



**Management's Discussion and Analysis
Consolidated Financial Statements**

For the year ended October 31, 2015

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SERVUS CREDIT UNION LTD.
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Servus Credit Union Ltd.'s (Servus or the credit union) 2015 annual report consists of Management's Discussion and Analysis and Consolidated Financial Statements for the year ended October 31, 2015, which detail our credit union's financial and operating results. This document is available upon request or online at servus.ca.

Note Regarding Forward-Looking Statements:

This annual report contains forward-looking statements about the operations, objectives and expected financial performance of Servus. These statements are subject to risks and uncertainties. Actual results may differ depending on a number of factors, including, but not limited to, legislative or regulatory changes, interest rates and general economic conditions in Alberta and Canada. These issues should be given careful consideration and readers should not place undue reliance on Servus's forward-looking statements.

Better Banking for Members

With roots that go back to 1938, Servus Credit Union has provided financial services to generations of Albertans. Over the years, we've grown to become Alberta's largest credit union and the first provincewide credit union in Canada. We're proud to provide personalized and exceptional service to our members, and we look forward to serving many more in the future.

Nearly 390,000 members are served by close to 2,400 hard-working and dedicated Servus employees from more than 100 locations in 60 communities across Alberta. Our offices in Red Deer, Lloydminster and Edmonton support the business and administrative needs of our members and employees.

Servus is a co-operative financial institution that is committed to:

- Member ownership
- Exceptional service
- Local decision-making
- Profit Share
- 100% deposit guarantee
- Community support

These principles serve as a guide for the work we do within the credit union and in our communities.

Our day-to-day operations are overseen by our Executive Leadership Team:

- Garth Warner, President & Chief Executive Officer
- Yves Auger, Chief Information Officer
- Dan Bruinooge, Chief People & Corporate Services Officer
- Ian Glassford, Chief Financial Officer
- Darcy Peelar, Chief Credit, Compliance & Operational Support Officer
- Gail Stepanik-Keber, Chief Brand & Corporate Social Responsibility Officer
- Caroline Ziober, Chief Operating Officer
- Taras Nohas, Vice President Strategy & Governance

Values, Vision, Mission

Our vision, mission and values tell the world who Servus is and what people can expect from us. They provide clear direction for our credit union, focus our efforts and guide our operations. The provincial, national and global economy may change, but we know where we're going and how we're getting there.

Our Vision

Servus Credit Union builds a better world — one member at a time.

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Our Mission

Servus Credit Union provides sound, advice-based financial products and services. We are here for our members through all stages of their lives. We help them achieve personal satisfaction, enjoy financial stability and a good quality of life, and we are committed to making a difference in the communities where they live and work.

Our Values

We have seven corporate values: community, fairness, integrity, investing in our people, life/work balance, member service and teamwork.

Helping in Our Communities

Servus has always been a strong advocate for investing in our communities. It's one of the principles that guides our business. In 2015, Servus contributed over \$2 million to a wide range of community organizations and initiatives across the province. This is on top of employee fundraising efforts and the time our employees spent volunteering.

Here are a few of the areas Servus supported this year:

- \$100,000 to Medicine Hat's new arena and event centre, the Canalta Centre
- \$138,000 for the Junior Achievement Dollars with Sense program that teaches junior high students how to make smart financial decisions
- \$20,000 to Sylvan Lake to help them rebuild their arena and curling rink
- \$30,000 in scholarships to 15 post-secondary students as part of our millennial program

We strengthened our relationship with United Way agencies in Alberta to improve people's financial literacy and address issues they face.

Servus gave members free access to community events and activities through our sponsorship of the Imax Theatre at the Telus World of Science — Edmonton, the Edmonton Ski Club and many other facilities and events.

Recognizing Our Credit Union

Servus and our employees were honoured to receive a number of awards this year for the difference we made for our members and our communities. We believe strongly in the work we do and appreciate the acknowledgement of our efforts. Our awards included:

- The 2015 Co-operative Innovation Award (from the Alberta Community & Co-operative Association) for engaging young leaders in the credit union movement
- The first ever Alberta Global Co-operator Award, which is the highest honour the Co-operative Development Foundation of Canada and the Canadian Co-operative Association jointly bestow on an organization
- Re-qualification as a member of the Platinum Club of Canada's 50 Best Managed Companies for the sixth year in a row
- Venture 250 recognition as one of Alberta's highest grossing companies

Servus is most proud that credit unions were first in Customer Service Excellence. Every year, Ipsos Reid asks Canadians about their banking experience, and for the eleventh year in a row, credit unions outperformed other Canadian financial institutions when it came to providing great service. For us, it's always about putting our members first.

