

# Desjardins Trust Inc. Financial Information and Information on Risk Management (unaudited)

For the period ended September 30, 2015

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## NOTES TO READERS

### USE OF THIS DOCUMENT

The Financial Information and Information on Risk Management (the document) is designed to support the transparency and disclosure of Desjardins Trust's financial information and information on risk management so that the various financial market participants can assess its risk profile. The information disclosed in this document is unaudited.

### DESJARDINS TRUST PROFILE

Desjardins Trust Inc. (the Company) is a trustee incorporated as a trust and loan company and registered under the *Trust and Loan Companies Act* (Canada) that provides a range of products and services, including asset custody and trust services to individuals and businesses. It is a wholly-owned subsidiary of Desjardins Financial Holding Inc. (formerly Desjardins Financial Corporation Inc.), which in turn is wholly-owned by the *Fédération des caisses Desjardins du Québec* (the Federation). The address of its head office is 1 Complexe Desjardins, Montreal, Quebec, Canada. Through a service and outsourcing agreement, the Company uses the services of the Federation and some of its subsidiaries to support its operations both in terms of managing staff as well as meeting its movable and immovable asset requirements. Under this agreement, the Federation and its subsidiaries agree to provide the Company with substantially all administrative and operating services. The Company is governed by the Office of the Superintendent of Financial Institutions (OSFI).

### BASIS OF PRESENTATION OF FINANCIAL INFORMATION

The Annual Financial Statements have been prepared by the Company's management in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and the accounting requirements of the *Autorité des marchés financiers* (AMF) in Quebec and OSFI, which do not differ from IFRS. The unaudited financial information presented in this document is excerpted from the Annual and Interim Financial Statements of the Company. Unless indicated otherwise, amounts are in Canadian dollars.

## FINANCIAL INFORMATION

**TABLE 1 – BALANCE SHEETS**

(In thousands of dollars)

	As at September 30, 2015	As at December 31, 2014 <sup>(1)</sup>
<b>Assets</b>		
Cash and deposits with financial institutions	\$ 33,634	\$ 14,319
Securities		
Securities at fair value through profit or loss	406,417	298,334
Available-for-sale securities	305,454	428,099
Securities purchased under reverse repurchase agreements	538,771	658,738
Interest receivable	1,851	1,568
Amounts receivable from clients	30,439	36,722
Deferred tax assets	613	821
Other assets	1,401	1,505
<b>Total assets</b>	<b>\$ 1,318,580</b>	<b>\$ 1,440,106</b>
<b>Liabilities and equity</b>		
<b>Liabilities</b>		
Deposits	\$ 391,803	\$ 407,797
Commitments related to securities lent or sold under repurchase agreements	789,974	907,742
Net defined benefit plan liabilities	2,091	2,194
Other liabilities	14,265	10,565
<b>Total liabilities</b>	<b>1,198,133</b>	<b>1,328,298</b>
<b>Equity</b>		
Share capital	59,972	59,972
Retained earnings	60,185	51,539
Accumulated other comprehensive income	290	297
<b>Total equity</b>	<b>120,447</b>	<b>111,808</b>
<b>Total liabilities and equity</b>	<b>\$ 1,318,580</b>	<b>\$ 1,440,106</b>

<sup>(1)</sup> Data for 2014 were reclassified to conform with the presentation for the current period.

