



Clarien Bank Limited

Consolidated Financial Statements
(With Independent Auditors' Report Thereon)

Year Ended December 31, 2014

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(With Independent Auditors' Report Thereon)

Year Ended December 31, 2014



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Independent Auditors' Report

To the Shareholder of Clarien Bank Limited

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Clarien Bank Limited (the "Bank"), which comprise the consolidated statement of financial position as at December 31, 2014, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Bank as at December 31, 2014, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Audit Limited

Chartered Professional Accountants
Hamilton, Bermuda
March 12, 2015

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Consolidated Statement of Financial Position

As at December 31, 2014
(Expressed in thousands of Bermuda dollars)



	<u>Notes</u>	<u>2014</u>	<u>2013</u>
Assets			
Cash and cash equivalents	5	\$ 107,135	\$ 168,032
Investment securities	6	136,179	145,264
Accounts receivable and prepaid expenses	7	5,397	6,821
Accrued interest on cash, deposits with banks and securities		470	698
Loans and advances	8, 14	876,457	942,624
Due from related parties	14	7,885	8,457
Assets held for sale	12	1,500	1,500
Investment property	9	3,880	4,543
Property and equipment	10	19,181	27,021
Intangible assets	11	<u>24,192</u>	<u>27,034</u>
Total assets		<u>\$ 1,182,276</u>	<u>\$ 1,331,994</u>
Liabilities			
Due to depositors	13, 14	\$ 1,081,406	\$ 1,223,333
Accounts payable and accrued liabilities	15	3,461	4,502
Due to clients		29	225
Deferred income		<u>109</u>	<u>106</u>
Total liabilities		<u>1,085,005</u>	<u>1,228,166</u>
Equity			
Preferred shares	16	20,000	20,000
Common shares	16	5,000	5,000
Contributed surplus	16	10,800	16,922
General reserve	16	10,000	10,000
Retained earnings		51,415	51,549
Accumulated other comprehensive income		<u>56</u>	<u>357</u>
Total equity		<u>97,271</u>	<u>103,828</u>
Total liabilities and equity		<u>\$ 1,182,276</u>	<u>\$ 1,331,994</u>

See accompanying notes to consolidated financial statements

Signed on behalf of the Board

Director

Director

Consolidated Statement of Comprehensive Income

For the Year Ended December 31, 2014
(Expressed in thousands of Bermuda dollars)



	<u>Notes</u>	<u>2014</u>	<u>2013</u>
Interest income	17	\$ 59,915	\$ 62,868
Interest expense	17	<u>(11,172)</u>	<u>(14,190)</u>
Net interest income		48,743	48,678
Fee and commission income	18	14,754	13,667
Fee and commission expense	18	<u>(3,069)</u>	<u>(3,150)</u>
Net fee and commission income		11,685	10,517
Net gains (losses) on investment securities and related swaps	6	591	(54)
Foreign exchange income		600	476
Rent		<u>664</u>	<u>629</u>
Revenue		62,283	60,246
Net impairment loss on financial assets	8	9,821	7,661
Impairment / loss on disposal of property and equipment and intangible assets	10, 11	278	-
Impairment loss on investment property	9	<u>471</u>	<u>513</u>
Net operating income		51,713	52,072
Personnel expenses	14, 20	28,455	27,430
Depreciation and amortisation	9, 10, 11	5,323	5,336
Other expenses	14, 19	<u>17,412</u>	<u>15,702</u>
Total other expenses		51,190	48,468
Profit for the year		\$ 523	\$ 3,604
Other comprehensive loss			
Items that may be reclassified subsequently to profit or loss:			
Net change in unrealized gains (losses) on available-for-sale securities		\$ 286	\$ (501)
Net change in unrealized gains on equity shares		4	-
Reclassification to earnings of net realized (gains) losses in the year		<u>(591)</u>	<u>50</u>
Other comprehensive loss for the year		<u>(301)</u>	<u>(451)</u>
Total comprehensive income for the year		\$ 222	\$ 3,153

All amounts included in the consolidated statement of comprehensive income relate to continuing operations.
See accompanying notes to consolidated financial statements

Consolidated Statement of Changes in Equity

For the Year Ended December 31, 2014
(Expressed in thousands of Bermuda dollars)



