2020 CONSOLIDATED FINANCIAL STATEMENTS OF FIRSTONTARIO CREDIT UNION LIMITED

CONTENTS

REPORT ON MANAGEMENT RESPONSIBILITY

The accompanying Consolidated Financial Statements and all information contained in this Annual Report are the responsibility of the Management of FirstOntario Credit Union Limited, which is responsible for the integrity and fairness of the information presented. The Consolidated Financial Statements, in the opinion of Management, have been prepared using appropriate accounting policies that are in accordance with International Financial Reporting Standards and the Credit Unions and Caisses Populaires Act, 1994 (Ontario), and are based on informed judgments and estimates of the expected effects of current events and transactions.

To meet its responsibility for the integrity and objectivity of data in the Consolidated Financial Statements, Management has developed and maintains a system of internal accounting controls. Management believes that this system of internal controls provides reasonable assurance that the financial records are reliable and form a proper basis for preparation of Consolidated Financial Statements and that assets are properly accounted for and are safeguarded.

The Board of Directors is responsible for reviewing and approving the Consolidated Financial Statements and for overseeing Management's performance of its financial reporting responsibilities. The Board of Directors carried out its responsibility for the Consolidated Financial Statements through its regular review of financial results and operations and through its Audit and Risk Committee. The Member-appointed auditors have full and free access to, and meet periodically with, the Audit and Risk Committee and may meet with the Board of Directors, with or without Management present, to discuss their audit and matters relating to financial statement presentation, internal controls and audit procedures.

The Financial Services Regulatory Authority of Ontario conducts periodic examinations of the financial conditions and affairs of FirstOntario. The examination includes review of FirstOntario's compliance with the provisions of the Act.

KPMG LLP, Member-appointed external auditors, has examined the Consolidated Financial Statements in accordance with Canadian generally accepted auditing standards and their independent auditors' report is included as part of the Consolidated Financial Statements.

Lloyd Smith, CPA, CGA, CCE
Chief Executive Officer

Barry Doan, CPA, CA, MAcc
Chief Financial Officer

March 4, 2021

REPORT OF THE AUDIT AND RISK COMMITTEE

FirstOntario Credit Union Limited's Audit and Risk Committee is a committee of the Board of Directors pursuant to Section 125 of the Credit Unions and Caisses Populaires Act, 1994 (Ontario) and Section 27 of Ontario Regulation 237/09. The Committee, which consists of seven directors, has a mandate to cover all of the duties, which are specified to be performed by audit committees in the Regulations of the Act.

The Audit and Risk Committee is pleased to report to the Members of FirstOntario that it has fulfilled its annual mandate. During the year the Committee held 10 meetings and completed the following significant activities:

(a) Served as the principal communication link between the external auditors and the Board of Directors and, in particular, reviewed the terms of engagement and scope of the audit and reviewed FirstOntario's annual financial statements prior to Board approval for issuance to the Members.

(b) Obtained a reasonable understanding of the important elements of internal controls that are important to safeguarding the assets of FirstOntario, ensuring the accuracy of financial reports and ensuring compliance with policies and procedures.

(c) Served as the Board's liaison with the internal auditor and reviewed the internal audit mandate, work plan and reports.

(d) Reviewed the policies, procedures and controls, which relate to legislative compliance, with a particular focus on requirements for liquidity, capital adequacy and interest rate management.

(e) Reviewed management's identification of the significant risks of FirstOntario in accordance with the Enterprise Risk Management policy and ensured processes were in place to measure, monitor, manage and mitigate significant risk exposures including appropriate policies, procedures and controls.

There are no significant recommendations made by the Audit and Risk Committee that have not been either implemented or are in the process of being implemented. In addition, there are no matters which the Audit and Risk Committee believes should be reported to the Members, other than as described above, nor are there any further matters that are required to be disclosed pursuant to the Act or the Regulations thereto.

Based on its findings, the Audit and Risk Committee issues reports and makes recommendations to the Board of Directors or senior management, as appropriate, with respect to the matters outlined above and follows up to ensure that the recommendations are considered and implemented. During the year, the Committee received full co-operation and support from management to enable it to play an effective role in maintaining the quality of financial reporting to the Members and enhancing the overall control structure of FirstOntario.

Stu Walker
Chair, Audit and Risk Committee

March 4, 2021

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INDEPENDENT AUDITORS' REPORT

To the Members of FirstOntario Credit Union Limited

Opinion

We have audited the accompanying consolidated financial statements of FirstOntario Credit Union Limited (the "Credit Union"), which comprise:

- the consolidated statement of financial position as at end of December 31, 2020
- the consolidated statement of income for the year then ended
- the consolidated statement of income and other comprehensive income for the year then ended
- the consolidated statement of changes in members' equity for the year then ended
- the consolidated statement of cash flows for the year then ended
- and notes to the consolidated financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Credit Union as at end of December 31, 2020 and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "*Auditors' Responsibilities for the Audit of the Financial Statements*" section of our auditors' report.

We are independent of the Credit Union in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other responsibilities in accordance with these requirements.

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

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, 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.

In preparing the financial statements, management is responsible for assessing the Credit Union's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Credit Union or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Credit Union's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Credit Union's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Credit Union's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Credit Union to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

Hamilton, Canada
March 4, 2021

FIRSTONTARIO CREDIT UNION LIMITED
Consolidated Statement of Financial Position

As at December 31, 2020, with comparative information for 2019

(In thousands of dollars)	**2020**	2019
Assets		
Loans Receivable from Members		
Residential mortgage loans (note 5)	**$ 3,350,091**	$ 3,080,625
Personal loans (note 5)	**95,262**	103,590
Commercial loans (note 5)	**801,386**	793,666
Accrued interest receivable	**19,514**	18,187
	4,266,253	3,996,068
Other		
Cash and cash equivalents (note 7)	**26,892**	25,712
Investments (note 9)	**559,892**	540,122
Fixed assets (note 10)	**56,105**	57,700
Derivative financial instruments (note 16)	**2,140**	1,648
Other assets	**11,079**	8,392
	$ 4,922,361	$ 4,629,642
Liabilities		
Members' Deposits and Shares		
Deposits (note 12)	**$ 3,988,368**	$ 3,616,266
Membership shares (note 13)	**9,131**	8,707
Investment shares (note 13)	**11,732**	12,049
Accrued interest on deposits and shares	**25,007**	22,515
	4,034,238	3,659,537
Other		
Loans payable and securitization liabilities (note 15)	**529,999**	652,340
Lease liabilities (note 11)	**17,057**	19,149
Accounts payable and accrued liabilities	**78,434**	58,853
Derivative financial instruments (note 16)	**2,582**	1,211
	4,662,310	4,391,090
Members' Equity		
Investment shares (note 13)	**112,293**	110,261
Contributed surplus	**5,474**	4,865
Retained earnings	**148,723**	127,514
Non-controlling interest	**(191)**	(122)
Accumulated other comprehensive loss	**(6,248)**	(3,966)
	260,051	238,552
	$ 4,922,361	$ 4,629,642

See accompanying notes to Consolidated Financial Statements.

On behalf of the Board:

Carey Smith
Board Chair

Stu Walker
Chair, Audit and Risk Committee

FIRSTONTARIO CREDIT UNION LIMITED
Consolidated Statement of Income

For the year ended December 31, 2020, with comparative information for 2019

(In thousands of dollars)		2020		2019
Interest Income				
Members' loans (note 5)	**$**	**149,846**	$	144,657
Other		**19,096**		7,085
		168,942		151,742
Interest Expense				
Members' deposits (note 12)		**67,955**		70,527
Dividends on membership and investment shares (note 13)		**1,133**		1,135
Loans payable and securitization liabilities (note 15)		**18,247**		14,306
Other		**465**		85
		87,800		86,053
Net Interest Income		**81,142**		65,689
Provision for impaired loans (note 6)		**(5,970)**		(3,297)
Other income (note 20)		**38,862**		42,447
Net Interest and Other Income		**114,034**		104,839
Non-interest Expenses				
Salaries and employee benefits		**48,075**		51,152
Administrative		**15,224**		15,188
Technology		**12,825**		11,556
Occupancy		**8,210**		8,116
Donations and community sponsorship		**530**		1,436
		84,864		87,448
Income Before Income Taxes		**29,170**		17,391
Income taxes (note 21)		**4,407**		3,247
Consolidated Net Income for the year	**$**	**24,763**	$	14,144
Net Income attributable to FirstOntario Credit Union Limited		**24,832**		14,193
Net Loss attributable to Non-controlling interest		**(69)**		(49)
Consolidated Net Income for the year	**$**	**24,763**	$	14,144

See accompanying notes to Consolidated Financial Statements.

FIRSTONTARIO CREDIT UNION LIMITED
Consolidated Statement of Income and Other Comprehensive Income

For the year ended December 31, 2020, with comparative information for 2019

(In thousands of dollars)	2020	2019
Consolidated Net Income for the year	**$ 24,763**	$ 14,144
Other Comprehensive Income (Loss)		
Items that are or may be reclassified subsequently to net income:		
Net loss on cash flow hedges	**(3,036)**	(765)
Net gain on cash flow hedges transferred to earnings	**1,329**	822
Related income tax expense (recovery) (note 21)	**316**	(11)
Items that are not recycled or reclassified to net income:		
Actuarial loss on employee benefits, net of tax (note 19)	**(891)**	(1,006)
	(2,282)	(960)
Total Income and Other Comprehensive Income for the year	**$ 22,481**	$ 13,184

See accompanying notes to Consolidated Financial Statements.

FIRSTONTARIO CREDIT UNION LIMITED
Consolidated Statement of Changes in Members' Equity

For the year ended December 31, 2020, with comparative information for 2019

(In thousands of dollars)	Investment shares	Contributed surplus	Retained earnings	Non-controlling interest	Accumulated Other Comprehensive Income (Loss): Cash flow hedging reserve	Accumulated Other Comprehensive Income (Loss): Employee benefits	Total
Balance, January 1, 2020	**$ 110,261**	**$ 4,865**	**$ 127,514**	**$ (122)**	**$ (1,333)**	**$ (2,633)**	**$ 238,552**
Shares issued during the year	**4,485**	**-**	**-**	**-**	**-**	**-**	**4,485**
Shares redeemed during the year	**(3,582)**	**-**	**-**	**-**	**-**	**-**	**(3,582)**
Acquisition of Creative Arts Financial (Note 23)	**1,129**	**609**	**-**	**-**	**-**	**-**	**1,738**
Net income for the year	**-**	**-**	**24,832**	**(69)**	**-**	**-**	**24,763**
Dividends paid (net of tax recovery $830)	**-**	**-**	**(3,623)**	**-**	**-**	**-**	**(3,623)**
Other comprehensive loss	**-**	**-**	**-**	**-**	**(1,391)**	**(891)**	**(2,282)**
Balance, December 31, 2020	**$ 112,293**	**$ 5,474**	**$ 148,723**	**$ (191)**	**$ (2,724)**	**$ (3,524)**	**$ 260,051**

(In thousands of dollars)	Investment shares	Contributed surplus	Retained earnings	Non-controlling interest	Accumulated Other Comprehensive Income (Loss): Cash flow hedging reserve	Accumulated Other Comprehensive Income (Loss): Employee benefits	Total
Balance, January 1, 2019	$ 106,934	$ 4,865	$ 116,857	$ (73)	$ (1,379)	$ (1,627)	$ 225,577
Shares issued during the year	4,340	-	-	-	-	-	4,340
Shares redeemed during the year	(1,013)	-	-	-	-	-	(1,013)
Net income for the year	-	-	14,193	(49)	-	-	14,144
Dividends paid (net of tax recovery $804)	-	-	(3,536)	-	-	-	(3,536)
Other comprehensive income (loss)	-	-	-	-	46	(1,006)	(960)
Balance, December 31, 2019	$ 110,261	$ 4,865	$ 127,514	$ (122)	$ (1,333)	$ (2,633)	$ 238,552

See accompanying notes to Consolidated Financial Statements.

FIRSTONTARIO CREDIT UNION LIMITED
Consolidated Statement of Cash Flows

For the year ended December 31, 2020, with comparative information for 2019

(In thousands of dollars)	2020	2019
Cash Flows from Operating Activities		
Consolidated net income for the year	**$ 24,763**	$ 14,144
Adjustments for:		
Amortization of fixed assets	**8,875**	8,564
Net change in fair value of assets recorded as fair value through profit or loss	**(13,377)**	(18,333)
Gain on sale of assets	**-**	16
Net changes in accrued employee retirement benefits	**1,202**	1,258
Other non-cash items, net	**9,709**	4,567
Net interest income	**(81,142)**	(65,689)
Income tax expense	**4,407**	3,247
Changes in operating assets:		
Net change in loans receivable from Members	**(274,837)**	(388,629)
Net change in derivative assets held for risk management	**837**	(383)
Changes in operating liabilities:		
Net change in deposits	**372,102**	327,028
Net change in derivative liabilities held for risk management	**(1,665)**	(749)
Interest received	**159,716**	153,309
Interest paid	**(83,710)**	(83,846)
Income tax paid	**-**	(2,032)
Income tax received	**1,090**	-
Cash flows from (used in) operating activities	**127,970**	(47,528)
Cash Flows from Financing Activities		
Net issuance (redemptions) in membership shares	**(198)**	(1,069)
Net redemptions in investment shares	**(3,248)**	(1,918)
Principal payments on leases	**(2,508)**	(2,426)
Net change in loans payable and securitization liabilities	**(122,341)**	44,252
Cash flows (used in) from financing activities	**(128,295)**	38,839
Cash Flows from Investing Activities		
Net investment purchases	**8,614**	(20,721)
Net investment income	**(243)**	(1,636)
Proceeds on disposition of investment	**-**	19
Purchase of fixed assets, net of disposals	**(6,866)**	(5,578)
Cash flows from (used in) investing activities	**1,505**	(27,916)
Cash and cash equivalents		
Net increase (decrease) during year	**1,180**	(36,605)
Balance at beginning of year	**25,712**	62,317
Balance at end of year	**$ 26,892**	$ 25,712

See accompanying notes to Consolidated Financial Statements.

1. Corporate Information:

FirstOntario Credit Union Limited (“FirstOntario”) is a financial institution incorporated in Ontario which operates in compliance with the Credit Unions and Caisses Populaires Act of Ontario (the “Act”) and is a member of Central 1 Credit Union (“Central 1”). The location of the head office and principal place of business of FirstOntario is 970 South Service Road, Stoney Creek, Ontario, L8E 6A2.

FirstOntario exists to help Members meet their financial needs in their local communities. FirstOntario’s principal activities are the provision of deposit-taking, lending and other financial services.

FirstOntario’s Member deposits are insured by the Financial Services Regulatory Authority of Ontario (“FSRA”) under a mandatory program, the expense for which amounted to $3,152,000 (2019 - $2,666,000). At December 31, 2020, there were 125,900 Members (2019 – 118,500).

2. Basis of Preparation:

Statement of compliance

The Consolidated Financial Statements of FirstOntario have been prepared in accordance with International Financial Reporting Standards (“IFRS”). IFRS comprise of accounting standards issued by the International Accounting Standards Board (“IASB”) as well as interpretations issued by the IFRS Interpretations Committee.

The financial statements were approved by FirstOntario’s Board of Directors on March 4, 2021.

