



Basel III Pillar III Disclosures

June 30, 2015

**Basel III Pillar III Disclosures**

This document represents the Pillar III disclosures for DirectCash Bank (the “Bank”) as at June 30, 2015 pursuant to OSFI’s November 2007 Advisory on Pillar III Disclosure Requirements. This report is unaudited.

**I. Capital Adequacy**

OSFI requires banks to measure capital adequacy in accordance with guidelines for determining risk adjusted capital and risk-weighting assets. The Bank complies with the Basel III framework. OSFI’s target for the Common Equity Tier 1 ratio (“CET1”) will be 7%, calculated on an “all in” basis. Further, OSFI expects all institutions to attain “all-in” target capital ratios of 8.5% for total tier 1 and 10.5% for total capital by the first quarter of 2014 (all of which include a 2.5% capital conservation buffer).

Risk Based Capital Ratio	30-Jun
<b>Assets</b>	
Total Assets	\$ 29,601,810
<b>Basic Indicator Approach</b>	
Charge for Operational Risk	\$ 5,300,838
Charge for Credit Risk	\$ 6,337,870
Total Risk Weighted Assets	\$ 11,638,708
<b>Regulatory Capital</b>	
	\$ 9,805,031
Total Risk Based Capital Ratio	84.2%
Tier 1 Risk Based Capital Ratio	84.2%

The Bank has used the basic indicator approach to determine operational risk which calculates operational risk to be 15% of the Bank’s total annual income multiplied by 12.5. This is a permitted approach under the Basel III framework.

The Bank has taken a charge for credit risk. This is a calculated amount which equals 20% of the Bank’s total assets.

The Bank’s Total risk based capital ratio is 84.2% versus the 10.5% mandated by OSFI and as such is in compliance.

Beginning in 2015, institutions will be expected to have Basel III Leverage Ratios that exceed 3%. However, consistent with the application of the ACM, OSFI intends to maintain the practice of setting an authorized level for the Leverage Ratio on an institution-by-institution basis. The Bank's Leverage Ratio is calculated by dividing total tier 1 capital by total assets.

The Bank has adopted and reported using the new Leverage Requirements (LR) report to OSFI effective Q1 – 2015. The bank's leverage ratio of 33.1% for Q2 – 2015 exceeds OSFI's authorized ratios and the Bank's internal targets.

Leverage Ratio	30-Jun
<b>Assets</b>	
Total Assets	\$ 29,601,810
<b>Capital</b>	
Common Shares	\$ 5,500,000
Retained Earnings	\$ 4,305,031
Total Tier 1 Regulatory Capital	\$ 9,805,031
<b>Leverage Ratio (Capital/Assets)</b>	
	33.1%

The Bank's assessment based upon stress testing its business model is that the Bank will not require any additional capital for the next 5 years. The Bank is in a strong financial position and is projected to be profitable for the next 5 years and beyond.

Capital is managed in accordance with policies and plans that are regularly reviewed and approved by the Board of Directors and take into account forecasted capital needs. The goal is to meet or exceed minimum regulated capital, protect individual and corporate deposits and provide capacity for internally generated growth.

## **II. Basel III Capital Disclosure**

The Basel Committee on Banking Supervision has published the Basel III rules supporting more stringent global standards on capital adequacy and liquidity (Basel III). OSFI has implemented the Basel III rules for Canadian banks and has issued guidance and advisories on its implementation plan for all Canadian financial institutions on an accelerated basis. Significant changes under Basel III that are most relevant to the Bank include additional capital buffers and new requirements for levels of liquidity and new liquidity measurements.

Management believes that the transition to Basel III will not significantly impact the Bank as the Bank's equity consists solely of Tier 1 components (common shares and retained earnings) therefore, there will be no phasing-out of non-qualifying regulatory capital instruments or phasing-in of regulatory adjustments. In addition, the strengthening of the risk weights for several asset categories will not affect the Bank due to its conservative investment policies, as well as non-presence of any loan portfolio. Pro forma Basel III calculations for the Bank confirm that the Bank will comply with Basel III's new minimum capital ratios for the next 5 years. Management also believes that the Bank will exceed the regulatory Basel III capital targets throughout the remainder of the transitional period (to 2018) and at the date of full implementation.

