

*Basel III Pillar 3 Supplemental Disclosures of*

**ALTERNA BANK**

**December 31, 2014**

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

---

**1. Scope of Application**

CS Alterna Bank, a member of the Canada Deposit Insurance Corporation (“CDIC”), operates under the name “Alterna Bank”. It is a Schedule 1 Bank and received letters patent from the Minister of Finance of Canada to operate under the Bank Act on October 2, 2000.

The registered office address of Alterna Bank is 400 Albert Street, Ottawa, Ontario, K1R 5B2. The nature of Alterna Bank’s operations and principal activities are the provision of deposit taking facilities and loan facilities to the clients of the bank in Ontario and Quebec.

The Pillar 3 Supplemental Disclosures are unaudited and are additional summary descriptions and quantitative financial information which supplements those made in Alterna Bank’s audited financial statements for 2014. The disclosures produced within this document have been prepared in accordance with minimum disclosure requirements interpreted by the Office of the Superintendent of Financial Institutions Canada (‘OSFI’) and established under the OSFI Advisory on Pillar 3 Disclosure Requirements (November 2007) and related OSFI guidelines and letters.

***Comparison with Alterna Bank’s audited financial statements for 2014***

The financial statements have been prepared on a historical cost basis, except for available-for-sale investments, derivative financial instruments and financial assets and financial liabilities held at fair value through profit or loss, that have been measured at fair value.

The preparation of financial statements in conformity with International Financial Reporting Standards (‘IFRS’) requires management to make estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, revenues and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from management’s estimates.

The Pillar 3 Disclosures have been prepared in accordance with regulatory capital adequacy concepts and rules, rather than in accordance with IFRS. Therefore, some information in the Pillar 3 Disclosures is not directly comparable with the financial information in the Alterna Bank’s audited financial statements for 2014.

***Significant subsidiaries***

Alterna Bank has no subsidiaries or entities for consolidation.

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

The table below provides the modified minimum composition of capital disclosures under Basel III as required by the Office of the Superintendent of Financial Institutions Canada ('OSFI') for the year ended December 31, 2014.

<b>all amounts in 000's CAD dollars, except where noted</b>		<b>31-Dec-14</b>	
		<b>All-in</b>	<b>Transitional</b>
<b>Transitional Common Equity Tier 1 capital: instruments and reserves</b>			
1	Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	15,000	
2	Retained earnings	10,654	
3	Accumulated other comprehensive income (and other reserves)	345	
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)	-	
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-	
6	<b>Common Equity Tier 1 capital before regulatory adjustments</b>	25,999	
<b>Common Equity Tier 1 capital: regulatory adjustments</b>			
28	Total regulatory adjustments to Common Equity Tier 1	(82)	
29	<b>Common Equity Tier 1 capital (CET1)</b>	25,917	
<b>Additional Tier 1 capital: instruments</b>			
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	-	
31	of which: classified as equity under applicable accounting standards	-	
32	of which: classified as liabilities under applicable accounting standards	-	
33	Directly issued capital instruments subject to phase out from Additional Tier 1	-	
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)	-	
35	of which: instruments issued by subsidiaries subject to phase out	-	
36	<b>Additional Tier 1 capital before regulatory adjustments</b>	-	
<b>Additional Tier 1 capital: regulatory adjustments</b>			
43	<b>Total regulatory adjustments to Additional Tier 1 capital</b>	-	
44	<b>Additional Tier 1 capital (AT1)</b>	-	
45	<b>Tier 1 capital (T1 = CET1 + AT1)</b>	25,917	25,983
<b>Tier 2 capital: instruments and allowances</b>			
46	Directly issued qualifying Tier 2 instruments plus related stock surplus	-	
47	Directly issued capital instruments subject to phase out from Tier 2	-	
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-	
49	of which: instruments issued by subsidiaries subject to phase out	-	
50	Collective allowances	-	
51	<b>Tier 2 capital before regulatory adjustments</b>	-	
<b>Tier 2 capital: regulatory adjustments</b>			
57	<b>Total regulatory adjustments to Tier 2 capital</b>	-	
58	<b>Tier 2 capital (T2)</b>	-	
59	<b>Total capital (TC = T1 + T2)</b>	25,917	25,983
60	<b>Total risk-weighted assets</b>	51,321	51,404
<b>Capital ratios</b>			