Basis of measurement

These financial statements were prepared on a going concern basis under the historical cost method, except for certain financial assets and liabilities, which are measured at fair value as described in Note 18. The significant accounting policies used in the preparation of these Consolidated Financial Statements are summarized below and have been applied consistently to all periods presented in the financial statements. Certain comparative figures have been reclassified to conform to the current year’s financial statement presentation.

Details of FirstOntario’s accounting policies, including changes during the year, are included in Note 3.

Use of estimates and judgments

The preparation of Consolidated Financial Statements in conformity with IFRS requires management to exercise judgment and develop estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts in revenue and expenses during the reporting year. Actual future results could differ from those estimates.

2. Basis of Preparation (continued):

Use of estimates and judgments (continued)

Items which result in the most significant areas of application of judgment and estimates include the following:

(a) Fair value of financial instruments:

Where fair value of financial assets and liabilities cannot be derived from active markets, FirstOntario uses valuation techniques that include inputs derived from either observable market data or utilizing management judgment. Refer to Note 18 for information relating to these estimates.

(b) Allowance for impairment on loans:

FirstOntario assesses whether credit risk has increased significantly since loan origination, estimates probability of default and loss given default, and incorporates forward-looking information in the measurement of expected credit loss on its loan portfolio.

Refer to Note 6 for information relating to these estimates.

(c) Employee retirement benefits:

FirstOntario estimates the present value of employee retirement benefits, which depends on a number of assumptions including discount rates, expected salary and other cost increases, and mortality rates. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability. Refer to Note 19 for information relating to these estimates.

(d) Hedging and securitizations:

FirstOntario enters into securitization and hedging transactions which require management's best estimates of key assumptions that market participants would use in determining fair value. For more information relating to these estimates refer to Note 8 for securitizations and Note 17 for hedges.

3. Significant Accounting Policies:

These consolidated financial statements have been prepared on a going concern basis. The significant accounting policies applied in the preparation of these consolidated financial statements are set out below. The policies have been consistently applied to all of the periods presented.

(a) Basis of consolidation:

The Consolidated Financial Statements include the assets, liabilities and results of the operations of FirstOntario, 1320818 Ontario Limited, FirstOntario Insurance Holdings Inc. (“FOIH”) and FirstOntario Insurance Brokers Inc. (“FOIB”).

1320818 Ontario Limited is a wholly owned subsidiary of FirstOntario. 1320818 Ontario Limited supplies information technology services and operates the banking system for FirstOntario. All intercompany transactions and balances have been eliminated.

FOIH is a wholly owned subsidiary of FirstOntario. FOIH is a holding company which manages FirstOntario’s holdings in FOIB. FOIH holds 51% of the ownership interests and voting rights of FOIB. All intercompany transactions and balances have been eliminated.

Investments in which FirstOntario exercises joint control are accounted for as a joint venture using the equity method of accounting. FirstOntario’s net investment in the joint venture is recognized as investments on the Consolidated Statement of Financial Position. The carrying value of the joint venture is subsequently increased (decreased) for FirstOntario’s share of any income (loss) received from the joint venture. FirstOntario’s share of any income (loss) received from the joint ventures is included in other income on the Consolidated Statement of Income. Investments are considered to be jointly controlled if there is a contractual agreement to share authority over determining the investments’ operating, investment and financing policies. The joint ventures in which FirstOntario participates include real estate development for the purpose of resale as well as retail and commercial complexes that generate rental and leasing income.

(b) Financial instruments – recognition and measurement:

FirstOntario initially recognizes loans, deposits and mortgage securitization liabilities on the date on which they are originated. All other financial instruments are recognized on the trade date, which is the date on which FirstOntario becomes a party to the contractual provisions of the instrument.

All financial assets and liabilities are initially measured at fair value, plus transaction costs that are directly attributable to its acquisition or issue, for an item not at fair value through profit and loss (“FVTPL”). Subsequent measurement is dependent upon the financial instrument’s classification.

Financial assets and liabilities comprise cash and cash equivalents, derivatives, investments, loans receivable from Members, Members’ deposits and shares, loans payable, securitization liabilities, accounts payable and accrued liabilities.

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

Classification and measurement of financial instruments

On initial recognition, a financial asset is classified as measured at amortized cost, fair value through other comprehensive income ("FVOCI") or fair value through profit and loss ("FVTPL").

The amortized cost of a financial instrument is the amount at which the instrument is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective interest rate method, and for financial assets, adjusted for any expected credit loss allowance.

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows;
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Subsequent to initial recognition, FVOCI financial assets are measured at fair value whereby the unrealized gains and losses are recorded in other comprehensive income ("OCI") and included in accumulated other comprehensive income ("AOCI"). Upon derecognition, the cumulative gains or losses of debt instruments are reclassified from OCI and recorded in the Consolidated Statement of Income.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, FirstOntario may irrevocably elect to present subsequent changes in FVOCI. This election is made on an investment by investment basis. Upon derecognition, any cumulative gains or losses in OCI on equity investments so designated is not recognized in profit or loss.

All other financial assets are classified as measured at FVTPL. Financial instruments measured at FVTPL are subsequently measured at fair value at each reporting date. Gains and losses realized on disposal together with dividends and interest earned on these instruments are reported in interest and other income. Unrealized gains and losses from changes in fair value are reported separately in other income in the Consolidated Statement of Income.

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

On initial recognition, FirstOntario may irrevocably designate a financial instrument that otherwise meets the requirements to be measured at amortized cost or at FVOCI as FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

Business model assessment involves determining whether financial assets are held and managed by FirstOntario for generating and collecting contractual cash flows, selling the financial assets or both. FirstOntario makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue or realizing cash flows through the sale of the assets;
- how the performance of the asset is evaluated and reported to FirstOntario's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how these risks are managed;
- how managers of the business are compensated (for example, whether compensation is based on the fair value of the assets managed or the contractual cash flows collected);
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity.

Financial assets that are held for trading and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

If upon origination of a financial asset, based on established criteria, the financial asset is expected to be securitized as part of a portfolio that qualifies for derecognition, the business objective of holding the financial asset to collect contractual cash flows is not met. Such financial assets are measured at FVTPL. If the financial asset is expected to be securitized as part of a portfolio that does not qualify for derecognition, the held to collect business model is considered to be met, and the financial asset is measured at amortized cost.

Assessment whether contractual cash flows are solely payments of principal and interest

The contractual cash flow characteristics assessment involves assessing the contractual features of an instrument to determine if they give rise to cash flows that are consistent with a basic lending arrangement, that is, if they represent cash flows that are solely payments of principal and interest ("SPPI").

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

Principal is defined as the fair value of the financial asset on initial recognition. Interest is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding and other basic lending risks and costs (for example, liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are SPPI, FirstOntario considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after FirstOntario changes its business model for managing financial assets. There were no changes to any of FirstOntario's business models during the current year.

Financial Liabilities

FirstOntario classifies its financial liabilities as measured at amortized cost or FVTPL.

FirstOntario has designated certain financial liabilities as FVTPL in either of the following circumstances:

- the liabilities are managed, evaluated and reported internally on a fair value basis; or
- the designation eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Classification of investment instruments is outlined in Note 9. Classification of all financial instruments is outlined in Note 18.

Effective interest rate method

Interest income and expense are recognized in the Consolidated Statement of Income using the effective interest method. The calculation of the effective interest rate includes transaction costs, fees and discounts or premiums that are an integral part of the effective yield on the financial asset or liability.

The effective interest rate is the rate that discounts the estimated future cash payments and receipts through the expected life of the financial instrument to the gross carrying amount of the financial asset or the amortized cost of the financial liability. When calculating the effective interest rate for financial instruments other than credit-impaired assets, FirstOntario estimates future cash flows considering all financial terms of the financial instrument, but not expected credit losses. For credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including expected credit losses.

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

Transaction costs

Transaction costs are incremental costs that are directly attributable to the acquisition, issuance or disposal of a financial asset or liability. Transaction costs related to FVTPL financial assets and liabilities are expensed as incurred. Transaction costs relating to amortized cost financial instruments are capitalized and amortized over the expected life of the instrument using the effective interest method.

Offsetting

Financial assets and liabilities are offset and the net amount presented in the Consolidated Statement of Financial Position when, and only when, FirstOntario has a legal right to set off the recognized amounts and it intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRSs, or for gains and losses arising from a group of similar transactions.

Identification and measurement of impairment losses

FirstOntario recognizes loss allowances for expected credit loss (“ECL”) on financial instruments that are not measured at FVTPL. Loss allowances are measured at an amount equal to lifetime ECL, except for financial instruments on which credit risk has not increased significantly since their initial recognition, for which they are measured at 12-month ECL. 12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

ECL is a probability-weighted estimate of credit losses, which considers multiple scenarios based on reasonable and supportable information about past events, current conditions and forecasts of future economic conditions. Forward-looking information is explicitly incorporated into the estimation of ECL.

Measurement of expected credit losses

The determination of whether the ECL is calculated on a 12 month or lifetime basis is dependent on the stage the financial asset falls into at the reporting date. A financial instrument moves across stages based on an increase or decrease in its risk of default at the reporting date compared to its risk of default at initial recognition. When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, FirstOntario considers reasonable and supportable information that is relevant and available without undue cost or effort. There is a rebuttable presumption that the risk of default of the financial instrument has increased since initial recognition when contractual payments are more than 30 days overdue.

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

In assessing whether a financial asset is credit-impaired, FirstOntario considers qualitative and quantitative factors. Evidence that a financial asset is credit-impaired includes significant financial difficulty of the borrower or issuer, a breach of contract such as a default or past due event, and/or it becoming probable that the borrower or issuer will enter bankruptcy or other financial reorganization. In addition, a loan that is overdue for 90 days or more is considered impaired.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognized and ECL is measured as follows:

- if the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset; or
- if the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Presentation of allowance for expected credit losses

Loss allowances for ECL are presented in the Consolidated Statement of Financial Position as follows:

- financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- where a financial instrument includes both a drawn and undrawn component, and FirstOntario cannot identify the ECL on the loan commitment component separately from those on the drawn component: FirstOntario presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognized in the Consolidated Statement of Financial Position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognized in the fair value reserve.

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

Write-offs

Impaired financial assets are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when FirstOntario determines the borrower cannot generate sufficient cash flows to repay the amounts subject to write-off. However, financial assets that are written off could still be subject to collection activities in compliance with FirstOntario's procedures. In subsequent periods, recoveries against written off loans are credited to the provision for impaired loans in the Consolidated Statement of Income.

Refer to Note 6 for further details.

Derivative financial instruments

Derivative financial instruments are financial contracts whose value is derived from interest rates or other financial indices in the equity markets. In the ordinary course of business, FirstOntario enters into various derivative contracts, including interest rate swaps, equity-linked options, foreign exchange forwards and bond forwards. FirstOntario enters into such contracts to manage interest rate fluctuations and foreign exchange risk as part of FirstOntario's asset/liability management program.

Interest rate swaps involve the periodic exchange of payments without the exchange of the notional principal amount upon which the payments are based. Equity-linked options are purchased to hedge deposit products whose interest is linked to various equity indices or a specific bundle of equities. These contracts pay returns based on the change in value of equity indices or a specific bundle of equities.

Foreign exchange contracts are used to hedge FirstOntario's net US dollar liability position.

Derivatives are measured at fair value and are reported as assets where they have a positive fair value and as liabilities where they have a negative fair value. In both cases they are reported as derivative financial instruments in the financial statements.

Derivatives embedded in other financial instruments are separated from the host contract and accounted for separately if their economic characteristics and risks are not closely related to those of the host contract; the terms of the embedded derivatives would meet the definition of a derivative if it was a free standing instrument, the combined contract is not designated as FVTPL and recorded at fair value, and the host contract is not an asset in the scope of IFRS 9. These embedded derivatives are classified as part of the host instrument and measured at fair value with changes therein recognized on the Consolidated Statement of Income.

Accrued interest receivable is recorded in other assets and accrued interest payable is recorded in accounts payable and accrued liabilities. Interest income or expense is recorded in interest income or interest expense, as applicable.

3. Significant Accounting Policies (continued):

(b) Financial instruments – recognition and measurement (continued):

Hedge accounting

FirstOntario formally documents all relationships between hedging instruments and hedged items; as well as risk management objectives and strategies for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities recognized on the Consolidated Statement of Financial Position or specific firm commitments or forecasted transactions that are highly probable to occur and prevent exposure to variations in cash flows that could ultimately affect reported net income. FirstOntario also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items attributable to the hedged risk. FirstOntario designates its interest rate hedge agreements as hedges of the underlying financial instrument.

IFRS specifies the criteria that must be satisfied in order for hedge accounting to be applied and prescribes the accounting treatment for those permitted hedging strategies applicable to FirstOntario – fair value hedges and cash flow hedges.

In a fair value hedge, the change in fair value of the hedging derivative is offset on the Consolidated Statement of Income by the change in fair value of the hedged item relating to the hedged risk. FirstOntario utilizes fair value hedges primarily to convert fixed rate financial assets and liabilities to floating rate. The main financial instruments designated in fair value hedging relationships are loans and mortgages. If the derivative expires or is sold, terminated or exercised, no longer meets the criteria for fair value hedge accounting, or the designation is revoked, hedge accounting is discontinued prospectively. The fair value of the hedged item related to the hedged risk is reported as other assets. The fair value of the hedging instrument is recorded as a derivative asset or liability.

In a cash flow hedge, the effective portion of changes in fair value of the derivative is recognized in other comprehensive income ("OCI") and presented in the cash flow hedging reserve in equity. The amount recognized in OCI is reclassified and included on the Consolidated Statement of Income in the same period that the hedged cash flows affect income. This will be offset by net interest income on assets and liabilities that are hedged. FirstOntario utilizes cash flow hedges primarily to convert floating rate assets and liabilities to fixed rate. Any hedge ineffectiveness is measured and is immediately recognized in the Consolidated Statement of Income.

When either a fair value or cash flow hedge is discontinued, any cumulative adjustment to either the hedged item or other comprehensive income (loss) is recognized in income over the remaining term of the original hedge (fair value hedge) and as the hedged item impacts earnings (cash flow hedge) or immediately if the forecast transaction is no longer expected to occur.

3. Significant Accounting Policies (continued):

(c) Loan securitizations:

FirstOntario securitizes residential mortgages and commercial loans by legally selling them to funding partners. Securitized assets are assessed for derecognition under IFRS 9. When the derecognition criteria are met, the assets are derecognized from the Consolidated Statement of Financial Position.

Securitized residential mortgages that are assessed under IFRS 9 generally do not meet derecognition requirements as substantially all of the risks and rewards of the loans are held with FirstOntario. As a result, these loans are reported on the Consolidated Statement of Financial Position. Certain securitized residential mortgages subsequently met the derecognition criteria through the transfer of certain risks and rewards to external parties.

Commercial loans sold met the derecognition requirements and are not reported on the Consolidated Statement of Financial Position as substantially all of the risks and rewards of the loan are transferred to the funding partner and FirstOntario has received consideration in exchange. For those commercial loans sold, no gain is recorded as the consideration received is equivalent to the carrying value of the asset.

Revenue from servicing loans and mortgages is recorded as the services are provided.

