
Weighted-average term to maturity	4.34 - 4.68 years	4.64years
Expected annual credit losses	-	-

At year end the key economic assumptions and the sensitivity of the current fair value of residual cash flows of an adverse change in the prepayment rate assumption is shown below:

	2011	2010
Carrying value of retained interests	$ 1,305,102	$ 1,491,377
Weighted-average term to maturity	3.010 years	3.120 years
Prepayment rate assumption	8%	8%
Impact of a 10% prepayment	$ (52,832)	$ (65,989)
Impact of a 20% prepayment	$ (323,998)	$ (373,600)

The cash flows from securitized mortgages under administration are based on variable rates which are estimated using a swap rate curve. Because a swap rate is being used a sensitivity analysis on an adverse change is not practical to complete.

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.

19. 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:

	2011	2010
Employee future benefits	$ 899,500	$ 591,000
Allowance for impaired loans	350,800	397,000
Capital assets	183,500	117,000
Other	48,200	40,000
	$ 1,482,000	**$ 1,145,000**

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:

	2011	2010
Income before income taxes	$ 7,619,234	$ 7,293,915
Statutory income tax rate	28.75%	32.25%
Expected income tax expense	2,190,530	2,352,288
Increase(decrease) in taxes resulting from:		
Available credit union small business deduction	(713,241)	(844,809)
General tax reduction unavailable	325,454	309,737
Change in future income taxes	(335,000)	(39,000)
Non-deductible expenses and other reconciling items	(70,743)	77,784
Income tax expense	**$ 1,397,000**	**$ 1,856,000**

The income tax expense consists of the following:

	2011	2010
Current provision	$ 1,732,000	$ 1,895,000
Future provision	(335,000)	(39,000)
	$ 1,397,000	**$ 1,856,000**

KAWARTHA CREDIT UNION
STAFF RECOGNITION AWARDS

	2007	2008	2009	2010	2011
BRANCH AWARDS					
Highest Overall Growth %	Huntsville	Little Britain	Keene	Huntsville	Huntsville
Highest Overall Growth $	Monaghan	Monaghan	Monaghan	Huntsville	Huntsville
100% Club	Kinmount	*No Entry*	*No Entry*	*No Entry*	No Entry
Community Commitment Award		Emsdale	Bancroft	Cobourg	Administration Department
INDIVIDUAL AWARDS					
Manager of the Year	Dana Farrell	Connie White	Karen Woodman	Susan Wakeford	Karen Munro
Extra Mile Award	Janice Barber Francine Currie	Carol Davis Linden Gage Lana Koch	Diana Andrews Susie Lodge Bonnie Rickward	Stefanie Kubica Betty Dickson Arlene McKee	Paige Harris Amie Keech Jessica Harnum-Ross
Glen Davies Award	Steve Olmstead	Kristy Tremblett	Suzanne Shannon	Dan MacNamee	Deb Elacqua