TABLE 2 – STATEMENTS OF INCOME

(in thousands of dollars)	For the three-month periods ended September 30		For the nine-month periods ended September 30	
	2015	2014 <sup>(1)</sup>	2015	2014 <sup>(1)</sup>
<b>Income</b>				
Fee and other income	\$ 27,153	\$ 27,735	\$ 79,547	\$ 93,266
Investment income				
Interest income	1,080	1,432	3,521	6,273
Interest expense	961	1,012	3,060	3,644
Net interest income	119	420	461	2,629
Other investment income				
Net realized gains on available-for-sale securities	254	137	772	1,102
Net income (loss) on securities at fair value through profit or loss	94	4	52	5
Other	207	88	382	132
	555	229	1,206	1,239
Net investment income	674	649	1,667	3,868
<b>Total income</b>	<b>27,827</b>	<b>28,384</b>	<b>81,214</b>	<b>97,134</b>
<b>Non-interest expense</b>				
Service agreements and outsourcing	14,539	13,562	45,220	44,274
Consulting fees	3,734	5,205	10,314	26,481
Custodian fees	2,423	2,049	6,771	5,670
Other	2,386	2,539	7,109	6,380
	23,082	23,355	69,414	82,805
<b>Income before income taxes</b>	<b>4,745</b>	<b>5,029</b>	<b>11,800</b>	<b>14,329</b>
Income taxes	1,242	1,356	3,154	3,811
<b>Net income for the period</b>	<b>\$ 3,503</b>	<b>\$ 3,673</b>	<b>\$ 8,646</b>	<b>\$ 10,518</b>

<sup>(1)</sup> Data for 2014 were reclassified to conform with the presentation for the current period.

TABLE 3 – STATEMENTS OF COMPREHENSIVE INCOME

(in thousands of dollars)	For the three-month periods ended September 30		For the nine-month periods ended September 30	
	2015	2014	2015	2014
<b>Net income for the period</b>	<b>\$ 3,503</b>	<b>\$ 3,673</b>	<b>\$ 8,646</b>	<b>\$ 10,518</b>
<b>Other comprehensive income, net of income taxes</b>				
<b>Items that will be reclassified subsequently to the Statements of Income</b>				
Net unrealized gains (loss) on available-for-sale securities	(160)	(37)	557	208
Reclassification to the Statements of Income of gains on available-for-sale securities	(185)	(101)	(564)	(806)
	(345)	(138)	(7)	(598)
<b>Comprehensive income for the period</b>	<b>\$ 3,158</b>	<b>\$ 3,535</b>	<b>\$ 8,639</b>	<b>\$ 9,920</b>

**TABLE 4 – STATEMENTS OF CHANGES IN EQUITY**

For the nine-month periods ended September 30

	Share capital	Retained earnings	Accumulated other comprehensive income	Total equity
(in thousands of dollars)				
<b>Balance as at December 31, 2014</b>	<b>\$ 59,972</b>	<b>\$ 51,539</b>	<b>\$ 297</b>	<b>\$ 111,808</b>
Net income for the period	-	8,646	-	8,646
Other comprehensive income for the period	-	-	(7)	(7)
Total comprehensive income for the period	-	8,646	(7)	8,639
<b>Balance as at September 30, 2015</b>	<b>\$ 59,972</b>	<b>\$ 60,185</b>	<b>\$ 290</b>	<b>\$ 120,447</b>
Balance as at December 31, 2013	\$ 59,972	\$ 40,013	\$ 793	\$ 100,778
Net income for the period	-	10,518	-	10,518
Other comprehensive income for the period	-	-	(598)	(598)
Total comprehensive income for the period	-	10,518	(598)	9,920
Balance as at September 30, 2014	\$ 59,972	\$ 50,531	\$ 195	\$ 110,698

**TABLE 5 – SECURITIES**

As at September 30, 2015

	Terms to maturity			
(in thousands of dollars)	Under 1 year	Over 1 year	No specific maturity	Total
<b>Securities issued or guaranteed by</b>				
Canadian Government entities	\$ 34,806	\$ 35,809	\$ -	\$ 70,615
Provincial government entities or municipal agencies in Canada	268,808	64,308	-	333,116
<b>Other securities</b>				
Financial institutions	274,700	33,400	-	308,100
Other issuers	-	40	-	40
<b>Total securities</b>	<b>\$ 578,314</b>	<b>\$ 133,557</b>	<b>\$ -</b>	<b>\$ 711,871</b>

As at December 31, 2014

	Terms to maturity			
(in thousands of dollars)	Under 1 year	Over 1 year	No specific maturity	Total
<b>Securities issued or guaranteed by</b>				
Canadian Government entities	\$ 210,374	\$ -	\$ -	\$ 210,374
Provincial government entities or municipal agencies in Canada	128,406	93,115	-	221,521
<b>Other securities</b>				
Financial institutions	262,235	32,263	-	294,498
Other issuers	-	40	-	40
<b>Total securities</b>	<b>\$ 601,015</b>	<b>\$ 125,418</b>	<b>\$ -</b>	<b>\$ 726,433</b>