(d) Cash and cash equivalents:

Cash and cash equivalents includes cash on hand, current accounts, short term deposits with other financial institutions, cheques and other items in transit. They are carried at amortized cost in the Statement of Financial Position.

(e) Investments:

Investments include debt investment securities measured at amortized cost, debt and equity investment securities mandatorily measured at FVTPL or designated as at FVTPL, and equity investment securities designated as at FVOCI.

(f) Intangible assets:

Computer software that is not an integral part of other property is accounted for as intangible assets. Computer software is stated at cost less accumulated amortization and accumulated impairment losses and is presented as part of fixed assets in the Consolidated Statement of Financial Position. Amortization of computer software is calculated by applying the straight-line method at rates based on estimated useful lives between 3 and 14 years. Amortization methods and useful lives are reviewed at each reporting date and adjusted if appropriate.

3. Significant Accounting Policies (continued):

(g) Fixed assets:

Fixed assets are stated at cost less accumulated amortization and accumulated impairment losses. When parts of an item of fixed assets have different useful lives, they are accounted for as separate items (major components) of fixed assets. Amortization is based on the cost of an asset less its residual value. Major components are amortized separately. Land is not amortized. Amortization on buildings and equipment is recognized in net income using the straight-line method at rates based on the estimated useful lives of the related assets and components as follows:

Asset	
Buildings	20 – 40 years
Parking lots and site improvements	10 – 25 years
Equipment	3 – 10 years
Leasehold improvements	Shorter of useful life and term of lease + one renewal period

Amortization methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

(h) Leases:

At the inception of a contract, FirstOntario assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

FirstOntario, as a lessee, recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to branches or office premises.

The right-of-use asset is subsequently amortized using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, FirstOntario’s incremental borrowing rate. Generally, FirstOntario uses its incremental borrowing rate as the discount rate.

3. Significant Accounting Policies (continued):

(h) Leases (continued):

The lease liability is subsequently measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in FirstOntario's estimate of the amount expected to be payable under a residual value guarantee, if FirstOntario changes its assessment of whether it will exercise a purchase, extension or termination option or if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in net income if the carrying amount of the right-of-use asset has been reduced to zero.

FirstOntario presents right-of-use assets in fixed assets and lease liabilities in accounts payable and accrued liabilities in the Consolidated Statement of Financial Position.

FirstOntario has elected not to recognize right-of-use assets and lease liabilities for leases of low-value assets and short-term leases. FirstOntario recognizes the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

(i) Investment properties:

Investment properties are properties held for rental, development and/or for capital appreciation. These investment properties are initially measured at cost and subsequently at fair value with any change therein recognized in profit or loss. Investment properties primarily consist of land and buildings held under joint venture agreements.

(j) Shares:

Membership and investment shares are classified either as liabilities or Members' equity. Where shares are redeemable at the option of the Member, either on demand or on withdrawal from membership, the shares are classified as liabilities and are measured at amortized cost. Shares that are redeemable at the discretion of FirstOntario's Board of Directors are classified as equity.

(k) Dividends:

Dividends on shares classified as liabilities are reported as interest expense. Dividends on shares classified as equity are charged to retained earnings on the date at which distributions are declared payable by the Board of Directors. All dividends on shares are deductible for income tax purposes.

3. Significant Accounting Policies (continued):

(l) Impairment of non-financial assets:

Non-financial assets other than deferred tax assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable at each reporting date. An impairment loss is recognized for the amount by which the asset's carrying value exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Impairment losses are recognized in net income.

Non-financial assets that have incurred impairment losses in prior years are reviewed for possible reversal of the impairment loss at each reporting date. A reversal of impairment is limited to the original impaired amount.

(m) Revenue recognition:

Loan interest and revenue is recognized in the Consolidated Statement of Income using the effective interest method. Refer to Note 3(b) for a detailed explanation of the effective interest rate method. Fee and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the effective interest rate.

FirstOntario enters into contracts with Members to provide banking services and is under agency contracts to provide access to credit card and insurance products, and investment advisory services to its Members. These contracts outline the terms and conditions for the services provided and a corresponding schedule that details the fee and commission for each performance obligation and when it is to be received. These revenues are recognized as the related services are performed.

(n) Foreign exchange:

The Consolidated Financial Statements are presented in Canadian dollars, which is FirstOntario's functional currency. Monetary assets and liabilities denominated in foreign currencies, primarily US dollars, are translated into Canadian dollars at exchange rates prevailing at the year-end. Fixed assets and intangible assets are carried at the historical Canadian dollar cost. Income and expenses are translated at the exchange rates in effect on the date of the transactions. Exchange gains and losses arising on the translation of monetary assets and liabilities are included in other income.

3. Significant Accounting Policies (continued):

(o) Provisions:

A provision is recognized if, as a result of a past event, FirstOntario has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

(p) Employee retirement benefits:

FirstOntario provides retirement benefits to certain employees. These benefits include registered pension plans, medical benefits, dental care and life insurance.

A defined contribution plan is a pension plan under which FirstOntario pays contributions to a separate entity. FirstOntario has no legal or constructive obligation to pay further contributions after its payment of a contribution in accordance with the pension plan. Defined contribution pension plan contributions are expensed in the period during which services are rendered by employees.

A defined benefit plan is a pension plan that defines the amount of the pension benefit that an employee will receive upon retirement, usually dependent on one or more factors, such as age, years of service and compensation. Employment retirement benefits include both pension and other post-retirement benefits.

FirstOntario’s net obligation in respect of defined benefit plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in the current and prior periods, discounting that amount and deducting the fair value of any plan assets.

The calculation of defined benefit obligations is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a potential asset for FirstOntario, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. To calculate the present value of economic benefits, consideration is given to any applicable minimum funding requirements.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognized immediately in OCI. FirstOntario determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognized in salaries and benefits in net income.

3. Significant Accounting Policies (continued):

(p) Employee retirement benefits (continued):

When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognized immediately in net income. FirstOntario recognizes gains and losses on the settlement of a defined benefit plan when the settlement occurs.

(q) Income taxes:

FirstOntario follows the asset and liability method of accounting for income taxes, whereby FirstOntario recognizes both the current and future income tax consequences of all transactions that have been recorded in the financial statements.

Current income taxes are the expected taxes refundable or payable on the taxable income for the year using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to taxes payable in respect of previous years. Current tax liabilities are classified as measured at amortized cost under IFRS 9.

Deferred income taxes provide for temporary differences between the carrying values of assets and liabilities and the amounts used for taxation purposes. The amount of deferred income tax provided is based on the expected timing of realization or settlement of the carrying value of assets and liabilities, using tax rates enacted or substantively enacted at the reporting period date. A deferred income tax asset is recognized only to the extent that it is probable that future taxable income will be available to utilize taxable benefits associated with the temporary difference in carrying value.

Deferred tax assets and liabilities are included either in other assets or accounts payable and accrued liabilities, as applicable, in the Consolidated Statement of Financial Position.

(r) Business Combinations:

Business combinations are accounted for using the acquisition method of accounting. For every business combination, an acquirer is identified, which is the entity that obtains control of the other entity. The effective date of the business combination is the date the acquirer gains control of the acquired entity. The identifiable assets (including previously unrecognized intangible assets) and identifiable liabilities (including contingent liabilities but excluding future restructuring costs) of the acquired entity are measured at fair value. The excess of the consideration transferred over the fair values of the identifiable net assets is recognized as contributed surplus.

Acquisition related costs are expensed as incurred and are included in operating expenses.

4. New Standards and Interpretations not yet effective:

Future changes in accounting policy:

On May 18, 2017 the IASB issued *IFRS 17 Insurance Contracts*. On March 17, 2020 the IASB announced the deferral of the effective date to annual periods beginning on or after January 1, 2023.

IFRS 17 will replace IFRS 4 Insurance Contracts.

This standard introduces consistent accounting for all insurance contracts. The standard requires a company to measure insurance contracts using updated estimates and assumptions that reflect the timing of cash flows and any uncertainty relating to insurance contracts. Additionally, IFRS 17 requires a company to recognize profits as it delivers insurance services, rather than when it receives premiums.

FirstOntario intends to adopt IFRS 17 in its financial statements for the annual period beginning on January 1, 2023. The extent of the impact of adoption of the standard has not yet been determined.

5. Loans Receivable from Members:

Loans receivable from Members, which are classified as amortized cost or FVTPL, are as follows:

(In thousands of dollars)	2020	2019
Residential mortgage loans	$ 3,350,826	$ 3,081,658
Allowance for expected credit losses	(735)	(1,033)
	3,350,091	3,080,625
Personal loans	96,471	105,275
Allowance for expected credit losses	(1,209)	(1,685)
	95,262	103,590
Commercial loans	809,479	799,384
Allowance for expected credit losses	(8,093)	(5,718)
	801,386	793,666
	$ 4,246,739	$ 3,977,881

FirstOntario classifies residential mortgage loans that do not meet the business model assessment of held to collect as FVTPL. At December 31, 2020, FirstOntario has classified $nil (2019 - $nil) residential mortgage loans as measured at FVTPL.

Certain residential mortgage loans are securitized and have been legally transferred to other entities for funding purposes. These loans are administered by FirstOntario and recognized on the Consolidated Statement of Financial Position to the extent of FirstOntario's continuing involvement.

A summary of the carrying values of residential mortgage loans is as follows:

(In thousands of dollars)	2020	2019
Loans held by FirstOntario	$ 2,850,827	$ 2,567,267
Loans held by Securitization Trusts	499,999	514,391
	$ 3,350,826	$ 3,081,658

Additional details are provided in Note 8 related to FirstOntario's securitization activity.

Interest income for the year is as follows:

(In thousands of dollars)	2020	2019
Residential mortgage loans	$ 106,903	$ 99,732
Personal loans	5,966	6,477
Commercial loans	36,977	38,448
	$ 149,846	$ 144,657

5. Loans Receivable from Members (continued):

Total fees paid to third parties associated with lending activities capitalized in other assets were $10,135,000 as at December 31, 2020 (2019 - $9,045,000). Charges amortized into interest expense in respect of these fees were $5,636,000 during the year ended December 31, 2020 (2019 - $5,945,000).

The following summarizes FirstOntario's loan portfolio by the contractual repricing or maturity date, whichever is earlier:

(In thousands of dollars)	**2020 Principal Balance**	**2020 Average Yield**	2019 Principal Balance	2019 Average Yield
Floating	**$ 575,665**	**4.11%**	$ 589,821	5.12%
Within 1 year	**921,536**	**4.00%**	839,579	4.39%
Over 1 year	**2,759,575**	**3.42%**	2,556,917	3.61%
	4,256,776	**3.64%**	3,986,317	4.00%
Allowance for expected credit losses (note 6)	**(10,037)**			(8,436)
	$ 4,246,739		$ 3,977,881	

6. Allowance for Expected Credit Losses:

FirstOntario applies the three stage approach to measure the allowance for expected credit losses, using the ECL approach as required under IFRS 9. The allowance is calculated based on the stage in which the financial asset falls at the reporting date. The financial assets migrate through the three stages based on the change in their risk of default since initial recognition.

ECL calculations are outputs of an ECL model with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. The ECL impairment model reflects the present value of all expected cash shortfalls related to default events either (i) over the following twelve months or (ii) over the expected life of the financial instrument, depending on the credit deterioration since its inception. The model reflects an unbiased, probability-weighted credit loss which considers multiple scenarios based on reasonable and supportable information about past events, current conditions and forecasts of future economic conditions. Forward looking information is explicitly incorporated into the estimation of ECL.

6. Allowance for Expected Credit Losses(continued):

The three stages of the allowance for expected credit losses are:

Stage 1 – Where there has not been a significant increase in credit risk ("SICR") since initial recognition of a financial asset, an amount equal to 12 months ECL is recorded. The ECL is computed using a probability of default ("PD") occurring over the next 12 months.

Stage 2 – When a financial asset experiences a SICR subsequent to initial recognition but is not considered to be in default, it is included in Stage 2. This requires the computation of ECL based on the PD over the remaining estimated life of the financial asset.

Stage 3 – Financial assets that are considered to be in default are included in this stage. Similar to Stage 2, the allowance captures lifetime ECL.

The probability of default, exposure at default ("EAD"), and loss given default ("LGD") are inputs used to estimate the ECL, and are modelled based on macroeconomic factors that are closely related with credit losses in the relevant portfolios, and are probability weighted using three scenarios. The measurement of ECL is based primarily on the product of the three variables:

- PD is an estimate of the likelihood of default over a given time horizon
- EAD is the expected exposure (balance of the loan plus accrued interest) in the event of default at a future default date
- LGD is an estimate of the loss arising where a default occurs at a given time and is based on the difference between the contractual cash flows due and those that FirstOntario would expect to receive, including from the realization of any collateral.

Assessment of significant increase in credit risk

The measurement of ECL for each stage and the assessment of SICR considers information about past events and current conditions as well as supportable forecasts of future events and economic conditions. The estimation and application of forward-looking information ("FLI") requires significant judgement. FirstOntario relies on a broad range of FLI's, such as expected real GDP, unemployment rates, house price indices, interest rates and debt ratios. The inputs used in the model for calculating ECL may not always capture all characteristics of the market at the reporting date. To capture portfolio characteristics and risks, adjustments are made using management judgement.

When determining whether the risk of default on a financial asset has increased significantly since initial recognition, FirstOntario considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on FirstOntario's historical experience and expert credit assessment, delinquency and monitoring, and macroeconomic outlook including FLI. There is a rebuttable presumption that the risk of default has increased since initial recognition when contractual payments are more than 30 days overdue.

6. Allowance for Expected Credit Losses (continued):

A summary of the loan allowance for expected credit losses is as follows:

(In thousands of dollars)	12-month ECL (Stage 1)	Lifetime ECL-Non-credit Impaired (Stage 2)	Lifetime ECL-Credit Impaired (Stage 3)	2020 Total
Balance at beginning of year	$ 3,421	$ 1,243	$ 3,772	$ 8,436
Transfer to (from):				
Stage 1	606	(336)	(270)	-
Stage 2	(689)	701	(12)	-
Stage 3	(37)	(21)	58	-
Re-measurement	(101)	3,463	5,536	8,898
Originations	1,855	-	50	1,905
Loans derecognized	(1,010)	(382)	(3,391)	(4,783)
Loans written-off	-	-	(4,591)	(4,591)
Recoveries	-	-	172	172
Balance at end of year	$ 4,045	$ 4,668	$ 1,324	$ 10,037

Provision for impaired loans amounting to $5,970,000 (2019 - $3,297,000) is comprised of ECL related to re-measurement changes of $8,898,000 (2019 - $4,281,000), loan originations of $1,905,000 (2019 - $1,594,000), less the recognized ECL balance from Creative Arts of $50,000 and loans derecognized of $4,783,000 (2019 - $2,578,000).