The new Basel III Pillar 3 public capital disclosure requirements are intended to improve both the transparency and comparability of the Bank's capital positions. The following table is prepared on the All-in Capital Disclosure template (Annex 1) provided in OSFI's Public Capital Disclosure Requirements. The template has been modified to exclude line items that are not relevant. However, for purposes of comparability, row numbering has been maintained from the OSFI template.

Basel III All-in Capital Disclosure Template			Cross-Reference <sup>(1)</sup>
<b>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	5,500,000	a
2	Retained earnings	4,305,031	b
3	Accumulated other comprehensive income (and other reserves)	n/a	
4	<i>Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)</i>	n/a	
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	n/a	
6	<b>Common Equity Tier 1 capital (CET1) before regulatory adjustments</b>	9,805,031	
<b>Common Equity Tier 1 capital: regulatory adjustments - n/a</b>			
28	Total regulatory adjustments to Common Equity Tier 1	0	
29	<b>Common Equity Tier 1 capital (CET1)</b>	9,805,031	
<b>Additional Tier 1 capital: instruments - n/a</b>			
36	<b>Additional Tier 1 capital before regulatory adjustments</b>	0	
<b>Additional Tier 1 capital: regulatory adjustments n/a</b>			
43	Total regulatory adjustments applied to Additional Tier 1 capital	0	
44	<b>Additional Tier 1 capital (AT1)</b>	0	
45	<b>Tier 1 capital (T1 = CET1 + AT1)</b>	9,805,031	
<b>Tier 2 capital: instruments and provisions - n/a</b>			
51	<b>Tier 2 capital before regulatory adjustments</b>	0	
<b>Tier 2 capital: regulatory adjustments - n/a</b>			
57	Total regulatory adjustments to Tier 2 capital	0	
58	<b>Tier 2 capital (T2)</b>	0	
59	<b>Total capital (TC = T1 + T2)</b>	9,805,031	
60	<b>Total risk weighted assets</b>	11,638,708	
<b>Capital ratios</b>			
61	Common Equity Tier 1 (as a percentage of risk weighted assets)	84.2%	
62	Tier 1 (as a percentage of risk weighted assets)	84.2%	
63	Total capital (as a percentage of risk weighted assets)	84.2%	
<b>OSFI all-in target</b>			
69	Common Equity Tier 1 all-in target ratio	7.0%	
70	Tier 1 capital all-in target ratio	8.5%	
71	Total capital all-in target ratio	10.5%	
<b>Amounts below the thresholds for deduction (before risk-weighting)</b>			
72	Non-significant investments in the capital of other financials	n/a	
73	Significant investments in the common stock of financials	n/a	
74	Mortgage servicing rights (net of related tax liability)	n/a	
75	Deferred tax assets arising from temporary differences (net of related tax liability)	n/a	
<b>Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)</b>			
80	<i>Current cap on CET1 instruments subject to phase out arrangements</i>	n/a	
81	<i>Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)</i>	n/a	
82	<i>Current cap on AT1 instruments subject to phase out arrangements</i>	n/a	
83	<i>Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)</i>	n/a	
84	<i>Current cap on T2 instruments subject to phase out arrangements</i>	n/a	
85	<i>Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)</i>	n/a	

**Statement of Financial Position as at June 30th, 2015** (as reported to Shareholders)

	Balance Sheet as reported to Shareholders	Under regulatory scope of consolidation	Cross-Reference to Definition of Capital Components
<b>Assets</b>			
<i>Cash resources:</i>			
Cash in bank	\$ 22,062,875	\$ 22,062,875	
	<b>22,062,875</b>	22,062,875	
<i>Securities:</i>			
Short term investments	6,993,120	6,993,120	
Accrued interest	23,930	23,930	
	<b>7,017,050</b>	7,017,050	
<i>Other:</i>			
Trade and Other Receivables	516,885	516,885	
Prepaid expenses	5,000	5,000	
	<b>521,885</b>	521,885	
	<b>\$ 29,601,810</b>	\$ 29,601,810	
<b>Liabilities and shareholders' equity</b>			
<i>Deposits (non-interest bearing):</i>			
Corporate	\$ 19,092,889	\$ 19,092,889	
Individual	458,203	458,203	
	<b>19,551,092</b>	19,551,092	
<i>Other:</i>			
Trade and other payables	123,399	123,399	
Income tax payable	122,287	122,287	
	<b>245,686</b>	245,686	
<b>Shareholders' equity:</b>			
Share capital	5,500,000	5,500,000	a
Retained earnings	4,305,031	4,305,031	b
	<b>9,805,031</b>	9,805,031	
	<b>\$ 29,601,810</b>	\$ 29,601,810	