**TABLE 5 – SECURITIES (continued)**

As at September 30, 2015	Distribution by province (excluding securities issued or guaranteed by Canadian government entities)					
	Quebec	Ontario	British Columbia	Alberta	Nova Scotia	Total
(in thousands of dollars)						
Securities issued or guaranteed	\$ 80,028	\$ 173,911	\$ 33,670	\$ 45,507	\$ -	\$ 333,116
Other securities	280,799	13,206	-	-	14,135	308,140
	\$ 360,827	\$ 187,117	\$ 33,670	\$ 45,507	\$ 14,135	\$ 641,256

As at December 31, 2014	Distribution by province (excluding securities issued or guaranteed by Canadian government entities)					
	Quebec	Ontario	British Columbia	Alberta	Nova Scotia	Total
(in thousands of dollars)						
Securities issued or guaranteed	\$ 122,488	\$ 39,709	\$ 34,231	\$ 25,093	\$ -	\$ 221,521
Other securities	294,538	-	-	-	-	294,538
	\$ 417,026	\$ 39,709	\$ 34,231	\$ 25,093	\$ -	\$ 516,059

**TABLE 6 – SECURITIES PURCHASED UNDER REVERSE REPURCHASE AGREEMENTS**

(in thousands of dollars)	As at September 30, 2015	As at December 31, 2014
Residents	\$ 538,771	\$ 658,738
Non-residents	-	-
<b>Total</b>	<b>\$ 538,771</b>	<b>\$ 658,738</b>

In the normal course of business, the Company carries out securities lending transactions, which include repurchase and reverse purchase agreements and securities lending. As part of such transactions, the Company acts as custodian for the securities holder who authorizes it to lend the securities to a borrower for a commission, the form and terms of which are determined in a pre-arranged contract under which the Company may assume certain risks.

**TABLE 7 – ALLOWANCE FOR CREDIT LOSSES**

(in thousands of dollars)	As at September 30, 2015	As at December 31, 2014
<b>Total</b>	<b>\$ -</b>	<b>\$ -</b>

**TABLE 8 – DEPOSITS**

(in thousands of dollars)	As at September 30, 2015	As at December 31, 2014
<b>Type</b>		
Payable on demand	\$ 121,170	\$ 125,479
Payable on a fixed date	270,633	282,318
<b>Total</b>	<b>\$ 391,803</b>	<b>\$ 407,797</b>

(in thousands of dollars)	As at September 30, 2015	As at December 31, 2014
<b>Distribution by province</b>		
Quebec	\$ 379,101	\$ 395,983
Ontario	12,654	11,796
New Brunswick	48	18
<b>Total</b>	<b>\$ 391,803</b>	<b>\$ 407,797</b>

**TABLE 9 – INTEREST RATE SENSITIVITY AND MATURITY MATCHING**

As at September 30, 2015	Terms to maturity							
	Floating rate	Under 3 months	Over 3 to 6 months	Over 6 to 12 months	Over 1 to 2 years	Over 2 years	Non-interest-sensitive	Total
(in thousands of dollars)								
<b>Assets</b>								
Cash and deposits with financial institutions	\$ -	\$ 33,634	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 33,634
Securities	-	333,448	124,620	120,246	68,102	65,415	40	711,871
Securities purchased under reverse repurchase agreements	-	538,750	-	-	-	-	21	538,771
Interest receivable	-	-	-	-	-	-	1,851	1,851
Amounts receivable from clients	-	-	-	-	-	-	30,439	30,439
Deferred tax assets	-	-	-	-	-	-	613	613
Other assets	-	-	-	-	-	-	1,401	1,401
<b>Total assets</b>	\$ -	\$ 905,832	\$ 124,620	\$ 120,246	\$ 68,102	\$ 65,415	\$ 34,365	\$ 1,318,580
<b>Liabilities and equity</b>								
Deposits	\$ 121,170	\$ 69,322	\$ 30,919	\$ 45,841	\$ 59,976	\$ 64,575	\$ -	\$ 391,803
Commitments related to securities lent or sold under repurchase agreements	-	789,940	-	-	-	-	34	789,974
Net defined benefit plan liabilities	-	-	-	-	-	-	2,091	2,091
Other liabilities	-	-	-	-	-	-	14,265	14,265
Equity	-	-	-	-	-	-	120,447	120,447
<b>Total liabilities and equity</b>	\$ 121,170	\$ 859,262	\$ 30,919	\$ 45,841	\$ 59,976	\$ 64,575	\$ 136,837	\$ 1,318,580
<b>Sensitivity gap - Balance Sheet items</b>	\$ (121,170)	\$ 46,570	\$ 93,701	\$ 74,405	\$ 8,126	\$ 840	\$ (102,472)	\$ -