(In thousands of dollars)	12-month ECL (Stage 1)	Lifetime ECL-Non-credit Impaired (Stage 2)	Lifetime ECL-Credit Impaired (Stage 3)	2019 Total
Balance at beginning of year	$ 3,024	$ 940	$ 4,142	$ 8,106
Transfer to (from):				
Stage 1	355	(326)	(29)	-
Stage 2	(112)	118	(6)	-
Stage 3	(79)	(16)	95	-
Re-measurement	(100)	817	3,564	4,281
Originations	1,594	-	-	1,594
Loans derecognized	(1,261)	(290)	(1,027)	(2,578)
Loans written-off	-	-	(3,220)	(3,220)
Recoveries	-	-	253	253
Balance at end of year	$ 3,421	$ 1,243	$ 3,772	$ 8,436

(In thousands of dollars)	Residential Mortgage Loans	Personal Loans	Commercial Loans	2020 Total
Balance at beginning of year	$ 1,033	$ 1,685	$ 5,718	$ 8,436
Loans written off	-	(538)	(4,053)	(4,591)
Recoveries	-	150	22	172
Recognized ECL balances from Creative Arts	-	50	-	50
Net provision for loan allowance	(298)	(138)	6,406	5,970
Balance at end of year	$ 735	$ 1,209	$ 8,093	$ 10,037

6. Allowance for Expected Credit Losses (continued):

(In thousands of dollars)	Residential Mortgage Loans	Personal Loans	Commercial Loans	2019 Total
Balance at beginning of year	$ 886	$ 1,645	$ 5,575	$ 8,106
Loans written off	-	(470)	(2,750)	(3,220)
Recoveries	-	149	104	253
Net provision for loan allowance	147	361	2,789	3,297
Balance at end of year	$ 1,033	$ 1,685	$ 5,718	$ 8,436

A summary of impaired loans is as follows:

(In thousands of dollars)	**Residential Mortgage Loans**	**Personal Loans**	**Commercial Loans**	**2020 Total**	2019 Total
Gross amount of loans identified as impaired	**$ 15,280**	**$ 425**	**$ 8,141**	**$ 23,846**	$ 48,026
Related security less expected costs	**15,037**	**79**	**7,406**	**22,522**	44,254
ECL	**$ 243**	**$ 346**	**$ 735**	**$ 1,324**	$ 3,772

A summary of loans past due but not impaired is as follows:

(In thousands of dollars)	**<30 days**	**30-59 days**	**60-89 days**	**2020 Total**	2019 Total
Residential mortgage loans	**$ 36,660**	**$ 9,268**	**$ 1,473**	**$ 47,401**	$ 72,675
Personal loans	**1,652**	**253**	**112**	**2,017**	3,633
Commercial loans	**3,223**	**-**	**-**	**3,223**	1,605
Balance at end of year	**$ 41,535**	**$ 9,521**	**$ 1,585**	**$ 52,641**	$ 77,913

The carrying amount of loans that were renegotiated during the year that otherwise would have been listed as past due greater than 90 days were $nil (2019 - $nil).

FirstOntario's commercial loan portfolio contains Member concentration risk, whereby a large amount of the loans are connected to certain individuals. Collectively, the largest five commercial Members by loan dollar value are associated with approximately 18% (2019 - 19%) of the commercial loan portfolio.

6. Allowance for Expected Credit Losses (continued):

FirstOntario's commercial loan portfolio consists of the following industry sectors:

	2020	2019
Hospitality	**25%**	23%
Retail & Commercial Buildings	**56%**	59%
Other	**19%**	18%

Collateral

There are documented policies and procedures in place for the valuation of financial and non-financial collateral. The fair value of non-financial collateral is updated if there has been a significant change in the terms and conditions of the loan and (or) the loan is considered impaired. For impaired loans, an assessment of the collateral is taken into consideration when estimating the expected future cash flows and net realizable amount of the loan.

The amount and type of collateral and other credit enhancements required depend upon FirstOntario's assessment of counterparty credit quality and repayment capacity. FirstOntario complies with industry standards for collateral valuation, frequency of recalculation of the collateral requirements, documentation, registration and perfection procedures, and monitoring. Non-financial assets accepted by FirstOntario as collateral include vehicles, residential real estate, real estate under development, commercial real estate and certain business assets (accounts receivable, inventory, and fixed assets). Financial collateral includes cash and negotiable securities issued by governments and investment grade issuers. Guarantees are also accepted to reduce credit risk.

At December 31, 2020, the related security less expected costs of credit impaired loans amounted to $22,522,000 (2019 - $44,254,000) and the value of identifiable collateral held against those loans amounted to $22,902,000 (2019 - $46,568,000). For each loan, the value of disclosed collateral is capped to the nominal amount of the loan that it is held against.

6. Allowance for Expected Credit Losses (continued):

The following table illustrates the credit quality of loans:

(In thousands of dollars)	12-month ECL (Stage 1)	Lifetime ECL- Non-credit Impaired (Stage 2)	Lifetime ECL- Credit Impaired (Stage 3)	2020	2019
Retail Mortgages and Personal Loans					
Unscored	**$ 26,872**	**$ 465**	**$ 129**	**$ 27,466**	$ 24,529
A+	**933,412**	**337**	**3**	**933,752**	764,753
A	**1,907,380**	**3,859**	**4,547**	**1,915,786**	1,713,922
B	**218,953**	**796**	**2,593**	**222,342**	255,655
C	**197,142**	**10,755**	**1,655**	**209,552**	251,255
D	**61,577**	**22,014**	**1,125**	**84,716**	107,660
E	**17,895**	**30,075**	**5,713**	**53,683**	69,159
Commercial Loans					
Undoubted	**8,561**	**-**	**-**	**8,561**	239
Superior	**25,415**	**-**	**-**	**25,415**	26,140
Satisfactory	**646,554**	**120,808**	**-**	**767,362**	748,505
Watch list	**-**	**-**	**8,141**	**8,141**	24,500
Gross loan balance	**4,043,761**	**189,109**	**23,906**	**4,256,776**	3,986,317
Allowance for impairment loans	**(4,045)**	**(4,668)**	**(1,324)**	**(10,037)**	(8,436)
Carrying amount	**$ 4,039,716**	**$ 184,441**	**$ 22,582**	**$4,246,739**	$3,977,881

Refer to Note 17 – Financial Risk Management for a detailed explanation of the credit risk rating process of both portfolios.

7. Cash and Cash Equivalents:

(In thousands of dollars)	2020	2019
Cash on hand	**$ 19,435**	$ 10,861
Cash at Central 1	**6,613**	13,620
Other cash and cash equivalents	**844**	1,231
Total cash and cash equivalents	**$ 26,892**	$ 25,712

8. Loan Securitizations:

FirstOntario enters into transactions in the normal course of business by which it transfers recognized financial assets directly to third parties or Special Purpose Entities ("SPE's"). FirstOntario securitizes mortgage backed securities through programs sponsored by the Canada Mortgage and Housing Corporation and other third party programs.

8. Loan Securitizations (continued):

Certain transactions allow FirstOntario to transfer its contractual right to receive cash flows from the financial assets, or retain the right but assume an obligation to pass on the cash flows from the asset, and transfer substantially all the risks and rewards of ownership. The risks include credit, interest rate, prepayment and other price risks. Under these conditions, the residential or commercial mortgages included in the mortgage backed security meet the qualifications required to be derecognized under IFRS.

Residential and commercial mortgages that have been derecognized are those that meet the qualifications required to be derecognized under IFRS.

The following table summarizes FirstOntario's securitization activity during the years ended December 31, 2020 and December 31, 2019:

	2020		2019	
(In thousands of dollars)	**Residential Mortgages**	**Commercial Mortgages**	Residential Mortgages	Commercial Mortgages
Amount securitized/sold	**$ 146,060**	**$ 783,856**	$ 170,759	$ 536,427
Net cash proceeds received	**141,748**	**781,926**	167,858	532,785
Outstanding balances of securitized loans	**901,726**	**2,671,055**	1,221,306	2,152,193

The following table summarizes the balances for securitized loans that are not recorded on the Consolidated Statement of Financial Position:

	2020		2019	
(In thousands of dollars)	**Residential Mortgages**	**Commercial Mortgages**	Residential Mortgages	Commercial Mortgages
Retained rights and receivables	**$ 1,739**	**$ 14,054**	$ 5,131	$ 34,324
Outstanding balances of off-balance sheet securitized loans	**401,727**	**2,671,055**	706,915	2,152,193

Retained rights are reported as investments on the Consolidated Statement of Financial Position (Note 9). The following table summarizes the weighted average key assumptions at the date of off-balance sheet securitization for retained rights related to all residential and commercial mortgages sold and derecognized under IFRS 9.

	2020	2019
Average life	**4.0 years**	4.6 years
Prepayment rate	**0.00%**	0.00%
Discount rate	**1.87%**	2.09%
Expected credit losses	**0.00%**	0.00%

9. Investments:

Investments are as follows:

(In thousands of dollars)		2020		2019
Equity securities measured at FVOCI:				
Shares – Central 1 (c)	**$**	**19,611**	$	19,610
Preferred shares		**2,009**		2,009
Equity securities measured at FVTPL:				
Managed funds (b)		**100,720**		94,939
Investments– other		**7,715**		6,260
Debt securities measured at FVTPL:				
Retained rights – loan securitizations		**15,793**		39,455
Debt securities measured at amortized cost:				
Liquidity reserve deposits (e)		**304,322**		275,341
Loans (f)		**11,912**		18,028
Investments measured under IFRS 9		**462,082**		455,642
Real estate joint ventures (d)		**97,679**		84,262
Other investments		**131**		218
	$	**559,892**	$	540,122

The following summarizes FirstOntario's investments by the contractual repricing or maturity date, whichever is earlier:

(In thousands of dollars)	**2020** Carrying Amount	**2020** Average Yield	2019 Carrying Amount	2019 Average Yield
Within 1 year	**$ 304,660**	**0.01%**	$ 66,889	1.36%
Over 1 year (f)	**11,510**	**10.85%**	224,665	2.55%
	316,170	**0.41%**	291,554	2.28%
Non-rate sensitive	**243,658**		246,753	
Accrued interest	**64**		1,815	
	$ 559,892		$ 540,122	

(a) Income earned on equity securities designated as at FVOCI:

(In thousands of dollars)		2020		2019
Interest and investment income	**$**	**1,033**	$	569

9. Investments (continued):

(b) Managed funds:

FirstOntario holds certain investments within actively managed investment funds issued by external investment providers. Given the investments are actively managed by investment advisors, these investments are held for trading and are measured at FVTPL.

(In thousands of dollars)		**2020**		2019
Fair value at the beginning of year	**$**	**94,939**	$	76,830
Additions to portfolio		**9,078**		25,732
Disposals from portfolio		**(6,102)**		(9,871)
Distributions		**(6,531)**		(4,075)
Change in fair value		**9,630**		8,169
Change from foreign exchange		**(294)**		(1,846)
Fair value at the end of year	**$**	**100,720**	$	94,939

(c) Central 1 shares:

As a member of Central 1, FirstOntario is required to maintain an investment in Central 1 shares based on FirstOntario's asset size relative to other Class A members. Central 1 rebalances their shares annually. During 2020, as part of this share rebalancing, FirstOntario was required to purchase 28,194 (2019 - 368) Class A shares and nil (2019 - 1,301,867) Class F shares; and return nil (2019 – nil) Class A shares and 99,282 (2019 – nil) Class F shares. As part of the Creative Arts Financial acquisition (Note 23), FirstOntario acquired 6,590 Class A shares and 65,304 Class F shares. FirstOntario received $939,000 (2019 - $475,000) in dividends in 2020.

The following table summarizes the investment in Central 1 Shares as at December 31, 2020:

(In thousands of dollars)		**2020**		2019
1,553,335 Class A Shares (2019 – 1,518,551)	**$**	**1,553**	$	1,519
39,736 Class E Shares (2019 - 39,736)		**3,974**		3,974
14,083,990 Class F Shares (2019 - 14,117,968)		**14,084**		14,117
	$	**19,611**	$	19,610

FirstOntario has designated the Central 1 shares as measured at FVOCI as FirstOntario intends to hold these shares for the long term.

Central 1 requires member credit unions to maintain with them liquidity and secondary liquidity reserve deposits equal to 6% of the member credit union's assets. These reserve deposits were determined on a monthly basis and are classified as measured at amortized cost. Effective January 1, 2021, Central 1 eliminated this requirement as part of the terms of membership.

9. Investments (continued):

(d) Real estate joint ventures:

FirstOntario periodically enters into agreements with third parties to jointly control investment properties. These joint ventures are initially measured at cost and subsequently at fair value with any change therein recognized in profit or loss. Costs include initial acquisition costs and other costs incurred prior to the real estate being ready for its intended use.

(In thousands of dollars)		**2020**		2019
Balance at the beginning of year	**$**	**84,262**	$	87,465
Acquisitions		**19,374**		23,403
Earnings from joint ventures		**330**		1,649
Distributions		**(10,628)**		(39,629)
Change in fair value		**4,340**		11,374
Balance at the end of year	**$**	**97,679**	$	84,262

FirstOntario's portion of the revenue and expenses from participation in the ventures has been included in other income as follows:

(In thousands of dollars)		**2020**		2019
Revenues	**$**	**8,475**	$	8,076
Expenses		**8,145**		6,427
Earnings from joint ventures	**$**	**330**	$	1,649

Revenue of the joint ventures includes interest received by FirstOntario from a promissory note issued to one of its partners in the amount of $142,000 (2019 - $32,000). The expenses of the joint ventures included amortization in the amount of $1,821,000 (2019 - $1,585,000). Operating cash flow generated by the ventures was $1,089,000 (2019 - $1,252,000). During the year ended December 31, 2020, FirstOntario received $10,628,000 (2019 - $39,629,000) in total distributions from the ventures. Of the 2020 distributions, $8,572,000 (2019 - $38,377,000 related to refinancing of two joint ventures) related to the refinancing of three joint ventures, whereby FirstOntario received a return of capital and the capital was replaced with debt financing.

9. Investments (continued):

(d) Real estate joint ventures (continued):

Investments properties held under the ventures is as follows:

(In thousands of dollars)		**2020**		2019
Real estate held at fair value for investment purposes	**$**	**89,609**	$	70,548
Construction in progress		**8,070**		13,714
Balance at the end of year	**$**	**97,679**	$	84,262

Fair value was determined by experienced registered independent appraisers having an appropriate recognized professional qualification. The fair value measurement for all of the joint ventures has been categorized as a level 3 fair value based on the inputs of the valuation technique used (see Note 18).

Joint venture values were based on the appraiser's opinion of value having undertaken the following approaches:

- The Income Approach method where the investment is expected to be acquired by an investor basing criteria on an expected income flow.
- The Direct Comparison Approach method which determines the market range of unit prices demonstrated by the sales or listings of comparable properties.

Below is a summary of the significant unobservable inputs used in the modeling process:

	2020	2019
Capitalization rate	**4.8% - 7.8%**	5.5% - 7.3%
Risk-adjusted discount rate	**7.5% - 8.5%**	8.0%
Occupancy rate	**96% - 98%**	95% - 99%

Other significant unobservable inputs are the expected market rental growth rate and the rent-free periods.

The estimated fair value of the joint ventures would increase (decrease) as a result of the following changes in the significant unobservable inputs:

	Change
Capitalization rate	lower (higher)
Risk-adjustment discount rate	lower (higher)
Occupancy rate	higher (lower)
Void periods	shorter (longer)
Expected market rental growth	higher (lower)
Rent-free periods	shorter (longer)

9. Investments (continued):

(e) Liquidity reserve deposits:

During 2020, FirstOntario entered into an arrangement with Central 1 Credit Union to liquidate its liquidity reserve deposits. The price was set on December 31, 2020 at fair market value, and consideration was provided by Central 1 Credit Union in the form of marketable fixed income securities of equivalent value on January 4, 2021. As a result of the adjustments in timing of receipt of cash flows, FirstOntario recorded an accounting gain of $7.9 million, reflecting the difference between the carrying cost of liquidity reserve deposits and the price determined on December 31, 2020.