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

61	Common Equity Tier 1 (as percentage of risk-weighted assets)	50.50%	
62	Tier 1 (as percentage of risk-weighted assets)	50.50%	
63	Total capital (as percentage of risk-weighted assets)	50.50%	
<b>OSFI all-in target</b>			
69	Common Equity Tier 1 capital all-in target ratio	7.00%	
70	Tier 1 capital all-in target ratio	8.50%	
71	Total capital all-in target ratio	10.50%	
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)			
80	<b>Current cap on CET1 instruments subject to phase out arrangements</b>	-	
81	Amounts excluded from CET1 due to cap (excess over cap after redemptions and maturities)	-	
82	Current cap on AT1 instruments subject to phase out arrangements	-	
83	Amounts excluded from AT1 due to cap (excess over cap after redemptions and maturities)	-	
84	Current cap on T2 instruments subject to phase out arrangements	-	
85	Amounts excluded from T2 due to cap (excess over cap after redemptions and maturities)	-	

The difference between the all-in and transitional capital ratios above is due to the deduction of deferred tax asset from CET1 and Risk Weighted Assets; this deduction is phased-in during the transition period of 2013 to 2018.

**2. Capital Structure**

OSFI's regulatory capital guidelines under Basel III allow for three tiers of capital. Tier 1 capital includes common shares and retained earnings. Alterna Bank currently does not hold any instruments in Tier 2 capital.

The table below provides the regulatory capital and ratios for the year ended December 31, 2014.

<b>(000s)</b>	<b>31-Dec-14</b>
Capital structure and ratios:	
Tier 1 Capital:	
Common shares	\$15,000
Retained earnings	10,654
Accumulated OCI	345
Regulatory adjustments	(82)
Total Tier 1 capital	\$25,917
Tier 2 capital:	
Total regulatory (eligible capital)	\$25,917
Risk-weighted assets	51,321
Capital ratios:	
Tier 1 Ratio	50.5%
<b>Total Ratio</b>	<b>50.5%</b>
<b>Total Net on- and off- balance sheet assets **</b>	<b>\$177,549</b>
<b>Assets-to-capital multiple *</b>	<b>6.83</b>

\* Total Capital for purposes of Assets-to-capital multiple is on a transitional basis (excludes Regulatory adjustments)

\*\*Total Assets at December 31, 2014 were \$177,565

Alterna Bank is in compliance with the imposed regulatory capital requirements to which it is subject.

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

---

**3. Capital Adequacy**

Under Section 485(1) of the Bank Act and OSFI Guideline A, Alterna Bank must maintain minimum capital requirements to support its ongoing operations. These capital requirements are based on total assets, types of assets that Alterna Bank owns and operational risk arising from its business activities and operating environment. As a general rule, the larger the total assets or riskier the asset types, the greater the capital required. The maximum asset to capital multiple is prescribed by OSFI.

In assessing the risk associated with Alterna Bank's assets, OSFI Guideline A provides guidance on the risk weights for each asset type. Capital required for risk-based assets is referred to as the Basel III Pillar 1 capital requirement or the risk-based capital requirement. OSFI generally requires that deposit-taking institutions target at least 7.00% and 10.50% for Tier 1 and total capital respectively. Alterna Bank's policy minimum, currently at 16.00%, is set in accordance with its Internal Capital Adequacy Assessment Process ('ICAAP'). All of Alterna Bank's capital is in the high-quality Tier 1 category, and therefore Tier 1 and total capital ratios are the same.

Basel III Pillar 1 does not necessarily capture all aspects of the overall risk profile. Pillar 2 addresses these limitations. Alterna Bank is tasked with implementing an ICAAP to ensure it has overall adequate capital in relation to its risk profile, to ensure it has a strategy for maintaining its capital levels, to enhance its capital management practices, and to develop and employ robust risk management techniques. In assessing Alterna Bank's capital requirements, management captures all enterprise risks and provides capital accordingly. The capital management planning ensures that the organization is well capitalized to manage in times of economic difficulty.

Alterna Bank uses the standardized approach for credit risk for all on-balance sheet portfolios and the basic indicator approach for all components of operational risk. Alterna Bank does not have any trading book assets or liabilities therefore no capital is required for market risk.