Ipsos 2015 Best Banking Awards are based on ongoing quarterly Customer Service Index (CSI) survey results. The sample source for CSI is from the Ipsos Online Global Opinion Panel for Canada, using online data collection. Sample size for the total 2015 CSI program year ended August 2015 was 45,391 completed surveys yielding 65,991 financial institution ratings nationally. The sample is representative of the general household population based on Statistics Canada census data.

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2015: In Review

Market and Economic Environment

Fiscal year 2015 was a mix of surprises and contradictions for Servus and our financial results.

We knew interest rates would remain low, but it was the Bank of Canada's drop in rates that affected the credit union far more than the weak economy.

We recognize that our financial results reflect the talent and effort of Servus employees. We did not see the level of loan losses one might expect with the drop in the price of oil. Timing was also a factor since we anticipate that the economy will continue to slow in 2016 and we will see more challenges in our loan portfolio as lower energy prices affect our members.

Key Performance Drivers

Management has developed key metrics to measure the success of the credit union. These metrics form the balanced scorecard and allow the credit union to make decisions on how to best meet the needs of our members and maintain a long-term performance perspective.

Objective	Measure	2015 Target	2015 Result	2014 Result
Financial Performance				
Financial growth	Operating income (millions) ¹	\$118.3	\$121.7	\$120.2
Reduced dependency on interest-based income	Other income as a percentage of average assets ¹	0.577%	0.602%	0.589%
Leveraging assets profitably	Return on assets ¹	0.826%	0.870%	0.890%
Employee Experience				
High-level employee satisfaction	Employee engagement score as reported by employee survey	78%	77%	77%
Dedicated to life-long learning	Percentage of employees attending a learning program that is not regulatory	80%	62.26%	44.75% ³
Member Experience				
Servus members are advocates	Member Loyalty Index	74%	71.2%	47%
Servus members as advocates	Member satisfaction score as reported by member survey	77%	76.2%	79%
Business Processes				
Business process improvements for effectiveness and efficiency	Operating efficiency ratio ^{1,2}	70.795%	68.582%	68.624%
	Operating expenses as a percentage of average assets ¹	2.199%	2.167%	2.177%

¹ Results are before patronage, income taxes, employee incentives and extraordinary items.

² The operating efficiency ratio is a ratio of expenses to revenues. In essence, it measures how much the credit union spent to earn a dollar of revenue. A lower percentage reflects better results.

³ The Member Loyalty Index expanded in 2015 from only "Definitely would recommend" to "Probably would recommend."

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Our Performance This Year

A key focus for the credit union and our employees in 2015 was to lower our expenses. Along with our work to increase capital, reduced expenses helped us realize strong financial results during an unpredictable year.

Costs were aggressively reduced in areas ranging from employee benefits to Board of Director travel. Unlike the banks, Servus avoided employee layoffs and, instead, evaluated all open positions and filled them only if absolutely necessary.

It is at times like these that our co-operative values shine as a competitive advantage. Our employees, management and board of the credit union truly appreciate our members' support in finding more balanced long-term solutions.

This deliberate and thoughtful approach helped us lower our operating expenses by \$0.9 million, or 0.3%. It enabled us to increase our operating efficiency and to compete for more business, which ultimately benefits the organization and our members.

Financial Highlights

	2015	2014
Loan growth	\$ 234,863	\$ 724,304
Percent over prior year	1.88%	6.17%
Deposit growth	\$ (336,709)	\$ 698,667
Percent over prior year	(2.68%)	5.89%
Net income before patronage and taxes	\$ 129,499	\$ 117,108
Percent over prior year	10.58%	(4.45%)
Net income	\$ 77,622	\$ 68,513
Percent increase over prior year	13.30%	(6.45%)
Patronage	\$ 25,901	\$ 28,259
Share dividends	\$ 21,988	\$ 21,673
As a percentage of average assets		
Net interest income	2.52%	2.55%
Income before patronage allocation to members and income taxes	0.91%	0.86%
Net income	0.55%	0.50%
Provision for credit loss (percentage of average loans)	0.12%	0.10%

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Balance Sheet

Servus's loan growth of \$234.9 million was lower than we would have liked. There were fewer lending opportunities throughout the province and more low-rate lenders, which increased the competition for every loan. For the long-term sustainability of the credit union, we chose to focus on member loans in areas that were mutually beneficial for the member and Servus.