As at December 31, 2014	Terms to maturity							
	Floating rate	Under 3 months	Over 3 to 6 months	Over 6 to 12 months	Over 1 to 2 years	Over 2 years	Non-interest-sensitive	Total
(in thousands of dollars)								
<b>Assets</b>								
Cash and deposits with financial institutions	\$ -	\$ 14,319	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 14,319
Securities	-	327,895	153,998	119,123	64,779	60,598	40	726,433
Securities purchased under reverse repurchase agreements	-	658,604	-	-	-	-	134	658,738
Interest receivable	-	-	-	-	-	-	1,568	1,568
Amounts receivable from clients	-	-	-	-	-	-	36,722	36,722
Deferred tax assets	-	-	-	-	-	-	821	821
Other assets	-	-	-	-	-	-	1,505	1,505
<b>Total assets</b>	\$ -	\$ 1,000,818	\$ 153,998	\$ 119,123	\$ 64,779	\$ 60,598	\$ 40,790	\$ 1,440,106
<b>Liabilities and equity</b>								
Deposits	\$ 125,479	\$ 79,575	\$ 21,363	\$ 60,293	\$ 60,259	\$ 60,828	\$ -	\$ 407,797
Commitments related to securities lent or sold under repurchase agreements	-	907,588	-	-	-	-	154	907,742
Net defined benefit plan liabilities	-	-	-	-	-	-	2,194	2,194
Other liabilities	-	-	-	-	-	-	10,565	10,565
Equity	-	-	-	-	-	-	111,808	111,808
<b>Total liabilities and equity</b>	\$ 125,479	\$ 987,163	\$ 21,363	\$ 60,293	\$ 60,259	\$ 60,828	\$ 124,721	\$ 1,440,106
<b>Sensitivity gap - Balance Sheet items</b>	\$ (125,479)	\$ 13,655	\$ 132,635	\$ 58,830	\$ 4,520	\$ (230)	\$ (83,931)	\$ -

**CAPITAL****BASEL III**

The new Basel III regulatory framework increases capital requirements. Even though the Basel III regulatory framework provides for a transitional period from 2013 to 2019 to mitigate the impact of the new capitalization rules, OSFI required the Company to meet the Common Equity Tier 1 capital ratio levels established for 2019 in the first quarter of 2013. For the Tier 1 and total capital ratios, OSFI required the Company to meet the levels established for 2019 in the first quarter of 2014.

The minimum Common Equity Tier 1 capital ratio that the Company must maintain to meet regulatory requirements is 7%. In addition, the Tier 1 capital ratio and total capital ratio must exceed 8.5% and 10.5%, respectively. These minimum ratios include a 2.5% capital conservation buffer.

Since January 1, 2015, OSFI has also required that the Company maintains a leverage ratio greater than 3%. This ratio is defined as the capital measure (namely Tier 1 capital) divided by the exposure measure. The exposure measure includes on-balance sheet exposures and securities financing transaction exposures. The new leverage ratio replaced the asset/capital ratio effective January 1, 2015.