Risk-weighted Assets (RWAs) – by Risk Type and Regulatory Capital Requirements:

<b>(000s)</b>	<b>31-Dec-14</b>
	RWAs
Credit risk	\$43,526
Market risk	-
Operational risk	7,795
Total	\$51,321
<b>Total Capital Ratio</b>	<b>50.5%</b>

Note: Tier 1 and Total Capital Ratios are the same.

Further information regarding Alterna Bank's risk management framework and processes can be found in Alterna Bank's audited financial statements for 2014, Note 19 "NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS".

**4. Credit Risk: General Disclosures**

Qualitative disclosures with respect to definitions of past due and impaired loans (for accounting purposes), description of approaches followed for individual and collective allowances, and discussion of the credit risk management policy are present in the following notes to Alterna Bank's audited financial statements for 2014: Notes 2e "IMPAIRMENT OF FINANCIAL ASSETS", 2m (iii) "Impaired losses on loans and advances", and 2m (iv) "Impairment of available-for-sale investments"; Note 5 "Allowance for Impaired Loans and Impaired Loans"; and Note 19 "NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS".

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

Quantitative disclosures:

Total Gross Credit Exposure – Counterparty type distribution broken down by major types of credit exposure:

(000s)	31-Dec-14							
Standardized	Drawn Exposure	Commitments (Undrawn)	OTC Derivatives*	Other Off Balance Sheet Items	Total	RWAs		
Sovereign	\$20,470	\$ -	\$ -	\$ -	\$20,470	\$0		
Bank	3,733	-	-	-	3,733	747		
Corporate	7,589	-	244	-	7,833	7,638		
Retail Residential Mortgages	141,182	59	-	-	141,241	31,645		
Other Retail (excl. SBEs)	3,913	-	-	-	3,913	2,928		
<b>Total Gross Credit Exposure</b>	<b>176,887</b>	<b>59</b>	<b>244</b>	<b>-</b>	<b>177,190</b>	<b>42,958</b>		
<i>Reconciliation to Financial Statements (Balance Sheet)</i>								
<i>CVA Adjustment</i>							<b>58</b>	
<i>Other Assets (not included in Standardized Approach)</i>								
	719						<b>510</b>	
<b>Total Assets subject to credit risk</b>	<b>\$177,606</b>							
<i>Less Collective Allowance</i>	41							
<b>Total Assets</b>	<b>\$177,565</b>					<b>\$43,526</b>		

\* includes replacement values

Geographic distribution of exposures broken down by major types of credit exposure:

(000s)	31-Dec-14						
Geographic Distribution of Exposures	Drawn Exposure	Commitments (Undrawn)	OTC Derivatives*	Other Off Balance Sheet Items	Total	%	
Canada:							
Quebec	\$107,712	\$59	\$ -	\$ -	\$107,771	60.8%	
Ontario	68,135	-	244	-	68,379	38.6%	
British Columbia	151	-	-	-	151	0.1%	
Alberta	785	-	-	-	785	0.4%	
Manitoba	104	-	-	-	104	0.1%	
<b>Total Gross Credit Exposure</b>	<b>\$176,887</b>	<b>\$59</b>	<b>\$244</b>	<b>-</b>	<b>\$177,190</b>	<b>100.0%</b>	

\* includes replacement values

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

Industry distribution of exposures broken down by major types of credit exposure:

<b>(000s)</b>						<b>31-Dec-14</b>
Standardized exposure by industry	Drawn Exposure	Commitments (Undrawn)	OTC Derivatives*	Other Off Balance Sheet Items	Total	%
<b>Bank</b>						
Sovereign	\$20,470	\$ -	\$ -	\$ -	\$20,470	11.6%
Financial Services	3,733	-	-	-	3,733	2.2%
<b>Corporate</b>						
Real Estate	6,613	-	-	-	6,613	3.7%
Retail & Wholesale	384	-	-	-	384	0.2%
Services	592	-	-	-	592	0.3%
Other	-	-	244	-	244	0.1%
Retail Residential Mortgages	141,182	59	-	-	141,241	79.7%
Other Retail (excl. SBEs)	3,913	-	-	-	3,913	2.2%
<b>Total Gross Credit Exposure</b>	<b>\$176,887</b>	<b>\$59</b>	<b>\$244</b>	<b>-</b>	<b>\$177,190</b>	<b>100.0%</b>