(f) Loans:

FirstOntario invests in a portfolio of short-term, low value personal loans, originated by a third party as follows:

(In thousands of dollars)		**2020**		2019
Principal loan balance	**$**	**12,279**	$	18,458
Accrued interest		**64**		96
Allowance for expected credit losses		**(431)**		(526)
Balance at the end of year	**$**	**11,912**	$	18,028

10. Fixed Assets:

(In thousands of dollars)		Cost		Accumulated amortization		2020 Net book value
Land	**$**	**1,321**	**$**	**-**	**$**	**1,321**
Parking lots/Site improvements		**348**		**285**		**63**
Buildings		**26,200**		**8,377**		**17,823**
Equipment		**25,292**		**17,729**		**7,563**
Leasehold improvements		**23,643**		**13,941**		**9,702**
Tangible assets		**76,804**		**40,332**		**36,472**
Intangible assets (software)		**36,815**		**17,182**		**19,633**
Total fixed assets	**$**	**113,619**	**$**	**57,514**	**$**	**56,105**

(In thousands of dollars)		Cost		Accumulated amortization		2019 Net book value
Land	$	1,321	$	-	$	1,321
Parking lots/Site improvements		348		271		77
Buildings		25,959		5,998		19,961
Equipment		23,929		15,557		8,372
Leasehold improvements		22,380		12,132		10,248
Tangible assets		73,937		33,958		39,979
Intangible assets (software)		32,733		15,012		17,721
Total fixed assets	$	106,670	$	48,970	$	57,700

Amortization in respect of the above assets for the year ended December 31, 2020 amounts to $8,875,000 (2019 - $8,564,000).

10. Fixed Assets (continued):

Reconciliations of the net book value for each class of fixed asset are summarized below:

(In thousands of dollars)		2020		2019
Land				
Net book value at the beginning and end of the year	**$**	**1,321**	$	1,321
Parking lots/Site improvements				
Net book value at the beginning of the year		**77**		90
Amortization		**(14)**		(13)
Net book value at the end of the year		**63**		77
Buildings				
Net book value at the beginning of the year		**19,961**		3,052
IFRS 16 adjustment (note 11)		**-**		19,248
Additions		**796**		169
Disposals		**(385)**		-
Amortization		**(2,549)**		(2,508)
Net book value at the end of the year		**17,823**		19,961
Equipment				
Net book value at the beginning of the year		**8,372**		6,332
IFRS 16 adjustment (note 11)		**-**		988
Additions		**1,556**		3,386
Disposals		**(32)**		(26)
Amortization		**(2,333)**		(2,308)
Net book value at the end of the year		**7,563**		8,372
Leasehold improvements				
Net book value at the beginning of the year		**10,248**		11,057
Additions		**1,263**		984
Amortization		**(1,809)**		(1,793)
Net book value at the end of the year		**9,702**		10,248
Intangible assets (software)				
Net book value at the beginning of the year		**17,721**		17,257
Additions		**4,082**		2,391
Amortization		**(2,170)**		(1,927)
Net book value at the end of the year		**19,633**		17,721
Total net book value	$	**56,105**	$	57,700

11. Leases:

Leases:

FirstOntario leases space for most of its branches and some computer equipment. The leases have varying terms, escalation clauses and renewal rights.

When measuring lease liabilities for new leases, FirstOntario discounted lease payments using its average incremental borrowing rate at the start of the lease term. FirstOntario estimated its incremental borrowing rates for portfolios of leases with similar characteristics, such as similar risk profiles, same or similar types of security, and similar lease terms. For new leases entered into in 2020, FirstOntario applied an incremental borrowing rate of 2.98% (2019 – 2.98%).

Information about leases for which FirstOntario is a lessee is presented below.

(i) Right-of-use assets:

Right-of-use assets relate to leased branch and office premises and computer equipment that are presented within fixed assets (see Note 10).

(In thousands of dollars)		**2020**		2019
Opening Balance	**$**	**18,842**	$	20,236
Additions		**807**		1,352
Disposals		**(393)**		(26)
Amortization		**(2,803)**		(2,720)
Balance at end of year	**$**	**16,453**	$	18,842

(ii) Lease liabilities:

(In thousands of dollars)		**2020**		2019
Opening Balance	**$**	**19,149**	$	20,216
Additions		**416**		1,359
Interest on lease liabilities		**548**		581
Repayments		**(3,056)**		(3,007)
Balance at end of year	**$**	**17,057**	$	19,149

(iii) Maturity analysis for leased liabilities is detailed below. FirstOntario has included optional lease renewal periods where FirstOntario has assessed the likelihood of renewal as “reasonably certain”.

(In thousands of dollars)		**2020**		2019
Within 1 year	**$**	**2,961**	$	2,982
1 to 5 years		**10,263**		10,993
Over 5 years		**6,181**		7,708
Total undiscounted lease liabilities	**$**	**19,405**	$	21,683

11. Leases (continued):

(iv) Total cash outflows for leases are presented below. Non-lease payments represent variable payments for FirstOntario's branches and payments relating to warranties on FirstOntario's equipment.

(In thousands of dollars)	2020	2019
Payments on lease liabilities	$ 3,056	$ 3,007
Payments on low-value leases	240	201
Payments on short-term leases	10	196
Non-lease payments	1,344	1,193
Total cash outflows	$ 4,650	$ 4,597

12. Members' Deposits:

Members' deposits, which are classified as amortized cost, are as follows:

(In thousands of dollars)	2020	2019
Chequing	$ 513,966	$ 393,452
Savings	971,934	724,519
Term deposits	1,752,366	1,777,457
Registered plans	750,102	720,838
	$ 3,988,368	$ 3,616,266

Included in registered plans and term deposits are $5,182,000 in Equity-Linked Deposits at December 31, 2020 (2019 - $1,955,000). See Note 16 for the related derivatives used to hedge exposure to equity market risk.

Concentra Financial Services Association acts as the trustee for the majority of FirstOntario's tax deferred savings plans (registered retirement savings plans and registered retirement income funds). FirstOntario accepts deposits on behalf of the trustee and retains the funds deposited.

Interest expense for the year is as follows:

(In thousands of dollars)	2020	2019
Savings	$ 6,600	$ 8,640
Term deposits	45,999	46,558
Registered plans	15,356	15,329
	$ 67,955	$ 70,527

12. Members' Deposits (continued):

The following summarizes FirstOntario's Members' deposits by the contractual repricing or maturity date, whichever is earlier:

(In thousands of dollars)	**Principal Balance**	**2020 Average Yield**	Principal Balance	2019 Average Yield
Floating	**$ 1,041,989**	**0.64%**	$ 795,263	1.39%
Within 1 year	**1,435,866**	**2.23%**	1,394,641	2.53%
Over 1 year	**866,939**	**2.07%**	929,152	2.72%
	3,344,794	**1.69%**	3,119,056	2.29%
Non-rate sensitive	**643,574**		497,210	
	$ 3,988,368		$ 3,616,266	

13. Membership and Investment Shares:

Authorized Share Capital

FirstOntario has authorized an unlimited number of membership shares. Such shares are issued for $5 each and Members under the age of 21 must hold one membership share while those 21 and over are required to hold at least five shares and increase their holdings of membership shares to 30 shares over a 25 year period. Membership shares are redeemable, on withdrawal from membership, at the amount paid thereon provided FirstOntario is meeting the "capital adequacy" requirements (see Note 14) and they rank junior to Class A and Class B special shares for priority in the payment of dividends.

An unlimited number of Class A and Class B special shares. Such shares are generally non-voting and non-participating with non-cumulative dividend entitlements. In respect of dividends, both classes rank senior to the membership shares and the Class B special shares rank ahead of the Class A special shares.

The Board of Directors has authorized a Series 1, Series 2, Series 2013, Series 2010, Series 2015 and Series 2020 A and Series 2020 B for Class B special shares ("investment shares"). The investment shares have an issue price of $1 each and are entitled to receive dividends if, as and when declared by the Board of Directors. Series 1, Series 2 and Series 2013 investment shares are redeemable at the holder's request. Series 2010 and Series 2015 investment shares are redeemable at the sole and absolute discretion of the Board of Directors. Series 2020 A and Series 2020 B investment shares are redeemable at the sole and absolute discretion of the Board of Directors starting in 2025. In any year, redemptions are restricted to 10% of the respective series of the outstanding investment shares.

13. Membership and Investment Share (continued):

Issued and Outstanding

Membership shares and Series 1, 2 and 2013 investment shares are classified as liabilities and are measured at amortized cost. Dividends are recorded using the effective interest rate method. Series 2010, 2015 and 2020 investment shares are classified as equity as these shares are redeemable at the sole and absolute discretion of the Board of Directors.

(In thousands of dollars)		2020		2019
Membership shares				
1,826,197 (2019 - 1,741,464) membership shares	$	**9,131**	$	8,707
Investment shares				
4,830,138 (2019 - 4,976,560)				
Class B, Series 1, Special Shares		**4,830**		4,977
6,012,678 (2019 - 6,109,352)				
Class B, Series 2, Special Shares		**6,013**		6,109
889,129 (2019 - 962,545)				
Class B, Series 2013, Special Shares		**889**		963
Investment shares classified as liabilities		**11,732**		12,049
47,420,832 (2019 - 46,808,363)				
Class B, Series 2010, Special Shares		**47,175**		46,562
64,242,888 (2019 - 63,952,161)				
Class B, Series 2015, Special Shares		**63,989**		63,699
313,467 (2019 - nil)				
Class B, Series 2020 A, Special Shares		**313**		-
815,932 (2019 - nil)				
Class B, Series 2020 B, Special Shares		**816**		-
Investment shares classified as equity		**112,293**		110,261
Total investment shares	$	**124,025**	$	122,310

Dividends

Dividends earned by membership and investment shares classified as liabilities and expensed on the Consolidated Statement of Income were as follows:

(In thousands of dollars)		2020		2019
Membership shares	$	**623**	$	606
Series 1, 2 and 2013 investment shares		**510**		529
Dividends on membership and investment shares	$	**1,133**	$	1,135
Dividends on Series 2010 and 2015 shares (classified as equity)	$	**4,485**	$	4,340

13. Membership and Investment Share (continued):

On March 5, 2020, the Board of Directors approved the issue of 487,928 Series 1, 2 and 2013 investment shares, 1,895,608 Series 2010 investment shares and 2,589,654 Series 2015 investment shares in payment of a dividend for the 12 months from January 1, 2019 to December 31, 2019.

The tables that follow present a reconciliation of the change in shares during the year:

	2020	2019
Membership Shares		
Opening balance	**1,741,464**	1,842,545
Shares issued during the year	**126,014**	240,387
Merger with Creative Arts Financial	**8,237**	-
Actual shares redeemed	**(49,518)**	(74,844)
Inactive member shares cleanup[1]	**-**	(266,624)
Membership shares	**1,826,197**	1,741,464
Class B, Series 1, Special Shares		
Opening balance	**4,976,560**	5,214,168
Shares issued during the year	**201,540**	210,970
Shares redeemed	**(347,962)**	(448,578)
Class B, Series 1, Special Shares	**4,830,138**	4,976,560
Class B, Series 2, Special Shares		
Opening balance	**6,109,352**	6,263,230
Shares issued during the year	**247,411**	253,273
Shares redeemed	**(344,085)**	(407,151)
Class B, Series 2, Special Shares	**6,012,678**	6,109,352
Class B, Series 2013, Special Shares		
Opening balance	**962,545**	948,056
Shares issued during the year	**38,977**	38,099
Shares redeemed	**(112,393)**	(23,610)
Class B, Series 2013, Special Shares	**889,129**	962,545
Class B, Series 2010, Special Shares		
Opening balance	**46,808,363**	45,121,199
Shares issued during the year	**1,895,608**	1,821,488
Shares redeemed	**(1,283,139)**	(134,324)
Class B, Series 2010, Special Shares	**47,420,832**	46,808,363
Class B, Series 2015, Special Shares		
Opening balance	**63,952,161**	62,312,494
Shares issued during the year	**2,589,654**	2,518,578
Shares redeemed	**(2,298,927)**	(878,911)
Class B, Series 2015, Special Shares	**64,242,888**	63,952,161

13. Membership and Investment Share (continued):

	2020	2019
<u>Class B, Series 2020 A, Special Shares</u>		
Opening balance	**-**	-
Merger with Creative Arts Financial (Note 23)	**313,467**	-
Class B, Series 2020 A, Special Shares	**313,467**	-
<u>Class B, Series 2020 B, Special Shares</u>		
Opening balance	**-**	-
Merger with Creative Arts Financial (Note 23)	**815,932**	-
Class B, Series 2020 B, Special Shares	**815,932**	-

[1]During 2019, FirstOntario undertook a membership share cleanup. Those members who had only membership shares, with no loans and deposits and who could not be located, had their membership closed with the shares transferred to unclaimed balances. Members who had duplicate shares had excess membership shares redeemed and returned. In addition, there were members who did not have the required membership shares, those shares were funded by FirstOntario. The 2018 membership total disclosed in Note 1 has been restated.

14. Regulatory Reporting and Disclosure:

(a) Capital management:

FirstOntario maintains policies and procedures relative to capital management so as to ensure that capital levels are sufficient to cover risks inherent in the business.

FirstOntario's objectives when managing capital are:

(i) To ensure that the quantity, quality and composition of capital required reflects the inherent risks of FirstOntario and to support the current and planned operations and portfolio growth.

(ii) To provide a basis for confidence among Members, depositors, creditors and regulatory agencies.

(iii) To ensure that FirstOntario maintains a level of capital that sufficiently protects against unanticipated losses and to comply with the minimum regulatory capital requirements set out in the Act.

Regulatory capital is calculated as a percentage of total assets and of risk-weighted assets. Risk-weighted assets are calculated by applying risk weight percentages, as prescribed by the Act, to various asset categories, operational and interest rate risk criteria. The prescribed risk weights are dependent upon the degree of risk associated with the asset.

FirstOntario manages its Tier 1 and Tier 2 capital in accordance with internal policies and regulatory requirements. Tier 1 capital is the highest quality and consists of retained earnings, contributed surplus, accumulated other comprehensive losses, membership shares and the portion of the value of Class B investment shares that are not redeemable within 12 months.

14. Regulatory Reporting and Disclosure (continued):

(a) Capital management (continued):

Tier 2 capital is comprised of the value of Class B investment shares ineligible as Tier 1 capital and the eligible portion of the allowance for impaired loans.