**TABLE 10 – STATEMENT OF CAPITAL**

(In thousands of dollars, as a percentage and as a coefficient)	All-in method <sup>(1)</sup>	
	As at September 30, 2015	As at December 31, 2014
<b>Common Equity Tier 1 capital</b>		
Common shares	\$ 59,972	\$ 59,972
Retained earnings	60,185	51,539
Accumulated other comprehensive income	290	297
<b>Net Common Equity Tier 1 capital</b>	<b>\$ 120,447</b>	<b>\$ 111,808</b>
<b>Total risk-weighted assets</b>	<b>\$ 444,848</b>	<b>\$ 396,435</b>
<b>Ratios</b>		
Common Equity Tier 1 capital ratio	27.1%	28.2%
Tier 1 capital ratio	27.1%	28.2%
Total capital ratio	27.1%	28.2%
Assets/capital ratio <sup>(2)</sup>	N/A	4.8
Leverage ratio <sup>(2)</sup>	7.5%	N/A
<b>Minimum ratios</b>		
Common Equity Tier 1 capital ratio	7.0%	7.0%
Tier 1 capital ratio	8.5%	8.5%
Total capital ratio	10.5%	10.5%
Assets/capital ratio <sup>(2)</sup>	N/A	20.0
Leverage ratio <sup>(2)</sup>	3.0%	N/A

<sup>(1)</sup> Under the all-in method, regulatory capital is calculated taking into account all the regulatory adjustments under Basel III effective January 1, 2013 and the phase-out of the capital value of instruments that are not eligible for regulatory capital under the Basel III rules.

<sup>(2)</sup> The asset/capital ratio has been replaced by the new leverage ratio effective January 1, 2015 in accordance with OSFI's Leverage Requirements Guideline.

## RISK MANAGEMENT

### STRUCTURE AND ORGANIZATION OF THE RISK MANAGEMENT FUNCTION

The Company is exposed to different types of risks in its normal course of operations, including credit risk, market risk, liquidity risk, operational risk, strategic risk, reputation risk, environmental risk and legal and regulatory environment risk. Strict and effective management of these risks is a priority for the Company in order to support its major orientations, particularly regarding its financial stability as well as its profitable growth, while complying with regulatory requirements. The Company considers risk an inextricable part of its development and consequently strives to promote a culture in which everyone in the organization is responsible for risk management.

### INTEGRATED RISK MANAGEMENT FRAMEWORK

The Company's objective in risk management is to optimize the risk-return trade-off, within set tolerance limits, by developing and applying integrated risk management and control strategies, frameworks and procedures to all its activities. In that respect, the Company adopted an Integrated Risk Management Framework designed to provide its management and Board of Directors an acceptable level of confidence and comfort with respect to understanding and managing the entire range of risks associated with achieving its objectives.

This risk management framework is consistent with that of Desjardins Group and covers all of the Company's activities. Like Desjardins Group, the Company uses an overall, coordinated approach to manage its risks in an integrated manner, i.e. by taking into account the interrelationships and interdependencies between the various risks.

As important components of this management framework, risk appetite and tolerance determine the type and level of risk that the Company is prepared to accept to achieve its business and strategic objectives. They provide a basis for integrated risk management by promoting a better understanding of the risks and their impact on the risk profile.

The risk appetite and tolerance framework determines the Company's orientations with respect to risk taking and risk management, including:

- Business practices that reflect the Desjardins Group values;
- Measures based on a long-term perspective;
- Activities for which the risks are adequately understood and managed;
- Performing its trustee functions in accordance with the highest ethical and prudential standards;
- Maintaining its reputation and the trust of its clients and partners.

The risk appetite and tolerance framework also provides for a system of qualitative and quantitative risk indicators that are regularly monitored to ensure that the Company's risk profile remains within the risk appetite and tolerance limits set out by management and the Board of Directors. The Board of Directors is responsible for approving the risk appetite and tolerance framework and ensuring that it reflects the Company's financial and strategic objectives.