Basel III Transitional Capital Disclosure Template

29	<b>Common Equity Tier 1 capital (CET1)</b>	9,805,031
45	<b>Tier 1 capital (T1 = CET1 + AT1)</b>	9,805,031
59	<b>Total capital (TC = T1 + T2)</b>	9,805,031
60	<b>Total risk weighted assets</b>	11,638,708
61	Common Equity Tier 1 (as a percentage of risk weighted assets)	84.2%
62	Tier 1 (as a percentage of risk weighted assets)	84.2%
63	Total capital (as a percentage of risk weighted assets)	84.2%

### **III. Description of the Bank**

DirectCash Bank (the “Bank”) is a Schedule 1 Canadian chartered bank. It was issued its letters patent of incorporation on October 3, 2007 and was granted its Order to Commence and Carry on Business on January 24, 2008 pursuant to the Bank Act (Canada).

The Bank provides innovative financial solutions for select niche markets. The Bank offers both individual and corporate deposit accounts. The Bank does not engage in any lending activities so it is not exposed to credit risk nor does it have currency risk or international exposure. All financial assets and liabilities are fully disclosed on the Bank’s balance sheet. The Bank has no subsidiaries, and all operations are carried out in Canada. The Bank operates online only with a head office in Calgary, Alberta.

### **IV. Risk Summary**

Risk management involves the identification, ongoing assessment, managing and monitoring of material risks that could affect the Bank and its capital position. The Bank is primarily exposed to counterparty and concentration risk.

The Bank’s most material risks relate to its ability to execute its business plan and its counterparty/concentration risk with one major customer. The Bank is party to various services and marketing agreements with this customer, whereby the Bank provides transaction processing and network sponsorship to the customer. The Bank’s operating revenue consists primarily of transaction processing revenue, program fees and branding fees received pursuant to exclusive agreements. This risk is mitigated by the fact that the revenue streams from these lines of business have been consistent for the past 9 years and the contracts are exclusive. In addition, the contracts contain minimum monthly fee payments which protect the Bank. The Bank has determined that this risk is within the Bank’s risk appetite.

The Bank does not currently pay any interest on its accounts and does not engage in any lending activities which eliminate its exposure to interest rate spread fluctuations. The Bank earns interest on its corporate and individual deposits. The Bank’s interest income could be negatively impacted by declines in interest rates but the Bank does not view this risk as material.

As the Bank does not engage in any lending activities it does not have any credit risk. As well, as the Bank does not engage in any trading or foreign exchange activities, it does not have any market risk which could result from changes in interest rates, foreign exchange rates or market prices and volatilities arising from funding and investment activities. The Bank does have regulatory risk exposure to Associations such as Interac, the Canadian Payments Association, Visa and MasterCard for non-compliance of rules and regulations. These risks are mitigated by the Bank’s policies and procedures and are subject to annual audit requirements from Interac and the payment card industry.

The Bank does have reputational risk arising from its agency relationships, however, the Bank's reputational risk is mitigated by the Bank's policies and procedures and audit requirements of each agent.

The Bank does have litigation risk arising from one of its agency relationships and has been named in four class action lawsuits. The Bank is fully indemnified for each of these lawsuits from the agent as well as another third party.

#### **V. Capital Structure**

The Bank's regulatory capital is comprised of share capital and retained earnings (Tier 1 Capital). At the issuance of the Bank's letters patent of incorporation, the Bank's initial capital was \$5,500,000. As at June 30, 2015, the Bank's capital is \$9,805,031. The capital ratios mandated by OSFI consist of the assets-to-capital multiple and the risk-based capital ratio.

#### **VI. Statement of Risk Appetite**

The Bank has a low tolerance for risk and its risk tolerance is reviewed quarterly by management and the board of directors.