The low-rate environment affected our lending rate and our deposit balances as members actively looked for higher-rate opportunities from any financial institution.

Deposit balances fell over the year as the credit union reduced its use of larger, more volatile commercial member deposits. Many members moved their balances to our wealth services area as they sought alternative investment solutions. While those balances contribute to our overall financial health and show a high degree of member confidence, they do not contribute to our balances since they are managed through our partner, Credential Asset Management.

Throughout the year, the credit union's capital was built up so that Servus is ready to deal with further economic slowdown in the years to come.

	2015	2014	2015 Regulatory Requirement
Capital to assets	8.27%	7.58%	4%
Capital as a % of risk weighted assets	14.55%	13.24%	11.50%*

*The regulator expects that Servus will have internal policies for capital that are at least 2% above this level.

Income Statement

Many financial institutions in Canada struggled with the impact of low interest rates in 2015. Servus was able to maintain our level of profitability during the year by aggressively managing costs. However, this performance will be difficult to maintain unless interest rates increase. It is very likely that the credit union will see downward pressure in this area in 2016.

The amount the credit union set aside for loan losses increased \$3.1 million, or 24.4% during 2015, despite a lower delinquency rate. This increase is consistent with our expectation that the impact of today's energy prices has affected the quality of the loan book (and will for a number of years to come), and allows the credit union to recognize the impact in the current statements since it results from the economic conditions of 2015.

Total other income increased during the year by \$7.3 million, or 9.0%. Members continued to benefit from the investment Servus has made in wealth services, taking advantage of the support and advice we can offer in areas from investments to insurance to estate planning. Income in this area rose \$3 million, or 18.8%, compared to 2014.

Service fee income in 2015 was mostly unchanged. This reflects ongoing service fee evaluation and revisions where some fees increase and others decrease.

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Operating Expenses

Total operating expenses were down slightly from 2014, which is a result of the work the Servus has done to manage costs. This in turn supports competitive rates and services for our members. Increases in areas like the cost of deposit insurance (up \$2.6 million or 15.2%), amortization (up \$3.5 million or 94.3%) and marketing (up \$1.8 million or 18.1%) were offset by decreases in admin fees (down \$1.6 million or 4%), computer processing fees (down \$2.0 million or 19%), and consulting fees (down \$2.8 million or 8.3%). Several information system projects were finalized in 2014, increasing amortization and decreasing consulting fees.

Net Income

Net income before patronage and taxes was \$129.5 million, which is \$12.4 million, or 10.6% higher, than last year. This solid number was the result of the work of our employees and the continued business support of our members. It allowed us to build our capital position and to share \$47.9 million in profits with our members.

Change Takes Time: Outlook for 2016

Many employers tried to retain skilled employees for as long as they could in 2015. Their layoffs affected employees from outside of Alberta first. Projects that were already underway were finished and new projects were delayed.

As late as Oct. 31, 2015, many economic forecasts called for Alberta's economy to rebound in 2016. However, our analysis and financial results suggest that Alberta's economy in 2016 will be the same as 2015 or possibly worse. The result of this could be that we'll see more rounds of layoffs throughout the province.

Looking forward, Servus and other financial institutions in the province will feel more of the impact from the slower Alberta economy. This may negatively affect our income, but it may also cause some competitors to decrease their financial services in the province and would provide a greater opportunity for Servus.

Our purpose is to serve our members, and that purpose has never been more important and held so much potential. Our policies that were sound in the good times are also sound in difficult times.

Our credit union has the capital to support more growth. We have the systems, the skills and the desire to earn more business from Albertans. We believe that Servus is ready for a period of economic disruption — both the good and the bad — and that all Servus members will ultimately benefit in the long run.