\* includes replacement values

Residual contractual maturity breakdown of the whole portfolio broken down by major types of credit exposure is presented in Alterna Bank's audited financial statements for 2014, Note 19 "NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS"

Amounts of impaired loans and reconciliation of changes in the allowances for loan impairment are presented in Alterna Bank's audited financial statements for 2014, Note 5 "Allowance for Impaired Loans and Impaired Loans". Impaired loans were approximately \$8,000 or 0.005% of Total Gross Credit Exposure at December 31, 2014. Therefore no additional disclosures related to industry and geographic areas of these loans have been presented.

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

**5. Credit Risk: Disclosures for Portfolios Subject to the Standardized Approach**

The External Credit Assessment Institutions (ECAI) used by Alterna Bank are Dominion Bond Rating Service ('DBRS') and Standard & Poor's ('S&P'). DBRS and S&P Ratings are recognized by OSFI as eligible ECAI's and are used to assess the credit quality of all exposure classes, where applicable, using the credit quality assessment scale that is set out by OSFI in its Guideline A 'Capital Adequacy Requirement (CAR) – Simpler Approaches'.

As per Alterna Bank's Investment Policy, all investments held in short-term instruments must be rated R1-L or better by Dominion Bond Rating Service (DBRS) and A-3 or better by Standard & Poor's (S&P).

The table below provides the amount of bank's outstandings in each risk bucket.

(000s)							31-Dec-14	
Standardized - Bank's Outstandings	Risk Weight	Drawn Exposure	Commitments (Undrawn)	OTC Derivatives*	Other Off Balance Sheet Items	Total	RWAs	
Sovereign	0%	\$ 20,470	\$ -	\$ -	\$ -	\$ 20,470	\$ -	
Bank								
AAA to AA-	20%	3,733	-	-	-	3,733	747	
A+ to A-	50%	-	-	-	-	-	-	
BBB+ to BBB-	100%	-	-	-	-	-	-	
Below B-	150%	-	-	-	-	-	-	
Unrated	100%	-	-	-	-	-	-	
<b>Total Bank Exposure</b>		<b>\$ 24,203</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 24,203</b>	<b>\$ 747</b>	
Retail Residential Mortgages	0%	\$ 50,831	\$ -	\$ -	\$ -	\$ 50,831	\$ -	
Retail Residential Mortgages	35%	90,351	56	-	-	90,407	31,643	
Retail Residential Mortgages	75%	-	3	-	-	3	2	
Corporate	20%	-	-	244	-	244	49	
Corporate	100%	7,589	-	-	-	7,589	7,589	
Other Retail **	75%	3,913	-	-	-	3,913	2,928	
<b>Total Gross Credit Exposure</b>		<b>\$ 176,887</b>	<b>\$ 59</b>	<b>\$ 244</b>	<b>\$ -</b>	<b>\$ 177,190</b>	<b>\$ 42,958</b>	

\* includes replacement values

\*\* RWA based on net credit exposure of 3,904



**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

**6. Credit Risk Mitigation**

General qualitative disclosures with respect to credit risk mitigation are presented in Alterna Bank’s audited financial statements for 2014, Note 19 (a) “Credit Risk”.

The following information gives details of the exposure (on- and / or off-balance sheet netting is not applicable) covered by eligible financial collateral and by guarantees / credit derivatives.

(000s)	31-Dec-14							
Standardized	Drawn Exposure	Commitments (Undrawn)	OTC Derivatives*	Other Off Balance Sheet Items	Total	RWAs	Financial Collateral	Guarantees
Sovereign	\$20,470	\$ -	\$ -	\$ -	\$20,470	\$0	\$ -	\$ -
Bank	3,733	-	-	-	3,733	747	-	-
Corporate	7,589	-	244	-	7,833	7,638	-	-
Retail Residential Mortgages	141,182	59	-	-	141,241	31,645	308	-
Other Retail (excl. SBEs)	3,913	-	-	-	3,913	2,928	-	-
<b>Total Gross Credit Exposure</b>	<b>176,887</b>	<b>59</b>	<b>244</b>	<b>-</b>	<b>177,190</b>	<b>42,958</b>	<b>308</b>	<b>-</b>
<i>Reconciliation to Financial Statements (Balance Sheet)</i>								
<i>CVA Adjustment</i>						58		
<i>Other Assets (not included in Standardized Approach)</i>	719					510		
<b>Total Assets subject to credit risk</b>	<b>\$177,606</b>							
<i>Less Collective Allowance</i>	41							
<b>Total Assets</b>	<b>\$177,565</b>					<b>\$43,526</b>	<b>\$308</b>	<b>-</b>