The Company's structure and governance principles comply with the regulatory criteria applicable to a federal trust company. The Company's Board of Directors is responsible for directing, planning, coordinating and monitoring all its activities. In particular, it is responsible for overseeing risk management, examining internal control systems as well as adopting and properly implementing relevant risk management frameworks. The Board of Directors is supported in its specific risk management responsibilities by the Risk Management Committee, the Audit Committee and the Review Committee. All of these committees benefit from Desjardins Group's support.

The Company's management is responsible for ensuring that sound risk management practices are complied with. In particular, it ensures that appropriate frameworks are developed, implemented, monitored and reviewed. It also ensures that the Company can identify all significant risks, assess their potential impact and implement practices, procedures and control measures to effectively manage them.

The risk management approach of Desjardins Group and the Company is based on principles promoting the accountability of business units. The risk management function of Desjardins Group and the Company ensures that these units successfully manage and control on a daily basis the risks associated with their activities.

### Risk management frameworks and practices

The Company uses risk management frameworks and practices to support its business development and meet its strategic objectives. They are either specific to a risk area or integrated (risk aggregation).

The Company takes the necessary measures to ensure that it implements, applies and maintains practices that allow it to meet the regulatory requirements to which it is subject.



The main risk management frameworks address in particular the following:

- Integrated risk management;
- Risk appetite and tolerance;
- Operational risk management;
- Business continuity and crisis management;
- Reputation risk management;
- Internal capital adequacy assessment program;
- Model governance;
- Risk analyses for financial projects and products;
- Stress testing;
- Matching and liquidity;
- Securities lending;
- Investments.

## CREDIT RISK

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*Credit risk is the risk of losses resulting from a borrower's or a counterparty's failure to honour its contractual obligations, whether or not these obligations appear on the Balance Sheets.*

Limits by commitments, issuers and counterparties, borrowers, groups of borrowers and industries are prescribed by policies. They are reviewed by management and the Risk Management Committee, which recommend them to the Board of Directors.

### Mitigating credit risk

In its securities lending transactions, which include repurchase and reverse repurchase agreements and securities borrowing and lending, the Company uses various techniques to reduce its counterparty credit risk.

Securities lending transactions are regulated by Investment Industry Regulatory Organization of Canada participation agreements. The Company also uses netting agreements with its counterparties to mitigate its credit risk exposure and requires a percentage of collateralization (a pledge) on these transactions.

The Company accepts from its counterparties only financial collateral that complies with the eligibility criteria set out in its policies. These eligibility criteria allow for the timely realization of collateral, if necessary, in the event of default. The types of collateral received and pledged by the Company are mainly cash and government securities.

## MARKET RISK

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*Market risk refers to the risk of changes in the fair value of financial instruments resulting from fluctuations in the parameters affecting this value, in particular, interest rates, exchange rates, credit spreads and their volatility.*

The Company is exposed to market risk primarily through its financial intermediation and securities lending activities. The Company has adopted policies that set out the principles, limits and procedures to use in managing market risk.

Interest rate risk is the main component of market risk to which the Company is exposed. Sound and prudent management is applied to optimize net interest income while minimizing the negative incidence of interest rate movements. The established policies describe the principles, limits and procedures that apply to interest rate risk management. The Company's Management Committee is responsible for analyzing and approving the various interest rate matching strategies while respecting the parameters defined in the policies.

Additional information of the Company's position with respect to interest rate sensitivity and maturity matching is provided in Table 9, "Interest rate sensitivity and maturity matching", in this document.

## LIQUIDITY RISK

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*Liquidity risk refers to the Company's capacity to raise the necessary funds (by increasing liabilities or converting assets) to meet a financial obligation, whether or not it appears on the Balance Sheets.*

The Company manages liquidity risk in order to ensure that it has timely and cost-effective access to the funds needed to meet its financial obligations as they become due, in both routine and crisis situations. Managing this risk involves maintaining a sufficient level of liquid securities. In addition, the Company ensures, through Desjardins Group, that there are stable and diversified sources of funding, that indicators are monitored and that there is a contingency plan to implement in the event of a liquidity crisis.