The topic of housing prices is rarely far from the headlines in Canada these days. Given that much of the business we have from members is connected to their mortgages, we need to speak to our expectations for housing in 2016. Growth in this area should slow, but we do not assume there will be a significant decline in values outside of some areas with significant energy exposure. Prices will likely soften, especially in those areas, but low interest rates and the strong average income of Albertans should help support values. We feel that the greatest threat to housing prices is a sustained rise in interest rates, and we don't believe this is in store during 2016.

As a member-owned financial institution that can balance profit with other considerations, we feel that our co-operative business model will show its advantages in a tougher economy. All economies go through cycles. Our hard work and preparation allow us to see this change in the economy as an opportunity rather than a threat. We can reaffirm our commitment to our members and demonstrate our sound financial practices to all Albertans.

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Setting the Direction: 2016 – 2018 Strategic Plan

While our operating environment saw significant change in 2015, Servus Credit Union was well-prepared to meet the challenges head on. We built on last year's successful completion of the foundational work that enhanced our banking system and product suite, and we were able to further enhance our members' lives by providing them sound, advice-based products and services.

We continued to implement our foundational strategies of value proposition, members first, corporate social responsibility, financial sustainability and leadership development. The implementation of these, along with continued development and implementation of our organizational change management strategies, people strategy, long-term delivery strategy and member experience strategy will continue to help guide how we operate and do business.

As we evolve the 2016 – 2018 strategic plan, there are some familiar themes that are woven throughout like technology innovation and strategic cost allocation, where spending is focused on only those areas that clearly support long-term differentiation and add value to members or that are an operational necessity.

Going forward, these themes will be central to achieving profitable growth and remaining competitive in today's economic and interest rate environment.

Balanced Scorecard

Servus continues to use a balanced scorecard system that allows us to measure and track our success. As an effective and comprehensive forward-looking tool, the balanced scorecard provides a clear understanding of what success looks like to Servus. The balanced scorecard shows our progress in achieving our strategic business plan under the following categories:

Member Experience

We will continue to provide exceptional member service by providing the most appropriate products, programs and services to meet members' expectations and diverse needs. Our decisions reflect the best interests of our members, communities, employees and our organization.

Employee Experience

We are proud that employees feel Servus provides a positive, safe, rewarding and engaging work environment. We will continue to invest in our employees by engaging, developing and advancing them through on-the-job experience, career opportunities, and mentoring and leadership development programs.

Financial Performance

As a member-owned financial institution, we strive for financial sustainability and diversity so we can be profitable and serve our members' best interests for years to come. A credit union is a generational trust and must be operated with a plan to ensure long-term financial viability so that we are available to help the next generation of members.

Business Processes

We will continuously focus attention and resources on improving processes, automate where it makes business sense and eliminate activities that cost more than the value they bring to our members, employees and the organization.

Governance and Credit Union Relations

Our Board of Directors governs with a focus on organization wide policy and strategy, recognizes its responsibility and accountability to our member-owners and is committed to continuously improving effectiveness. As an organization, we are committed to being a leader in our industry and provide guidance within a strong credit union system provincially, nationally and internationally.

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A Framework for Success

Corporate Governance

We embrace the credit union principle of democratic ownership through our Board of Directors. The Servus Credit Union Board of Directors represents our member-owners, ensuring they have a voice in the direction of the credit union. By holding to the principles of openness, transparency, accountability, ethics and rule of law, the board is a strong and effective governing body that keeps our members' interests top of mind. The Servus Board of Directors sets the strategic direction and puts in place the controls necessary for our credit union to be a success.

Board Mandate

The Board of Directors ensures that Servus creates and maintains value for stakeholders and serves the needs of our members and their communities. The board sets the credit union's strategic direction, formulates and monitors policies, evaluates organizational performance and ensures an effective risk management framework is in place.

The board uses a Servus policy governance model and functions in accordance with the Credit Union Act and Servus Credit Union bylaws. It is responsible for the election of the board chair and vice-chair and for the selection of directors to represent Servus on the Board of Credit Union Central of Alberta. The board also hires and supervises the president and chief executive officer (CEO).

Board Structure

Our Board of Directors is made up of 12 Servus member-owners and has established committees to help govern Servus effectively and to better manage risk.

There are three board committees:

Audit & Finance Committee

The Audit and Finance Committee oversees the financial reporting process, reviews financial statements, liaises with internal and external auditors and regulators and reviews internal control procedures.