#### **VII. Material Risks**

Risk management involves the identification, ongoing assessment, management and monitoring of material risks that could adversely affect the Bank. Senior management is responsible for establishing the framework for identifying risks and developing appropriate risk management policies and framework. The Bank's Board of Directors, either directly or indirectly through its committees, reviews and approves Bank policies, including specific reporting procedures. This enables them to monitor ongoing compliance with policies and review management's assessment of risk in its major risk taking activities. An internal auditor is employed to provide a continuing review of policies and procedures to ensure that they are appropriate and being followed and that adequate controls are in place in order to mitigate risk to acceptable levels. The internal auditor reports directly to the audit committee of the Board of Directors.

##### **a) Credit Risk**

Credit risk is the potential for loss due to the failure of a borrower to meet its financial obligations. The Bank does not have any credit risk as it does not engage in any lending activities.



b) Market and Interest Risk

Market risk is the risk of a loss resulting from changes in interest rates, foreign exchange rates and market prices and volatilities that arise from the Bank's funding and investment activities. The Bank does not engage in any foreign exchange or trading activities. As well, the Bank does not pay any interest on any accounts and therefore does not have any interest rate spread risk. The Bank's investment policy maintains that the Bank's capital and deposits are invested in direct government risk or deposits with financial institutions, including bankers' acceptances, treasury bills, debt securities with government, GICs or investment products of similar quality and low risk profiles.

The Bank does earn interest income on its capital invested and this income may decline with interest rate declines.

c) Operational Risk

Operational risk is the risk associated with the Bank's operations including information technology risk, anti-money laundering risk and regulatory risk. The Bank is exposed to operational risk but the Bank has policies and procedures in place to monitor and mitigate these risks.

d) Reputation Risk

Reputation risk is the impact on the Bank's earnings and capital arising from negative public opinion; thereby affecting the Bank's ability to establish new relationships or continue servicing existing customers. The Bank's value is only minimally exposed by reputation risk. The Bank's reputational risk arises from its relationship with agents. Exposure from reputation risk is expected to remain low in the foreseeable future; however, the Bank continues to exercise an abundance of caution in dealing with its agents to effectively monitor these risks.

e) Funding Risk

Funding risk is the risk of the Bank being unable to honor all cash outflow obligations as they come due. The Bank has established policies (the Funding and Liquidity Policy) to ensure that its cash outflows and inflows are closely matched and that appropriate procedures and reporting is in place to update the Board of directors quarterly. The Bank's funding risk is considered low as all of the deposits are invested in bankers' acceptances, treasury bills and GICs. As well, to further reduce the risk the Bank invests its original capital and excess cash in GIC with two financial institutions - Alberta Treasury Branch and Bank of Montreal. The Government of Alberta fully guarantees all deposits with the Alberta Treasury Branch.

f) Insurance Risk, Residual Risk, Securitization Risk

The Bank does not engage in any lending activities and as such does not have any of these types of risk exposures.

g) Business and Concentration Risk

The Bank's most material risk relates to its ability to execute its business plan and its counterparty/concentration risk with one major customer. The Bank is party to various services and marketing agreements with this customer, whereby the Bank provides transaction processing and network sponsorship to the customer. The Bank's operating revenue consists primarily of transaction processing revenue, program fees and branding fees received pursuant to exclusive agreements. This risk is mitigated by the fact that the revenue streams from these contracts have been consistent for the past 9 years and the contracts are exclusive. In addition, the contracts contain minimum monthly fee payments which protect the Bank. The Bank has determined that this risk is within the Bank's risk appetite.

h) Litigation Risk

The Bank does have litigation risk arising from one of its agency relationships and has been named in four class action lawsuits (in Manitoba, Alberta, Ontario and British Columbia). The Bank is fully indemnified for each of these lawsuits from the agent as well as another third party.

**VIII. Remuneration**

The Bank's key management personnel (which is comprised of senior executive officers and directors) receive compensation in the form of short-term employee benefits. The Bank has a compensation committee which reviews the compensation of the President & Chief Executive Officer and recommends the same to the Board of Directors for approval. Unaffiliated Directors are paid a quarterly retainer.

For the year ended December 31, 2014 the Bank has paid out executive personnel remuneration of \$605,283 plus \$128,630 of other short-term employee benefits (2013 - \$737,500 and \$104,838, respectively).