Liquidity risk management is a key component of the overall risk management strategy. The Company has established policies describing the principles, limits, risk appetite and tolerance thresholds as well as the procedures that apply to liquidity risk management. The policy is reviewed on a regular basis to ensure that it is appropriate for the operating environment, prevailing market conditions and regulatory requirements. It incorporates, in particular, the requirements of OSFI's Guideline B-6, *Liquidity Principles*, as well as monitoring and compliance with the new standards for the liquidity coverage ratio (LCR), the net stable funding ratio (NSFR) and net cumulative cash flow (NCCF) under Basel III. This policy has been approved by the Board of Directors and is monitored by the Risk Management Committee. In 2014, OSFI issued its public disclosures requirements for Domestic Systemically Important Banks (D-SIBs) on LCR. As the Company is not a D-SIB, it is not subject to these requirements. However, during the quarter, the Company filed with OSFI the monthly LCR reports, which more than met the minimum requirements. The Company also filed monthly its report of NCCF.

## OPERATIONAL RISK

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*Operational risk is the risk of inadequacy or failure attributable to processes, people, internal systems or external events resulting in particular in losses, failure to achieve objectives or a negative impact on reputation.*

Operational risk is inherent to all business activities as well as internal and outsourced activities. It may lead to losses mainly resulting from theft and fraud, damage to tangible assets, illegal acts, systems failures, unauthorized access to computer systems (cybercrimes) and problems or errors in process management. Although this risk cannot be totally eliminated, procedures are in place in the Company and Desjardins Group to keep it at an acceptable level.

### Operational risk management framework

The purpose of the operational risk management framework is to identify, measure, mitigate and monitor this risk as well as make interventions and disclosures in accordance with risk appetite and tolerance and the frameworks adopted by the Board of Directors. It is supported by guidelines setting out risk management foundations.

The operational risk management framework is reviewed annually to ensure its adequacy and its relevance based on Desjardins Group's risk profile and developments in industry practices.

In keeping with the global trend, Desjardins Group considers technology risk to be a major operational risk. To better respond to it, a specific management framework has been put in place that coordinates with the operational risk management framework and is supported by a specific control framework.

## STRATEGIC RISK

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*Strategic risk refers to a possible loss attributable to an inability to adapt to a changing environment because of failure to act, an inappropriate strategic choice or the inability to effectively implement strategies.*

It is first up to management and the Board of Directors to address and define the strategic orientations of Desjardins Group and the Company, taking into account risk appetite, according to the consultation processes specific to Desjardins, and to monitor the development of such orientations. Events that could compromise the achievement of the strategic objectives and initiatives of Desjardins Group and the Company are systematically and regularly monitored by their management personnel and management. Business segments and support functions periodically identify and assess events and risks that could prevent the achievement of strategic objectives, and report thereon to the appropriate bodies.

## REPUTATION RISK

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*Reputation risk is the risk that a negative perception by the stakeholders, whether or not justified, of the Company's practices, actions or lack of action could have an unfavourable impact on its income and equity, or the trust that the Company or Desjardins Group inspires.*

A reputation is of critical importance, and reputation risk cannot be managed separately from other risks. Therefore, managing reputation risk in all their spheres of activity is a constant concern for Desjardins Group and the Company. In that regard, the objective of Desjardins Group and the Company is to ensure that all employees are constantly aware of the potential implications of their actions on the organization's reputation and image. Desjardins Group and the Company consider that it is essential to promote a risk management culture in which integrity and ethics are fundamental values.

Desjardins Group has defined guidelines, a management framework, and roles and responsibilities with regard to reputation risk. This framework is in addition to various processes already in place, such as the regulatory compliance program, ethical requirements, and reputation risk assessment as part of new initiatives and the introduction of new products. All these aspects are aimed to promote sound reputation risk management. All management personnel and employees are required to perform their duties in accordance with these principles and the values of Desjardins Group and the Company.