Governance & Human Resources Committee

The Governance and Human Resources Committee establishes and maintains effective governance guidelines, ensures the performance and succession of the CEO and ensures compliance with governance policies and Servus bylaws. This committee also serves as the Nominating Committee for the director elections.

Enterprise Risk Management Committee

The Enterprise Risk Management Committee oversees the identification, understanding and management of risks that may affect Servus.

In addition to these committees, the Board of Directors appoints qualified employees, as recommended by the CEO, to a credit committee. This committee authorizes loans within limits established by the Board of Directors and provides reports to the board.

Position Descriptions

Servus's directors provide strategic advice and business oversight of our operations. They are required to act honestly and in good faith with a view to the best interests of our credit union. They must exercise care, diligence and skill. The board annually reviews the position descriptions for the board chair, committee chairs, directors and CEO.

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Orientation and Education

New Servus directors must complete an orientation session within two months of their election and are encouraged to complete a policy governance course during their first year in office. We also expect our directors to complete the online training curriculum for the Credit Union Director Achievement program within one year of their election.

These and other learning opportunities enable our directors to further develop their knowledge and skills and enhance their performance on the board. A board competency and skills matrix was developed and introduced for use by the board in 2012 to help determine training needs, and it continues to be updated.

Ethical Conduct

The board is committed to ethical, professional and lawful conduct. Directors work to ensure that Servus meets all public, regulatory and member expectations in compliance with existing laws.

Directors must represent loyalty without conflict to the interests of our members. This accountability comes before any personal interest. We require our directors to declare any conflicts or perceived conflicts of interest immediately upon becoming aware of them.

Nomination

Servus holds an annual election to fill vacancies on the board. Our member-owners elect directors to a three-year term, at the end of which they may run for re-election. Servus has no limit on the number of terms a director may serve. The Governance and Human Resources Committee, through the Nominating Committee, plays an active role in identifying potential candidates for the board. Individuals interested in serving on the board must submit nomination papers that provide detailed information such as:

- Work experience
- Educational background
- A self-assessment of skills, knowledge and experience
- Previous board and volunteer experience

Candidates must also undergo a criminal record check.

We provide profiles on all board candidates to our members on our website and in our branches. Voting is held at every branch and online. The Governance and Human Resource Committee reviews the electoral process. Below are some recent changes to the election process that have been approved by the board and implemented.

- The total number of candidates is limited to twice the number of available positions.
- Candidate selection criteria are based on skills and competencies that are key to the continued success of the credit union.
- The board nominating Committee is made up of members of the board's Governance and Human Resources Committee, two Community Council representatives and an independent advisor from the private sector.
- Candidates provide responses to four questions in addition to other background materials, which are then made available so members can get a better understanding of where they stand on key issues.
- Amended campaigning policy allows for the use of social media by candidates as long as the organization's brand is preserved.

Each candidate is interviewed by the Nominating Committee to confirm that the candidate's skills and competencies match those required by the organization going forward.

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Director Remuneration

Servus provides each member of the board with an honorarium for their activities during the course of their term. These activities include attending board, committee and general meetings; branch openings; education and planning sessions; and credit union system conferences. We also reimburse board members for all travel expenses and pay a meeting per diem.

Honorarium

Directors	\$30,000 per annum
Vice chair	\$35,000 per annum
Chair	\$40,000 per annum
Committee chair	\$4,000 per annum

Servus's management (or a third party on behalf of Servus) conducts regular compensation reviews to help determine the appropriate rate of remuneration for the board. We also participate in biannual national credit union surveys that look at board remuneration. Expense reimbursement is excluded, and the total is reported separately in the financial statements.

Committee names:

- Audit & Finance (AFC)
- Enterprise Risk Management (ERM)
- Governance & Human Resources (GHR)

November 1, 2014 – October 31, 2015

Director	Board Meetings*	Committee	Committee Meetings	Total Remuneration: Honorarium + Per Diem (includes CPP)
Doug Hastings (Board Chair)	11 of 11	Chair/Vice/CEO GHR AFC LCUC	11 8 5 3 days	\$67,879.91
John Lamb (Vice Chair)	11 of 11	Chair/Vice/CEO AFC GHR Community Council CUCA AGM CUCC AGM CUDA	10 6 11 6 3 days 3 days 2.5 days	\$67,879.99
Alison Starke	10 of 11	ERM AFC GHR Central Briefing Community Council	2 2 8 5 1	\$48,523.54
Amy Corrigan	11 of 11	GHR(C) ERM (C) AGM Committee 2016 AFC Community Council CUCA AGM CUCC AGM CUDA	10 2 of 2 2 5 3 3 days 3 days 1.5 days	\$65,830.03