The amount and composition of Tier 1 and Tier 2 capital were as follows:

(In thousands of dollars)	**2020**	2019
Tier 1 Capital		
Retained earnings	**$ 148,723**	$ 127,514
Contributed surplus	**5,474**	4,865
Membership shares	**9,131**	8,707
Class B Investment Shares, Series 1 (90%)	**4,347**	4,479
Class B Investment Shares, Series 2 (90%)	**5,412**	5,498
Class B Investment Shares, Series 2010 (90%)	**42,457**	41,906
Class B Investment Shares, Series 2013 (90%)	**800**	867
Class B Investment Shares, Series 2015 (90%)	**57,590**	57,329
Class B Investment Shares, Series 2020 A	**313**	-
Class B Investment Shares, Series 2020 B	**816**	-
Total Tier 1 Capital	**275,063**	251,165
Tier 2 Capital		
Class B Investment Shares, Series 1 (10%)	**483**	498
Class B Investment Shares, Series 2 (10%)	**601**	611
Class B Investment Shares, Series 2010 (10%)	**4,718**	4,656
Class B Investment Shares, Series 2013 (10%)	**89**	96
Class B Investment Shares, Series 2015 (10%)	**6,399**	6,370
Accumulated other comprehensive losses – employee benefit adjustments	**(3,524)**	(2,633)
Stage 1 and 2 ECL	**8,713**	4,664
Total Tier 2 Capital	**17,479**	14,262
Total Regulatory Capital	**$ 292,542**	$ 265,427
Total Assets	**$ 4,922,361**	$ 4,629,642
Total Risk Weighted Assets	**$ 2,268,224**	$ 2,267,461

Under the Regulations of the Act, FirstOntario must maintain minimum levels of regulatory capital. The leverage ratio calculates regulatory capital as a percentage of assets. The risk-weighted capital ratio calculates regulatory capital as a percentage of risk-weighted assets. FirstOntario complied with these requirements as follows:

	Regulatory Capital	Leverage Ratio Minimum	Leverage Ratio Actual	Risk-Weighted Capital Ratio Minimum	Risk-Weighted Capital Ratio Actual
2020	**$ 292,542,000**	**4.00%**	**5.94%**	**8.00%**	**12.90%**
2019	$ 265,427,000	4.00%	5.73%	8.00%	11.71%

14. Regulatory Reporting and Disclosure (continued):

(b) Remuneration of officers and employees:

The Act requires disclosure of the five highest paid officers and employees of FirstOntario where total remuneration exceeds $150,000 during the year. The individuals and their respective remuneration (salary, benefits including any applicable retirement and post-employment benefits) included Thomas Bijvoet, Former Chief Information Officer ($41,000, $688,000), Lloyd Smith, Chief Executive Officer ($647,000, $39,000), James Olson, Former President (nil, $481,000), Barry Doan, Chief Financial Officer ($428,000, $41,000) and David Schurman, Chief Operating Officer ($432,000, $36,000).

Remuneration is fair and competitive with salaries of similar positions at credit unions of approximately equal asset size used as comparators. FirstOntario actively participates in compensation surveys to ensure alignment with the market and employs third party compensation consultants to provide more independence to the process.

Executive compensation is reviewed and approved by the Board on an annual basis. As part of this review, the Board considers market expectations and projections of changes for comparable positions using, where available, independent, competent and relevant sources.

(c) Related party transactions:

FirstOntario's related parties include:

(i) All members of the Board, Officers and Executives of FirstOntario.

(ii) FirstOntario's subsidiaries (1320828 Ontario Limited, FOIH, FOIB) and joint ventures noted in Note 9.

FirstOntario Insurance Holdings Inc. is a wholly owned subsidiary of FirstOntario. FOIH is a holding company which manages FirstOntario's holdings in FirstOntario Insurance Brokers Inc. FOIH holds 51% of the ownership interests and voting rights of FOIB. All intercompany transactions and balances have been eliminated.

FOIB is an insurance brokerage which commenced operations during 2018. The remaining 49% of ownership interests and voting rights not held by FOIH are held by non-controlling interests. During the year, a net loss of $69,000 (2019 - net loss of $49,000) was allocated to non-controlling interests, resulting in accumulated non-controlling interests of $191,000 at December 31, 2020. All intercompany transactions and balances have been eliminated.

(iii) Defined benefit plans that are referred to in Note 19. FirstOntario's transactions with the plans include contributions paid into the plans. FirstOntario also pays for the expenses of the employee defined contribution plan. FirstOntario has not entered into other transactions with the defined benefit plans.

14. Regulatory Reporting and Disclosure (continued):

(c) Related party transactions (continued):

The following table outlines remuneration of members of the Board, Officers and Executives:

(In thousands of dollars)		**2020**		2019
Salaries, bonuses, and other short-term employee benefits	**$**	**2,723**	$	2,600
Post-employment benefits		**1,292**		4,113
Directors' remuneration		**375**		384
Total compensation	**$**	**4,390**	$	7,097

Related party balances as at December 31 are outlined in the following table:

(In thousands of dollars)		**2020**		2019
<u>Loans</u>				
Residential mortgages	**$**	**2,968**	$	2,868
Personal loans		**192**		160
Accrued interest		**2**		1
<u>Deposits and Shares</u>				
Deposits		**2,304**		2,224
Membership shares		**3**		3
Investment shares		**168**		215
Accrued interest		**5**		4

Total interest revenue derived from lending activity relating to key management personnel was $93,000 during the year ended December 31, 2020 (2019 - $83,000). Total interest expense from deposit-taking activity from related parties was $23,000 during the year ended December 31, 2020 (2019 - $33,000). During 2020 and 2019, no loans held by related parties were impaired.

15. Loans Payable and Securitization Liabilities:

The following table details loans payable to Central 1 and other funding partners. Security pledged is set out in Note 22(b). All loans payable are classified as amortized cost.

(In thousands of dollars)	2020	2019
Central 1 Credit Facilities		
Term loan facilities, bearing a variable interest rate of 0.98% (2019 – 2.58%) due within one year	$ 30,000	$ 48,000
Caisse centrale Desjardins Credit Facilities		
Term loan facility, bearing a fixed interest rate of nil (2019 - 2.98%), settled in 2020	-	40,000
Term loan facility, bearing a variable interest rate of 1.09% plus 0.50% (2019 – 2.05% plus 0.50%), maturity date of 2020	-	50,000
Securitization Liabilities		
Mortgage Backed Securities secured by residential mortgage loans, bearing a weighted average fixed interest rate of 2.04% (2019 – 2.19%), expected weighted average maturity date of 2023 (2019 - 2023)	498,729	512,141
Mortgage Backed Securities secured by residential mortgage loans, bearing a weighted average variable interest rate of 0.97% (2019 - 2.56%), expected weighted average maturity date of 2021 (2019 - 2021)	1,270	2,199
	$ 529,999	$ 652,340

As at December 31, 2020 and December 31, 2019, FirstOntario was in compliance with all financial and non-financial covenants.

Interest expense associated with loans payable during the year consisted of the following:

(In thousands of dollars)	2020	2019
Term loans	$ 3,882	$ 3,382
Securitization of residential mortgages	14,365	10,924
	18,247	$ 14,306

16. Derivative Financial Instruments:

(a) Asset liability management:

In the ordinary course of business, FirstOntario purchases derivative instruments from multiple counterparties in order to hedge against exposure to interest rate fluctuations.

Derivative instruments have a fair value that varies based on the particular instrument and changes in interest rates. The purpose of these instruments is to provide a hedge against interest rate fluctuations by improving FirstOntario's matching of its asset and liability position.

(b) Product related:

FirstOntario offers deposit products linked to changes in equity indexes or specific bundles of equities. FirstOntario hedges the underlying risk of these products by entering into equity-linked purchase option contracts. Under the terms of these contracts, FirstOntario will receive payments approximate to the future payments to Members.

(c) Foreign exchange forward contracts:

FirstOntario offers deposit products denominated in US dollars. In order to meet liquidity reserve requirements FirstOntario sells US dollars and purchases US dollar foreign exchange forward contracts to hedge the exchange risk.

The following table summarizes the notional amounts, maturities and fair values of FirstOntario's derivative portfolio as at December 31, 2020 and December 31, 2019:

						2020
	Within	**1 to 5**	**Over**		**Fair Value**	
(In thousands of dollars)	**1 year**	**years**	**5 years**	**Total**	**Assets**	**Liabilities**
Pay fixed interest rate swaps	**$ 1,497**	**$ 110,000**	**$ -**	**$ 111,497**	**$ 11**	**$ 902**
Bond forwards	**-**	**-**	**-**	**-**	**-**	**-**
Equity-linked options	**368**	**4,852**	**-**	**5,220**	**128**	**206**
Foreign exchange forward contracts	**147,569**	**-**	**-**	**147,569**	**2,001**	**1,474**
2020 Total	**$ 149,434**	**$ 114,852**	**$ -**	**$ 264,286**	**$ 2,140**	**$ 2,582**

						2019
	Within	1 to 5	Over		Fair Value	
(In thousands of dollars)	1 year	years	5 years	Total	Assets	Liabilities
Pay fixed interest rate swaps	$ 55,000	$ 31,561	$ -	$ 86,561	$ 368	$ 72
Bond forwards	20,000	-	-	20,000	120	-
Equity-linked options	831	1,056	-	1,887	137	118
Foreign exchange forward contracts	147,741	-	-	147,741	1,023	1,021
2020 Total	$ 223,572	$ 32,617	$ -	$ 256,189	$ 1,648	$ 1,211

16. Derivative Financial Instruments (continued):

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, other than foreign exchange forward contracts, are not exchanged.

FirstOntario is exposed to credit risk which arises from the possibility that a counterparty to a derivative contract could default on their obligation to FirstOntario. However, credit risk associated with derivative contracts is normally a small fraction of the notional principal amount of the contract. Derivative contracts expose FirstOntario to loss only if changes in market rates cause a material unfavourable effect on a counterparty's position, which could then lead to the counterparty defaulting on its payment. FirstOntario only enters into derivative contracts with counterparties that FirstOntario has determined to be creditworthy.

17. Financial Risk Management:

The Board of Directors (the "Board") has overall responsibility for the establishment and oversight of FirstOntario's risk management framework. The Board has delegated to the Audit and Risk Committee the responsibility for the development and monitoring of risk management policies. The Audit and Risk Committee reports regularly to the Board on its activities.

All risk management policies and established limits ensure that FirstOntario is in full adherence to the regulatory requirements prescribed in the Act as well as FSRA's standards of Sound Business and Financial Practices. The Board receives reports from management on FirstOntario's exposure to credit, interest rate, liquidity, foreign currency and other price risk regularly in order to monitor financial risks.

(a) Credit Risk:

Credit risk is the potential for financial loss to FirstOntario if a borrower or guarantor fails to meet payment obligations in accordance with agreed terms. FirstOntario's financial assets that are affected by credit risk include loans receivable from Members, investments, and derivative financial instruments. Credit risk is one of the most significant financial risks to FirstOntario.

FirstOntario's primary objective when managing credit risk is to ensure a portfolio of high quality financial assets properly diversified so as to balance the risk associated with the portfolio and return on assets.

Credit risk is managed in accordance with the Credit Risk Management Policy for loans receivable from Members and the Market Risk Management Policy for investments and derivative financial instruments.

17. Financial Risk Management (continued):

(a) Credit Risk (continued):

For loans receivable from Members, credit risk is managed through an infrastructure based upon:

(i) Approval by the Board of all credit risk management policies;

(ii) Approval by the Chief Risk Officer of the discretionary limits of lending officers throughout FirstOntario;

(iii) Credit adjudication subject to compliance with established policies, exposure guidelines and discretionary limits, as well as adherence to established standards of credit assessment. Credit approvals are escalated to the Management Credit Committee and ultimately to the Board of Directors dependent upon credit exposure level and restricted party transactions;

(iv) The Credit Department is charged with oversight of the following:

a. The establishment of guidelines to monitor and limit concentrations in the portfolios in accordance with Board approved policies governing regulatory requirements, industry risk and group exposures;

b. The development and implementation of credit risk models and policies for establishing borrower risk ratings to quantify and monitor the level of risk and facilitate management of retail and commercial credit;

c. Implementation of an ongoing monitoring process of the key risk factors used in FirstOntario credit risk models.

Management has designed and implemented an effective system to measure, monitor and report credit risk exposure. Management reports credit risk exposure to the Board regularly.

In conducting lending activities, FirstOntario diversifies its portfolio of loans receivable from Members in order to reduce overall credit risk. Residential mortgage and personal loans are diversified between authorized loan types, forms of security and certain sectoral groupings.

Commercial loans are diversified through the establishment of credit exposure limits for specific industry sectors, groups of related borrowers and geographic location.

Credit exposure is assessed through the following:

(i) Probability of default, which is an estimate of probability that a Member with a certain borrower risk rating, will default within a one year time horizon.

(ii) Loss given default, which represents the unsecured portion expected to be lost when a borrower defaults.

17. Financial Risk Management (continued):

(a) Credit Risk (continued):

Credit risk rating systems are designed to assess and quantify the risk inherent in credit activities in an accurate and consistent manner as follows:

(i) Commercial loans are principally assessed based on factors including the Member’s ability to service debt (debt service coverage ratio) and the secured amount (loan to value ratio). Management regularly reviews the commercial loan portfolio and assesses the credit risk associated with each loan.

(ii) Automated credit scoring systems assist in assessing credit risk associated with residential mortgage and personal loans. These loans are managed as pools of homogeneous risk exposures using internal benchmarks based upon TransUnion Credit Vision and/or Equifax Beacon Scores. These global standard credit scores track each individual’s past credit history and, using a mathematical model, predicts how likely a person is to repay a loan.

For investments and derivative financial instruments, risk is measured by reviewing exposure to individual counterparties to ensure the assets are within the policy limit by issuer weightings and by dollar amount. The quality of the counterparties is assessed through published credit rating agencies.

Except as noted, the carrying amount of financial assets recorded in the financial statements represents FirstOntario’s maximum exposure to credit risk without taking into account the value of any collateral obtained. FirstOntario is also exposed to credit risk through transactions which are not recognized in the Consolidated Statement of Financial Position, such as granting financial guarantees and extending loan commitments. Refer to Note 6 for further details. The risk of losses from loans undertaken is reduced by the nature and quality of collateral obtained. Refer to Note 6 for a description of the nature of the security held against loans as at the date of the Consolidated Statement of Financial Position.

(b) Interest Rate Risk:

Interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. FirstOntario is exposed to interest rate risk when entering into banking transactions with Members, primarily deposit and lending activities.

FirstOntario’s exposure to interest rate risk depends on the size and direction of interest rate changes, and on the size and maturity of mismatched positions. An interest-sensitive asset or liability is repriced when market interest rates change, when there is cash flow from final maturity, normal amortization, or when Members exercise prepayment, conversion or redemption options are offered for the specific product.

Interest rate risk is managed in accordance with the Structural Risk Management Policy. The Board delegates the responsibility to manage interest rate risk on a day-to-day basis to management.

17. Financial Risk Management (continued):

(b) Interest Rate Risk (continued):

FirstOntario's Structural Risk Management Policy includes:

(i) Guidelines and limits on the structuring of the maturities, price and mix of deposits, loans, mortgages and investments and the management of cash flows derived from financial assets in relation to liabilities.

(ii) Guidelines and limits on the use of derivative products to hedge against changes in cash flows as a result of changes in interest rates.