## ENVIRONMENTAL RISK

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*Environmental risk is the risk of financial, operational or reputational loss for Desjardins Group and the Company as a result of environmental impact or issues, whether they occur through the credit or investment activities or the operations of Desjardins Group and the Company.*

*In addition to the potential financial losses that could be incurred through poor management of environmental risk, there is increased credit risk through the impairment of assets pledged as security and greater reputational risk should assets taken as collateral become the subject of discussions in the media of social and environmental issues.*

Environmental risk is an integral part of Desjardins Group's Integrated Risk Management Framework. Risks associated with climate change were subjected to a comprehensive assessment in 2013 and 2014 in order to identify any risks, for which measures had not been taken, that should be integrated into current risk management. In connection with Desjardins Group being a signatory of the Carbon Disclosure Project, work will continue to strengthen the management regarding this risk. An internal audit, performed in 2015, on the compliance with the Global Reporting Initiative guidelines related to social responsibility disclosures confirms that Desjardins Group's disclosures are in compliance with these guidelines.

## LEGAL AND REGULATORY ENVIRONMENT RISK

*Legal and regulatory environment risk refers to the risk arising from the non-compliance by Desjardins Group, including the Company, with the laws, regulations, standards and practices governing its operations, as well as its various internal codes of conduct and its contractual commitments, which could have adverse effects in the form, in particular, of financial loss, the imposing of penalties, damage to its reputation or litigation.*

Legal and regulatory environment risk entails, inter alia, effectively preventing and handling possible disputes and claims that may lead in particular to judgments or decisions by a court of law or regulatory body that could result in financial penalties or sanctions. Present and future judicial decisions and legislative activity could increase the Company's exposure to new types of litigation. In addition, some lawsuits against the Company may be very complex and be based on legal theories that are new or have never been verified. The outcome of such lawsuits may be difficult to predict or estimate until the proceedings have reached an advanced stage, which may take several years. Class action lawsuits or multi-party litigation may feature an additional risk of judgments with substantial monetary, non-monetary or punitive damages. Plaintiffs who bring a class action or other lawsuit sometimes claim very large amounts and it is impossible to determine the Company's liability, if any, for some time. Legal liability or an important regulatory measure could have an adverse effect on the current activities of the Company, its results of operations and its financial position, in addition to damaging its reputation. Even if the Company won its court case or was no longer the subject of measures imposed by regulatory bodies, these situations could harm its reputation and have an adverse impact on its financial position, due in particular to the costs associated with such proceedings, and its brand image.

The financial services industry is one of the most strictly regulated and monitored sectors. In recent years, the regulations governing the industry have expanded significantly in response to numerous socio-economic phenomena such as the development of new, increasingly complex financial products, the continuing volatility in the securities industry, financial fraud, and the fight against money laundering and terrorist financing, to mention but a few. In addition to federal (Canada and the U.S.) and provincial government requirements, the regulatory environment also includes organizations such as the Office of the Superintendent of Financial Institutions, the *Autorité des marchés financiers* and the Financial Transactions and Reports Analysis Centre of Canada. Complying with important legislative and regulatory provisions, such as those in the *Foreign Account Tax Compliance Act* and the Basel accords, requires considerable technical, human and financial resources and also affects the way Desjardins Group, including the Company, manages its current operations.

The Office of the Chief Compliance Officer of Desjardins Group fosters a proactive compliance culture by fully integrating compliance into the organization's current operations. It is responsible for developing, updating and maintaining the compliance management framework, which is based on the identification and monitoring of regulatory obligations and the functional units subject to them. Regulatory developments and their impact on operations are therefore monitored on an ongoing basis by the compliance function in cooperation with the Office of the Chief Legal Officer. The compliance function provides support to managers in charge of business segments and support functions so that they can effectively manage their risks, by developing an appropriate framework and documentation, acting in an advisory capacity, setting up training programs and conducting periodic inspections of operations. The Desjardins Group Monitoring Office provides an independent assessment of the effectiveness of the compliance management framework. Lastly, the Company has set up a formal reporting process related to compliance for its senior management and various decision-making bodies. In addition, to maintain its reputation for integrity as well as the confidence of its members and clients, Desjardins Group has developed a code of ethics and professional conduct applicable to all its officers and employees and to all its components, including the Company. This overall management of compliance provides reasonable assurance that the Company's operations are carried out in compliance with applicable regulations.