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Darcy Mykytyshyn	9 of 11	AFC ERM Community Council	4 1 5	\$42,331.49
Dianne Brown	11 of 11	GHR ERM AFC AGM Committee 2015 Community Council CUCA AGM CUDA	14 2 4 5 12 3 days 1 day	\$61,912.21
Iris Evans (New director)	6 of 6	GHR(C) AFC ERM Community Council Central AGM CUDA	9 4 2 2 3 days 2 days	\$37,833.38
Jon Holt	11 of 11	AFC GHR ERM Central Briefing Community Council CUCC AGM	5 9 1 6 2 3 days	\$54,663.11
Ken Cameron (New director)	6 of 6	GHR AFC Community Council CUCC Conference	8 3 5 3 days	\$37,051.24
Penny Reeves	11 of 11	ERM AFC GHR Community Council CUCA AGM CUCC AGM	4 6 2 3 3 days 3 days	\$50,800.00
Perry Dooley	11 of 11	AFC (C) AFC GHR ERM Central Briefing Community Council CUCC Conference CUDA	4 4 2 1 6 1 3 days 1 day	\$57,681.05
Peter Elzinga (Retired Mar 15)	5 of 5	GHR AFC	10 1	\$20,800.00
Simon Neigum	11 of 11	AFC AFC (C) ERM GHR Community Council CUCA AGM CUDA	4 4 3 3 2 3 days 1 day	\$57,794.68
William Anhorn (Retired Mar 2015)	3 of 5	ERM (C)	1	\$16,694.19

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- Board meetings include Servus's annual general meeting, annual board planning session, joint meeting with the CUDGC board and ad hoc board teleconferences.
- Standing board committees include Audit & Finance, Governance & Human Resources and Enterprise Risk Management.
- The Board of Director chair is an ex officio member of all committees.
- Board members are assigned to one committee at the organizational meeting in March but can attend any committee meeting. Committee assignments can cross two fiscal years. One board member sits on the AFC and ERM committees as a crossover member.
- The Governance & Human Resources Committee includes the Nominating Committee, which holds candidate interviews in November in addition to a candidate orientation meeting.
- (C) stands for committee chair. Because the chair may change in March of each year, more than one committee chair may appear in the table.
- AGM 2015 and AGM 2016 denote Servus's Board of Directors' representative on the AGM Committee.
- Central briefing means the board member is on the Credit Union Central of Alberta's (CUCA) board.
- Chair/Vice Chair/CEO refers to briefing meetings.
- Directors also receive per diems when attending Alberta and Canada's Credit Union Centrals' annual general meetings and conference as well as the Credit Union Director Achievement (CUDA) program.
- There are 34 community councils around the province.
- LCUC stands for Large Credit Union Conference.

Performance Evaluation

Each year, the Board of Directors and the CEO are evaluated to assess their effectiveness and to identify opportunities for improvement. Performance evaluations for the board include a self-assessment tool as well as a peer review. Additional feedback is gathered for the board chair and each board committee regarding their performance and areas for improvement.

The board assesses the CEO's performance each year by reviewing results against the balanced scorecard targets as well as looking at overall performance.

Board and Committee Meetings

The Board of Directors held seven regular board meetings in 2015 and one two-and-a-half-day planning session in April.

In addition, the Audit and Finance Committee met eight times, the Enterprise Risk Management Committee met six times, and the Governance and Human Resources Committee met 10 times. Additional ad-hoc committee meetings were held as required.

Directors participated in the following:

- Servus's Annual General Meeting in March 2015
- The Credit Union Central of Alberta Conference and Annual General Meeting in April 2015
- The Credit Union Central of Canada Conference and Annual General Meeting in May 2015
- The World Credit Union Conference in July 2015

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Risk Management

Servus has in place a risk management structure that enables us to adapt to changes in economic and operational environments. The following is an overview of this structure and the types of risk we’re typically exposed to. (See Note 29 on Financial Risk Management in the 2015 Consolidated Financial Statements for more details.)