\* includes replacement values

**7. Counterparty Credit Risk**

All of Alterna Bank’s derivatives contracts are Over the Counter (‘OTC’) call option contracts that are privately negotiated between Alterna Bank and the counterparty to the contract.

For qualitative and quantitative disclosures refer to Alterna Bank’s audited financial statements for 2014, Note 2(g) “Derivatives”, Note 19 “NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS”, Note 18 “FAIR VALUE OF FINANCIAL INSTRUMENTS”, and Note 20 “DERIVATIVE FINANCIAL INSTRUMENTS”.

**8. Operational Risk**

Alterna Bank has adopted the basic indicator approach in determining its operational risk capital requirement.

Operational risk is the risk of loss resulting from failed or inadequate infrastructure, including internal or outsourced processes, people, information technology, and customer management. Alterna Bank has established policies that have been approved by the Board to manage and control this risk. Operations and the handling of day-to-day risks are the responsibility of management. In this regard, detailed operating procedures have been developed with built-in checks and balances. One of the key controls built into the procedures is the concept of segregation of duties, whereby transactions of any consequence require the interaction of more than one person. Risk mitigation through insurance is used where appropriate.

**ALTERNA BANK**  
**Basel III Pillar 3 Supplemental Disclosures**  
**December 31, 2014**

---

**9. Remuneration**

Alterna Bank is a wholly-owned subsidiary of Alterna Savings and Credit Union Limited (“Alterna Savings”), a credit union operating in the province of Ontario. Alterna Bank due to its small size and to reduce its need for capital expenditures outsources certain management and other services to assist in conducting its business. These services are provided by Alterna Savings, and are identified in the Outsourcing Agreement between Alterna Bank and Alterna Savings.

There are no executives employed by Alterna Bank; rather, executive services are included in the Outsourcing Agreement. Payment for these services includes executives overseeing branch operations and finance. Compensation costs attributable to other senior executives, such as the President & CEO, Senior Vice President & Chief Administrative Officer, and Senior Vice President & Chief Information Officer are allocated to Alterna Bank as part of an overhead component attached to the price charged by Alterna Savings for various transactions.

The employees of Alterna Bank are governed by the remuneration policies of Alterna Savings. In addition to their salaries, Alterna Bank’s employees participate in Alterna’s group benefits plans ( which provides certain health care, dental care, life insurance, and other benefits), as well as Alterna Savings’ pension plan and corporate bonus plan.

Alterna Savings’ executive compensation program is overseen by the Governance Committee of its Board (the “Committee”). The Committee is comprised of four (4) Directors, they convene at a minimum on a quarterly basis, and in 2014 two meetings were held at which compensation matters were addressed. The Committee is responsible for reviewing and recommending the remuneration structure for Alterna Savings’ executive management to the Alterna Savings Board of Directors, as defined in an Executive Compensation Policy (the “Policy”). The objectives of the Policy address the key risks related to remuneration and are as follows: support the attraction and retention of high caliber executives; provide competitive total rewards that encourage high levels of group and individual performance, and align the interests of Alterna Savings’ executives with those of its members. The Policy is reviewed annually by the Committee for approval by the Board of Directors. The current year Policy review was completed on December 22, 2014.

Alterna Savings’ executives participate in a short-term incentive plan (“STIP”) based on key organizational value drivers that include, but are not limited to, financial and strategic measures. The STIP is offered solely at the discretion of the Board of Directors. The Board of Directors may seek the advice of external compensation experts to ensure that total remuneration for executives remains aligned with the Policy. Alterna Savings currently doesn’t have a long-term incentive plan.

For the different forms of remuneration that Alterna Bank utilizes and for quantitative disclosures, refer to its audited financial statements for 2014, Note 24 (a) “Transactions with Key Management Personnel”.