The following table summarizes carrying amounts of Consolidated Statement of Financial Position assets, liabilities and equity, and derivative instruments to arrive at FirstOntario's interest rate gap based on the earlier of contractual repricing and maturity dates:

						2020
(In thousands of dollars)	**Within 3 months**	**3 Months to 1 year**	**1 to 5 years**	**Over 5 years**	**Non Interest Sensitive**	**Total**
Assets						
Loans receivable	**$ 606,779**	**$ 884,728**	**$ 2,746,484**	**$ 8,748**	**$ -**	**$ 4,246,739**
Cash and cash equivalents	**-**	**-**	**-**	**-**	**26,892**	**26,892**
Investments	**304,344**	**315**	**11,510**	**-**	**243,723**	**559,892**
Other	**2,050**	**13**	**77**	**-**	**86,698**	**88,838**
	$ 913,173	**$ 885,056**	**$ 2,758,071**	**$ 8,748**	**$ 357,313**	**$ 4,922,361**
Liabilities and equity						
Deposits	**$ 1,477,267**	**$ 1,000,588**	**$ 866,915**	**$ 24**	**$ 643,574**	**$ 3,988,368**
Loans and securitization liabilities	**55,082**	**171,386**	**303,530**	**-**	**-**	**529,998**
Other	**1,552**	**37**	**993**	**-**	**401,413**	**403,995**
	$ 1,533,901	**$ 1,172,011**	**$ 1,171,438**	**$ 24**	**$ 1,044,987**	**$ 4,922,361**
Gap-Financial position	**(620,728)**	**(286,955)**	**1,586,633**	**8,724**	**(687,674)**	**-**
Gap-Derivatives	**(111,497)**	**1,497**	**110,000**	**-**	**-**	**-**
Interest rate gap 2020	**$ (732,225)**	**$ (285,458)**	**$ 1,696,633**	**$ 8,724**	**$ (687,674)**	**$ -**

17. Financial Risk Management (continued):

(b) Interest Rate Risk (continued):

						2019
(In thousands of dollars)	Within 3 months	3 Months to 1 year	1 to 5 years	Over 5 years	Non Interest Sensitive	Total
Assets						
Loans receivable	$ 551,829	$ 873,546	$ 2,546,035	$ 6,471	$ -	$ 3,977,881
Cash and cash equivalents	-	-	-	-	25,712	25,712
Investments	12,224	54,665	224,665	-	248,568	540,122
Other	1,145	60	443	-	84,279	85,927
	$ 565,198	$ 928,271	$ 2,771,143	$ 6,471	$ 358,559	$ 4,629,642
Liabilities and equity						
Deposits	$ 1,132,931	$ 1,056,973	$ 929,139	$ 13	$ 497,210	$ 3,616,266
Loans and securitization liabilities	125,640	109,941	416,759	-	-	652,340
Other	958	159	94	-	359,825	361,036
	$ 1,259,529	$ 1,167,073	$ 1,345,992	$ 13	$ 857,035	$ 4,629,642
Gap-Financial position	(694,331)	(238,802)	1,425,151	6,458	(498,476)	-
Gap-Derivatives	(61,561)	50,000	11,561	-	-	-
Interest rate gap 2020	$ (755,892)	$ (188,802)	$ 1,436,712	$ 6,458	$ (498,476)	$ -

Key metrics involved in management of interest rate risk include the use of Earnings at Risk ("EaR") and Economic Value of Equity at Risk ("EVEaR"). EaR is defined as the change in the net interest income from a 100 basis point ("bps") shock to interest rates. This exposure is measured over a 12 month period. EVEaR is defined as the difference in the change in the present value of the asset portfolio and the change in the present value of the liability portfolio, including off-Statement of Financial Position instruments, resulting from a 100 bps interest rate shock.

The following table summarizes the EaR and EVEaR as follows:

(In thousands of dollars)	**2020**	2019
EaR - Up 100 bps	**$ 58**	$ (1,252)
EaR - Down 100 bps	**(101)**	913
EVEaR - Up 100 bps	**(3.59)%**	(3.77)%
EVEaR - Down 100 bps	**3.39%**	3.56%

17. Financial Risk Management (continued):

(b) Interest Rate Risk (continued):

Fair Value Hedges

FirstOntario had designated hedging relationships involving bond forwards that hedged mortgage assets that were associated with debt issuances relating to securitization activity as fair value hedges. Realized gains (losses) on these derivatives were deferred and amortized in accordance with the effective interest rate method along with the asset originated. During the year, income of $nil (2019 - $nil) due to hedge ineffectiveness arose and was recorded in other interest income in the Consolidated Statement of Income. Fair values of the bond forwards involved in these hedges that were unrealized at the end of the year was $nil (2019 - $nil). The amount of deferred gain that is expected to be reclassified to the Consolidated Statement of Income over the next 12 months is $nil (2019 - $74,000).

FirstOntario has designated certain hedging relationships involving interest rate swaps that are used to hedge a portfolio of fixed rate, prepayable mortgages as fair value hedged. Gains (losses) associated with the fair value adjustment of these derivatives are recognized in the Consolidated Statement of Income and are offset by the change in fair value of the hedged mortgages with any remaining difference representing hedge ineffectiveness. During the year, a net loss of $207,000 (2019 - $nil) arose due to hedge ineffectiveness and was recorded in other interest income. Fair values of the interest rate swaps involved in these hedges at the end of the year was a liability of $875,000 (2019 - $nil) and the fair value increment of the hedged mortgages was $1,037,000 (2019 - $nil).

Cash Flow Hedges

FirstOntario has designated certain hedging relationships involving interest rate swaps that converted variable rate deposits to fixed rate deposits as cash flow hedges. During the year ended December 31, 2020 amortization of other comprehensive gain of $3,000 (2019 - $338,000) was recorded in other interest expense in the Consolidated Statement of Income. The fair value of interest rate swaps involved in hedging relationships at the end of the year was a liability of $nil (2019 - liability of $41,000). The amount of other comprehensive gain that is expected to be reclassified to the Consolidated Statement of Income over the next 12 months is $nil (2019 - $3,000).

FirstOntario has also designated hedging relationships involving bond forwards that hedged forecasted debt issuances associated with securitization activity as cash flow hedges. Realized gains (losses) on these derivatives are deferred and amortized in accordance with the effective interest rate method along with the debt originated. The fair value of bond forwards involved in these hedges at the end of the year was an asset of $nil (2019 – asset of $120,000). The amount of other comprehensive gain that is expected to be reclassified to the Consolidated Statement of Income over the next 12 months is $1,813,000 (2019 - $574,000).

17. Financial Risk Management (continued):

(c) Liquidity Risk:

Liquidity risk is the risk that FirstOntario will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or other financial assets.

FirstOntario engages in proper liquidity risk management practices to comply with regulatory requirements and to guarantee the funding of Member needs and obligations. FirstOntario's overall objective when managing liquidity is to ensure limited exposure to material liquidity risk.

Liquidity risk is managed in accordance with the Liquidity Risk Management Policy. Key elements of this policy include limits on the sources, quality and amount of liquid assets to meet operational requirements, regulatory requirements and contingency funding. Liquidity is monitored by management through FirstOntario's Asset/Liability Committee ("ALCO"), consisting of the executive.

Under the Regulations, FirstOntario must establish and maintain prudent levels of liquidity that are sufficient to meet its cash flow needs, including depositor withdrawals and all other obligations as they come due. FirstOntario targets to maintain operating liquidity within the range of 8% to 16%. The low end of the range has been established in order to maintain a comfortable cushion beyond the minimum policy requirements in order to meet cash needs, even during periods of market volatility. As at December 31, 2020, FirstOntario's liquidity ratio was 14.05% (2019 – 9.53%) and assets held for liquidity purposes totaled $641,414,000 (2019 - $387,141,000), consisting of $304,322,000 (2019 - $275,341,000) liquidity reserve deposits, $310,200,000 (2019 - $87,808,000) National Housing Act mortgage-backed securities held for liquidity and $26,892,000 (2019 - $25,712,000) cash.

The following tables demonstrate FirstOntario's ability to pay future obligations as financial assets and liabilities mature as at December 31, 2020 and 2019. These cash flows include both the contractual cash flows currently exposed on the Consolidated Statement of Financial Position and the cash flows that will be generated in the future. In the case of loans, the cash flows include estimated prepayments and credit losses based on experience and current economic conditions.

17. Financial Risk Management (continued):

(c) Liquidity Risk (continued):

							2020
(In thousands of dollars)	Within 1 month	2 to 12 months	1 to 3 years	3 to 5 years	Over 5 years	Not Specified	Total
Assets							
Loans receivable from Members	$ 507,104	$ 1,455,366	$ 1,512,612	$ 1,001,626	$ 9,557	$ -	$ 4,486,265
Cash	26,892	-	-	-	-	-	26,892
Investments	304,976	5,822	5,353	446	-	243,658	560,255
Derivative financial instruments	2,037	24	66	13	-	-	2,140
Total cash inflow	$ 841,009	$ 1,461,212	$ 1,518,031	$ 1,002,085	$ 9,557	$ 243,658	$ 5,075,552
Liabilities							
Members' deposits and shares	$ 1,789,643	$ 1,343,269	$ 760,141	$ 133,742	$ 18	$ 133,156	$ 4,159,969
Loans payable	39,774	194,049	183,276	151,241	-	-	568,340
Other liabilities	78,681	2,715	5,723	4,540	6,181	-	97,840
Derivative financial instruments	1,288	295	919	80	-	-	2,582
Total cash outflow	$ 1,909,386	$ 1,540,328	$ 950,059	$ 289,603	$ 6,199	$ 133,156	$ 4,828,731

							2019
(In thousands of dollars)	Within 1 month	2 to 12 months	1 to 3 years	3 to 5 years	Over 5 years	Not Specified	Total
Assets							
Loans receivable from Members	$ 511,215	$ 1,396,291	$ 1,373,478	$ 942,574	$ 6,848	$ -	$ 4,230,406
Cash	25,712	-	-	-	-	-	25,712
Investments	7,741	72,883	124,027	103,304	-	246,849	554,804
Derivative financial instruments	2	1,202	120	324	-	-	1,648
Total cash inflow	$ 544,670	$ 1,470,376	$ 1,497,625	$ 1,046,202	$ 6,848	$ 246,849	$ 4,812,570
Liabilities							
Members' deposits and shares	$ 1,374,709	$ 1,369,883	$ 790,740	$ 179,584	$ 6	$ 131,016	$ 3,845,938
Loans payable	57,362	187,243	283,414	165,998	-	-	694,017
Other liabilities	78,002	-	-	-	-	-	78,002
Derivative financial instruments	26	1,091	88	6	-	-	1,211
Total cash outflow	$ 1,510,099	$ 1,558,217	$ 1,074,242	$ 345,588	$ 6	$ 131,016	$ 4,619,168

17. Financial Risk Management (continued):

(d) Foreign Currency Risk:

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates. FirstOntario is exposed to foreign currency risk as a result of its Members' activities in US dollar currency denominated deposits and cash transactions, as well as US dollar investments. Activities that expose FirstOntario to currency risk are measured, monitored and controlled daily to minimize risk. At any point in time, net US dollar exposure is limited by the Market Risk Management Policy to $1,000,000 through the use of foreign exchange forward contracts. As at December 31, 2020, FirstOntario does not have significant exposure to changes in foreign currency exchange rates.

(e) Equity and Other Price Risk:

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices other than those arising from interest rate risk or currency risk. FirstOntario is primarily exposed to other price risk through actively traded fair value investments. However, these investments are limited by policy to ensure diversification and quality of financial assets. As at December 31, 2020, had the value of FirstOntario's managed funds, preferred, and common shares increased or decreased by 10% with all other variables remaining unchanged, the portfolio's asset value would have increased or decreased respectively by $11,044,000 (2019 - $10,322,000) or 4.2% (2019 - 4.3%) of total Members' Equity.

18. Fair Values of Financial Instruments:

The following table represents the fair values of FirstOntario's financial instruments. The fair values disclosed do not include the value of assets that are not considered financial instruments, such as fixed assets. The value of intangibles such as long-term Member relationships are also not included in the fair value amounts.

While the fair value amounts are intended to represent estimates of the amounts at which these instruments could be exchanged in a current transaction between willing parties, some of FirstOntario's financial instruments lack an available trading market. Consequently, the fair values presented are estimates derived using present value and other valuations techniques and may not be indicative of the net realizable values.

Due to the judgment used in applying a wide range of acceptable valuation techniques and estimates in calculating fair value amounts, fair values are not necessarily comparable among financial institutions. The calculation of estimated fair values is based on market conditions at a specific point in time and may not be reflective of future fair values.

18. Fair Values of Financial Instruments (continued):

(In thousands of dollars)	**FVTPL-Mandatorily**	**FVOCI-Equity Instruments**	**Amortized Cost**	**Total Carrying Value**	**2020 Fair Value**
Financial Assets					
Cash and cash equivalents	**$ -**	**$ -**	**$ 26,892**	**$ 26,892**	**$ 26,892**
Investments	**124,228**	**21,620**	**316,234**	**462,082**	**491,389**
Loans receivable from Members	**-**	**-**	**4,266,253**	**4,266,253**	**4,377,967**
Derivatives	**2,140**	**-**	**-**	**2,140**	**2,140**
Total financial assets	**$ 126,368**	**$ 21,620**	**$ 4,609,379**	**$ 4,757,367**	**$ 4,898,388**
Financial Liabilities					
Members' deposits and shares	**$ -**	**$ -**	**$ 4,034,238**	**$ 4,034,238**	**$ 4,053,668**
Loans payable and securitization liabilities	**-**	**-**	**529,999**	**529,999**	**541,269**
Accounts payable and accrued liabilities	**-**	**-**	**78,434**	**78,434**	**78,434**
Lease liabilities	**-**	**-**	**17,057**	**17,057**	**17,057**
Derivatives	**2,582**	**-**	**-**	**2,582**	**2,582**
Total financial liabilities	**$ 2,582**	**$ -**	**$ 4,659,728**	**$ 4,662,310**	**$ 4,693,010**

(In thousands of dollars)	FVTPL-Mandatorily	FVOCI-Equity Instruments	Amortized Cost	Total Carrying Value	2019 Fair Value
Financial Assets					
Cash and cash equivalents	$ -	$ -	$ 25,712	$ 25,712	$ 25,712
Investments	140,654	21,619	293,369	455,642	455,043
Loans receivable from Members	-	-	3,996,068	3,996,068	3,961,608
Derivatives	1,648	-	-	1,648	1,648
Total financial assets	$ 142,302	$ 21,619	$ 4,315,149	$ 4,479,070	$ 4,444,011
Financial Liabilities					
Members' deposits and shares	$ -	$ -	$ 3,659,537	$ 3,659,537	$ 3,661,059
Loans payable and securitization liabilities	-	-	652,340	652,340	649,460
Accounts payable and accrued liabilities	-	-	58,853	58,853	58,853
Lease liabilities	-	-	19,149	19,149	19,149
Derivatives	1,211	-	-	1,211	1,211
Total financial liabilities	$ 1,211	$ -	$ 4,389,879	$ 4,391,090	$ 4,388,732

Interest rate sensitivity is the main cause of change in fair values of FirstOntario's financial instruments.

The following methods and assumptions were used to estimate the fair value of financial instruments:

(a) The fair values of cash and accounts payable and accrued liabilities are assumed to approximate their book values, due to their short-term nature.