Enterprise Risk Management

Servus uses an enterprisewide approach to identify, measure, monitor and manage risk. We based this approach primarily on the ISO 31000 risk management framework (International Organization of Standardization).

The primary goals of risk management are to ensure that the outcomes of risk-taking activities are consistent with our credit union’s objectives and risk tolerance and that there is an appropriate balance between risk and reward to maximize value for our member-owners.

We believe that effective enterprise risk management is a journey and not a destination, so we continue to grow, evolve and adapt our risk management program. The framework we use provides processes for identifying risks and assessing the likelihood of their occurrence and impact. The framework is also used to establish policies, procedures and controls to ensure that we manage risk within acceptable tolerances.

Servus’s enterprise risk management governance model begins with oversight by the Board of Directors, either directly or through its committees, as shown in Figure 1.

The CEO is responsible and accountable for risk management. Day-to-day monitoring and reporting on risk is delegated to the senior vice president Risk and Audit. Four management committee — the Asset Liability Committee, the Management Credit Committee, the Management Corporate Social Responsibility (CSR) Committee and the Management Risk Committee — identify, assign and monitor risks through their work. Ownership of key risks is delegated to the appropriate Executive Leadership Team member.



Figure 1: Servus Credit Union’s Enterprise Risk Management Governance Model

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Traditional risk management solutions tend to focus on negative events and often depend on diligent corporate compliance programs. We proactively elevate material risk issues to senior management and the board. This helps Servus find a better balance between loss prevention, risk mitigation efforts and entrepreneurial risk-taking.

Servus’s risk management framework has four cornerstones (see Figure 2). We review and update each cornerstone to ensure consistency with risk-taking activities and relevance to our business and financial strategies, the Credit Union Deposit Guarantee Corporation (CUDGC) Standards of Sound Business practices and the legislative environment.

Practices and the Legislative Environment

Policies, Strategies and Limits

The governance, risk management direction and extent of Servus’s risk-taking activities are established through policies, strategies and limits. Policies are also developed based on the requirements of the regulator and require input from the Board of Directors and senior management.

Guidelines

Guidelines are the directives provided to implement the policies. Generally, these describe types of risks and exposures, whether geographic or industry related.

Processes and Standards

Processes are the activities associated with identifying, evaluating, documenting, reporting and controlling risk. Standards define the breadth and quality of information required to make a decision and the expectations in terms of quality of analysis and presentation.

Measurement and Reporting

Servus monitors its risk exposure to ensure it is operating within approved limits or guidelines. Breaches, if any, are reported to senior management or board committees (depending on the limit or guideline). Servus’s Internal Audit department independently monitors the effectiveness of risk management policies, procedures and internal controls.

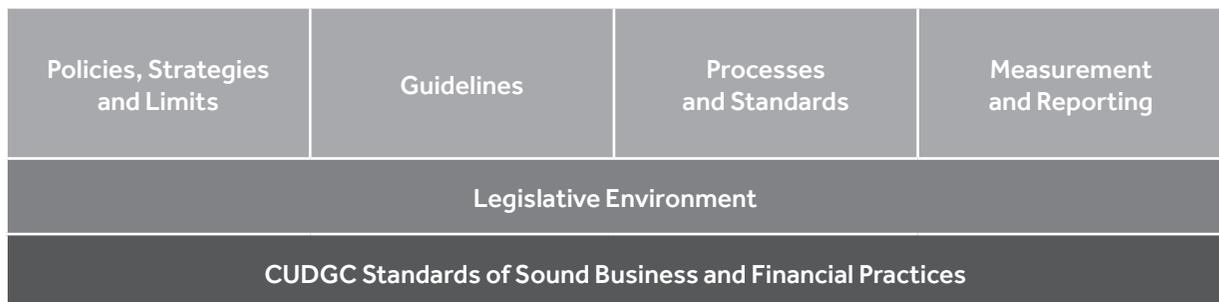


Figure 2: Servus Credit Union’s Risk Management Framework

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Types of Risk

Servus groups its major risks into eight categories:

1. Credit Risk

Credit risk is the risk of financial loss resulting from the failure of an individual or business to honour an obligation to our credit union. Credit risk arises any time credit union funds are extended, committed, invested or otherwise exposed through actual or implied contractual agreements. Credit risk is found primarily in the lending portfolio but is also present in other transactions.