(b) The estimated fair value of floating rate loans, demand deposits and floating rate deposits are assumed to be equal to book value as the interest rates on these loans and deposits reprice to market on a periodic basis.

18. Fair Values of Financial Instruments (continued):

(c) The estimated fair values of fixed rate investments, fixed rate loans and fixed rate deposits are determined by discounting the expected future cash flows of these investments, loans, deposits and borrowings at current market rates for products with similar terms and credit risks.

(d) The estimated fair values of derivative instruments are determined through valuation models on the derivative notional amounts, maturity dates and rates.

(e) The estimated fair values of investments in publicly listed equity securities are determined using quoted market prices.

Fair value measurements can be classified in a hierarchy in order to discern the significance of management assumptions and other inputs incorporated into the measurements. The three levels of fair value hierarchy are:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 – Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3 – Inputs for the asset or liability that are not based on observable market data. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments are required to reflect differences between the instruments.

The following table summarizes the classification of FirstOntario's financial instruments held and reported on the Consolidated Statement of Financial Position at fair value:

				2020
(In thousands of dollars)	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Investments – FVTPL	**$ -**	**$ 116,513**	**$ 7,715**	**$ 124,228**
Investments – FVOCI	**-**	**-**	**21,620**	**21,620**
Derivative financial instruments	**-**	**2,140**	**-**	**2,140**
Total assets held at fair value	**$ -**	**$ 118,653**	**$ 29,335**	**$ 147,988**
Liabilities				
Derivative financial instruments	**$ -**	**$ 2,582**	**$ -**	**$ 2,582**
Total liabilities held at fair value	**$ -**	**$ 2,582**	**$ -**	**$ 2,582**

18. Fair Values of Financial Instruments (continued):

(In thousands of dollars)	Level 1	Level 2	Level 3	2019 Total
Assets				
Investments – FVTPL	$ -	$ 134,394	$ 6,260	$ 140,654
Investments – FVOCI	-	-	21,619	21,619
Derivative financial instruments	-	1,648	-	1,648
Total assets held at fair value	$ -	$ 136,042	$ 27,879	$ 163,921
Liabilities				
Derivative financial instruments	$ -	$ 1,211	$ -	$ 1,211
Total liabilities held at fair value	$ -	$ 1,211	$ -	$ 1,211

The following table summarizes the Level 2 fair values of FirstOntario's financial instruments whose carrying value are not fair value on the Consolidated Statement of Financial Position as at December 31, 2020 and December 31, 2019. Financial assets and liabilities whose carrying values are a reasonable approximation of fair value are not included. FirstOntario's financial instruments held at amortized cost are all classified as Level 2 as identified below:

(In thousands of dollars)	**2020**	2019
Assets		
Loans receivable	**$ 4,337,967**	$ 3,961,608
Investments	**323,336**	292,771
Total assets held at fair value	**$ 4,661,303**	$ 4,254,379
Liabilities		
Deposits and shares	**$ 4,053,668**	$ 3,661,059
Loans payable	**541,269**	649,460
Total liabilities held at fair value	**$ 4,594,937**	$ 4,310,519

The fair value measurement of all of the joint ventures has been categorized as a level 3 fair value based on the inputs of the valuation techniques used (See Note 9).

19. Employee Retirement Benefits:

FirstOntario provides retirement benefits to certain employees. These benefits include registered pension plans, medical benefits, dental care and life insurance.

The fair value of accrued benefit obligations were determined by independent actuaries as at December 31, 2020 and December 31, 2019.

	Defined Benefit Pensions		Other Defined Benefit Plans	
(In thousands of dollars)	**2020**	2019	**2020**	2019
Accrued benefit obligation				
Balance at the beginning of year	**$ 19,972**	$ 17,453	**$ 5,366**	$ 5,091
Current service cost	**566**	433	**53**	46
Interest cost	**612**	677	**163**	192
Benefits paid	**(1,578)**	(1,070)	**(143)**	(239)
Actuarial loss	**1,849**	2,479	**201**	276
Balance at end of year	**$ 21,421**	$ 19,972	**$ 5,640**	$ 5,366
Plan assets				
Fair value at beginning of year	**$ 17,066**	$ 15,530	**$ -**	$ -
Expected return on plan assets	**513**	596	**-**	-
Actuarial gain on plan assets	**972**	1,506	**-**	-
Employer contributions	**614**	504	**143**	239
Benefits paid	**(1,578)**	(1,070)	**(143)**	(239)
Fair value at end of year	**17,587**	17,066	**-**	-
Balance at end of year	**$ (3,834)**	$ (2,906)	**$ (5,640)**	$ (5,366)

The following table provides the amounts recognized in the Consolidated Statement of Financial Position as follows:

	Defined Benefit Pensions		Other Defined Benefit Plans	
(In thousands of dollars)	**2020**	2019	**2020**	2019
Accrued benefit liabilities recorded in accounts payable and accrued liabilities	**$ (3,834)**	$ (2,906)	**$ (5,640)**	$ (5,366)
Balance at end of year	**$ (3,834)**	$ (2,906)	**$ (5,640)**	$ (5,366)

19. Employee Retirement Benefits (continued):

FirstOntario's net benefit plan expenses recognized in other comprehensive income were as follows:

	Defined Benefit Pensions		Other Defined Benefit Plans	
(In thousands of dollars)	**2020**	2019	**2020**	2019
Cumulative actuarial losses at beginning of year	**$ (3,858)**	$ (2,885)	**$ 647**	$ 923
Actuarial loss in the year on liability	**(1,849)**	(2,479)	**(201)**	(276)
Actuarial gain in the year on plan assets	**972**	1,506	**-**	-
Cumulative actuarial gain (loss)	**$ (4,735)**	$ (3,858)	**$ 446**	$ 647

The net loss recognized in other comprehensive income of $891,000 (2019 net loss - $1,006,000) during the year are net of a tax recovery of $187,000 (2019 tax recovery- $243,000) as disclosed in Note 21.

FirstOntario's net benefit plan expenses recognized in the Consolidated Statement of Income were as follows:

	Defined Benefit Pensions		Other Defined Benefit Plans	
(In thousands of dollars)	**2020**	2019	**2020**	2019
Current service cost	**$ 566**	$ 433	**$ 53**	$ 46
Interest cost	**612**	677	**163**	192
Expected return on plan assets	**(513)**	(596)	**-**	-
Total included in employee benefits expense	**$ 665**	$ 514	**$ 216**	$ 238

	Defined Contribution Pension	
(In thousands of dollars)	**2020**	2019
Contributions recorded as expenses	**$ 2,091**	$ 1,968

These net benefit plan and contribution expenses are included in salaries and employee benefits on the Consolidated Statement of Income. Aggregate contributions relating to defined benefit pensions and other defined benefit plans expected for the year ended December 31, 2021, is $1,040,000.

The significant actuarial assumptions adopted by FirstOntario are as follows (weighted-average assumptions):

	Defined Benefit Pensions		Other Defined Benefit Plans	
(In thousands of dollars)	**2020**	2019	**2020**	2019
Discount rate	**2.6%**	3.1%	**2.6%**	3.1%
Rate of compensation increase	**2.0%**	2.0%		-

19. Employee Retirement Benefits (continued):

The expected rate of return on plan assets is based on the risks and associated returns expected of the underlying plan assets. Plan assets are held in balanced funds which includes equities and long-term bonds.

For measurement purposes, 5% and 3% rates of increase in the per capita cost of covered health care and dental care benefits respectively were assumed for 2020. The rate of increase for health care benefits was assumed to remain unchanged at 5%. The rate of increase for dental care benefits was assumed to remain unchanged at 3%.

A one percentage-point change in assumed health-care cost trend rates, discount rates and salary costs would have the following impact on other defined benefit plans:

	2020		2019	
(In thousands of dollars)	**Defined benefit**	**Other plans**	Defined benefit	Other plans
Health care				
1% increase	**$ n/a**	**$ 456**	$ n/a	$ 422
1% decrease	**n/a**	**(396)**	n/a	(364)
Discount rate				
1% increase	**$ (3,534)**	**$ (559)**	$ (3,191)	$ (546)
1% decrease	**4,240**	**622**	3,803	609
Salary rate				
1% increase	**$ 211**	**$ n/a**	$ 164	$ n/a
1% decrease	**(204)**	**n/a**	(160)	n/a

20. Other Income:

(In thousands of dollars)	**2020**	2019
Service charges	**$ 3,736**	$ 4,023
Mortgage and loan fees	**4,695**	3,943
Commissions	**2,222**	2,122
Other operational income	**701**	1,022
Wealth management	**2,696**	2,504
Securitization	**9,295**	5,424
Real estate	**4,450**	13,139
Other investment income	**11,067**	10,270
Total other income	**$ 38,862**	$ 42,447

21. Income Taxes:

The components of income tax expense are as follows:

(In thousands of dollars)		2020		2019
Current income tax expense	$	4,144	$	1,382
Deferred income tax expense		263		1,865
Total income tax expense	$	4,407	$	3,247

Major components of income tax expense (benefit) include the following:

	2020	2019
Combined federal and provincial income taxes	26.5%	26.5%
Small business and credit union deductions	(8.3)	(8.0)
Income and expense permanent differences	0.1	0.3
Non-taxable capital gains on investment income	(1.5)	-
Other	(1.7)	(0.2)
Total income tax expense	15.1%	18.6%

The movements of deferred tax assets and liabilities are presented below:

(In thousands of dollars)		January 1, 2020		Charge to Income		Charge to OCI		Charge to Contributed Surplus		December 31, 2020
Fixed assets	$	(3,781)	$	134	$	-	$	-	$	(3,647)
Allowance for loan losses		933		781		-		-		1,714
Derivatives		247		321		-		-		568
Employee retirement benefits		1,528		24		187		-		1,739
Investments		(6,535)		(1,238)		-		-		(7,773)
Cash flow hedges		313		-		316		-		629
Other		(666)		(285)		-		641		(310)
Total	$	(7,961)	$	(263)	$	503	$	641	$	(7,080)

21. Income Taxes (continued):

(In thousands of dollars)	January 1, 2019	Charge to Income	Charge to OCI	Charge to Contributed Surplus	December 31, 2019
Fixed assets	$ (3,397)	$ (384)	$ -	$ -	$ (3,781)
Allowance for loan losses	810	123	-	-	933
Derivatives	221	26	-	-	247
Employee retirement benefits	1,289	(4)	243	-	1528
Investments	(4,593)	(1,942)	-	-	(6,535)
Cash flow hedges	324	-	(11)	-	313
Other	(982)	316	-	-	(666)
Total	$ (6,328)	$ (1,865)	$ 232	$ -	$ (7,961)

The tax effect of items recorded in the Consolidated Statement of Income and Other Comprehensive Income was as follows:

(In thousands of dollars)	**2020**	2019
Net (gain) loss on cash flow hedges	**$ 563**	$ (13)
Net (gain) loss on cash flow hedges transferred to earnings	**(247)**	2
Actuarial (gain) loss on defined benefit pension plans	**187**	243
Total tax effect of components of other comprehensive income	**$ 503**	$ 232

22. Commitments:

a. Mortgage commitments and lines of credit:

At December 31, 2020, FirstOntario has issued commitments to provide residential mortgage and commercial loans totaling $217,323,000 (2019 - $252,186,000). FirstOntario has also provided lines of credit to Members totaling $815,376,000 at December 31, 2020 (2019 - $825,377,000), against which Members have drawn $350,078,000 (2019 - $377,413,000).

b. Credit facilities:

Central 1 has provided an operating loan facility to FirstOntario of $164,700,000 (2019 - $164,700,000). Loans to Members have been pledged as security for these facilities and the term loan by an assignment of book debts and a general security agreement.

Caisse centrale Desjardins has provided an operating facility to FirstOntario in the amount of $100,000,000 (2019 - $100,000,000). When amounts are drawn against the facility, certain residential mortgages have been pledged as security.

See the Consolidated Statement of Financial Position and Note 15 for the outstanding amounts on these facilities.

22. Commitments (continued):

c. Contracts:

Interac ATM and point of sale switching servicing totaling $4,328,000 over the next 3 years at present service levels (2019 - $2,893,000 over the next 4 years).

Banking system support services and software maintenance totaling $6,860,000 over the next 11 years (2019 - $6,578,000 over the next 12 years).

Software licensing and support services totaling $1,190,000 over the next 5 years at present service levels (2019 - $850,000).

Telephone network and voice services totaling $3,675,000 over the next 5 years at present service levels (2019 - $4,766,000over the next 5 years).

Sponsorship agreement totaling $507,000 over the next year (2019 - $1,005,000 over the next 2 years).

d. Naming rights:

In fiscal 2017, FirstOntario entered into an agreement with Global Spectrum Facility Management, L.P. for the naming rights to the FirstOntario Concert Hall. The agreement is effective January 1, 2017 and provides the naming rights for 10 years at an average estimated cost of $267,000 per year for an aggregate total of $2,670,000.

In fiscal 2017, FirstOntario entered into an agreement with The Corporation of the Town of Milton for the naming rights to the FirstOntario Centre for the Arts. The agreement is effective January 24, 2017 and provides the naming rights for 25 years at an estimated cost of $226,000 per year for the first five years for an aggregate total of $1,130,000.

In fiscal 2015, FirstOntario entered into an agreement with The Corporation of the City of St. Catharine's, for the naming rights to the FirstOntario Performing Arts Centre. The agreement is effective January 1, 2016 and provides the naming rights for 25 years at an estimated cost of $678,000 per year for the first five years for an aggregate total of $3,390,000.

In fiscal 2014, FirstOntario entered into an agreement with Global Spectrum, L.P. for the naming rights to the FirstOntario Centre. The agreement provides the naming rights for 10 years at an average estimated cost of $373,000 per year for an aggregate total of $3,730,000.

23. Business Combination:

On October 31, 2020, FirstOntario Credit Union acquired Creative Arts Savings and Credit Union (“Creative Arts”) and the results of its operations have been included in the consolidated financial statements since that date. FirstOntario assumed liabilities totalling $29,182,000 in exchange for assets of $29,791,000. Post-acquisition, Creative Arts was rebranded as Creative Arts Financial.

(In thousands of dollars)	**Fair Value**
Cash and cash equivalents	**$ 12,987**
Member loans	**14,403**
Deferred tax asset	**641**
Other assets	**1,759**
Member deposits	**(27,891)**
Member shares	**(41)**
Other liabilities	**(120)**
Investment shares	**(1,129)**
Fair market value of net assets acquired	**$ 609**

The fair market value of net assets acquired was recorded in contributed surplus.

The carrying value of cash and cash equivalents and investments approximate their fair value due to their short-term nature.

The carrying values of loans was approximated using discounted cash flow techniques based on the contractual repayment of the products.

The vast majority of the acquired deposits were demand deposits in nature and as such, the carrying value of deposits was presumed to be equal to the fair value.

The acquired fixed assets consist of significantly depreciated office furniture and equipment, and the banking system used by Creative Arts prior to the acquisition which had no value subsequent to the acquisition. As such, the acquired fixed assets were determined to have a fair value of $nil.

Income and expenses derived from the acquisition of Creative Arts have been included in the consolidated financial statements from November 1, 2020 onwards. In subsequent years, the amount of profit or loss attributable to Creative Arts will not be disclosed separately, as it is not practical and would be immaterial in amount.