Servus manages credit risk through policies and limits to ensure broad diversification across Alberta and within various industries and product mixes. We also manage risk through maximum limits on individual and connected accounts, participation in syndicated loans and minimum standards for loan quality. As well, Servus manages this risk through experienced and skilled lenders who have demonstrated experience, education and clearly documented decision-making authority, and through approval processes that include a Management Credit Committee.

2. Operational Risk

Operational risk is the possibility that Servus may not be able to offer its products and services to members or continue to operate its business. It is also the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. While operational risk cannot be completely eliminated, proactive operational management is a key strategy to mitigate this risk.

Servus manages operational risk through a knowledgeable and experienced management team. The team members are committed to the risk management policies and to promoting an ethical culture with clear communication to reinforce and guide our operational risk-taking activities. Our implementation of supporting policies and procedural controls includes (among others) the segregation of duties and built-in systemic checks and balances. Additional controls include an established "whistleblower" process, an employee code of conduct, regular internal audits by an independent audit team and continual review and upgrade of systems and procedures.

3. Liquidity Risk

Liquidity risk is the possibility that Servus is unable to meet its financial obligations as they fall due. It entails:

- The sufficiency of the deposit base and/or other funding sources to maintain the asset base
- The risk of having insufficient liquid resources to meet our credit union's cash or funding requirements
- The risk of having insufficient liquid investments to meet statutory liquidity requirements

Servus's liquidity policies include the measurement and forecast of cash flows, a stable base of core deposits from retail and commercial customers, limits on single deposits and sources of deposits and monitoring of wholesale demand and term deposits. The Servus liquidity management strategy includes daily monitoring of expected cash inflows and outflows, as well as tracking and forecasting the liquidity position of our credit union on a forward 90-day rolling basis.

4. Market Risk

Market risk is the risk of financial loss resulting from changes to the value of the assets or liabilities of Servus, most commonly through interest rate changes.

To manage interest rate risk effectively, the Asset Liability Committee establishes policy guidelines and meets regularly to monitor the Bank of Canada's position and determine future strategies. The Board of Directors approves and reviews interest rate risk policies at least annually, with regular reporting provided to its Enterprise Risk Management and Audit and Finance Committees.

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5. Reputation Risk

Reputation risk is the risk to earnings and capital arising from negative public or stakeholder opinion. This can result from actual or alleged conduct in any number of activities but often involves questions about business ethics and integrity, competence, corporate governance practices, quality and accuracy of financial reporting disclosures or quality of products and services. Negative public or stakeholder opinion could adversely affect our ability to attract and keep members and could expose Servus to legal or regulatory action.

Servus manages and measures reputation risk by monitoring the external media environment; conducting regular surveys of members, non-members and employees; and reviewing regular reports from the Management Risk Committee. In addition, our employee code of conduct, our corporate values and our CSR policy reinforce the standards and sound business practices we believe are essential to maintaining our reputation.

6. Regulatory and Compliance Risk

Regulatory and compliance risk is the risk of Servus not fulfilling the requirements of external or internal regulatory functions. Regulatory risk differs from other banking risks, such as credit risk or market risk, in that it is typically not a risk actively or deliberately assumed by management in expectation of a return. Rather, it occurs as part of the normal course of operating our credit union.

The Servus philosophy is to manage regulatory risk by maintaining a strong culture of integrity and sound controls. Business units and corporate areas are responsible for managing day-to-day regulatory and legal risk, while our Compliance departments assist them by providing advice and oversight. Again, our code of conduct and corporate values help set the tone for a culture of integrity. The code stipulates that concern for what is right, including compliance with the law, should be the first consideration in all business decisions and actions. All directors, officers and employees are required to attest annually that they understand the code of conduct and comply with its provisions.

7. Emerging Risks

Servus monitors and reports to both the Management Risk Committee and the Board Enterprise Risk Management Committee on risks that, although not fitting in any of the previous risk categories, may have an impact on its operations. These include changing economic conditions, the impacts of geographic concentration within single industry locations, fraud and crime trends and issues relating to continuing consolidation through amalgamations.

We continue to mature our enterprise risk management program to ensure that the business understands the environment in which we operate while monitoring key risk indicators to effectively manage risk.