	Preferred shares	Common shares	Contributed surplus	General reserve	Retained earnings	Accumulated other comprehensive income	Total
Balance at January 1, 2014	\$ 20,000	\$ 5,000	\$ 16,922	\$ 10,000	\$ 51,549	\$ 357	\$ 103,828
Total comprehensive income for the year							
Profit for the year	—	—	—	—	523	—	523
Total other comprehensive loss	—	—	—	—	—	(301)	(301)
Total comprehensive income for the year, net of tax	—	—	—	—	523	(301)	222
Transactions with owner, recorded directly in equity							
Contributions by and distributions to owners							
Preferred share dividends declared (Note 16)	—	—	—	—	(657)	—	(657)
Distribution to shareholder (Note 16)	—	—	(6,122)	—	—	—	(6,122)
Balance at December 31, 2014	\$ 20,000	\$ 5,000	\$ 10,800	\$ 10,000	\$ 51,415	\$ 56	\$ 97,271

See accompanying notes to consolidated financial statements

Consolidated Statement of Changes in Equity

For the Year Ended December 31, 2014
(Expressed in thousands of Bermuda dollars)



	Preferred shares	Common shares	Contributed surplus	General reserve	Retained earnings	Accumulated other comprehensive income	Total
Balance at January 1, 2013	\$ 20,000	\$ 5,000	\$ 15,672	\$ 10,000	\$ 48,604	\$ 808	\$ 100,084
Total comprehensive income for the year							
Profit for the year	—	—	—	—	3,604	—	3,604
Total other comprehensive loss	—	—	—	—	—	(451)	(451)
Total comprehensive income for the year, net of tax	—	—	—	—	3,604	(451)	3,153
Transactions with owner, recorded directly in equity							
Contributions by and distributions to owners							
Preferred share dividends declared (Note 16)	—	—	—	—	(659)	—	(659)
Capital contribution from shareholder (Note 16)	—	—	1,250	—	—	—	1,250
Balance at December 31, 2013	\$ 20,000	\$ 5,000	\$ 16,922	\$ 10,000	\$ 51,549	\$ 357	\$ 103,828

See accompanying notes to consolidated financial statements

Consolidated Statement of Cash Flows

For the Year Ended December 31, 2014
(Expressed in thousands of Bermuda dollars)



	<u>Notes</u>	<u>2014</u>	<u>2013</u>
Cash flows from operating activities			
Profit for the year	\$	523	\$ 3,604
Adjustments to reconcile net income to net cash (used in) provided by operating activities:			
Depreciation and amortization		5,323	5,336
Amortization of premiums/discounts on fixed income securities		1,114	1,290
Net (gains) losses on investment securities and related swaps		(591)	54
Net impairment loss on financial assets		9,821	7,661
Impairment / loss on disposal of property and equipment and intangible assets		278	-
Impairment loss on investment property		471	513
Net changes in non-cash balances relating to operations:			
Change in loans and advances		56,346	20,655
Change in accrued interest on cash, deposits with banks and securities		228	(61)
Change in due from related parties		572	380
Change in accounts receivable and prepaid expenses		1,424	947
Change in due to depositors		(141,927)	23,184
Change in accounts payable and accrued liabilities		(1,041)	1,190
Change in deferred income		3	8
Change in due to clients		(196)	122
Net cash (used in) provided by operating activities		(67,652)	64,883
Cash flows from investing activities			
Acquisition / reinvestment of available-for-sale securities		(198,051)	(17,478)
Proceeds / maturity of available-for-sale securities		206,312	64,000
Proceeds from debt securities classified as loans and receivables		-	337
Intangible assets acquired	11	(143)	(987)
Investment property acquired	9	-	(57)
Property and equipment purchased	10	(706)	(1,274)
Net cash provided by investing activities		7,412	44,541
Cash flows from financing activities			
Preferred share dividends paid	16	(657)	(659)
Contribution from shareholder	16	-	1,250
Net cash (used in) provided by financing activities		(657)	591
Net (decrease) increase in cash and cash equivalents		(60,897)	110,015
Cash and cash equivalents, beginning of year		168,032	58,017
Cash and cash equivalents, end of year	5	\$ 107,135	\$ 168,032

See accompanying notes to consolidated financial statements

1. General

Clarien Bank Limited (the “Bank” or “CBL”), formerly CAPITAL G Bank Limited, is incorporated under the laws of Bermuda and has a banking license under the Bank and Deposit Companies Act, 1999 (“the Act”). On December 31, 2013 Capital G Limited (“CGL”), the Bank’s former parent company, announced that it had entered into a formal agreement to amalgamate with Clarien Group Limited (“Clarien”), a wholly owned subsidiary of CWH Limited. Post-amalgamation, Clarien was owned 20% by Edmund Gibbons Limited and 80% by CWH Limited, whereby CWH Limited became the ultimate parent company of the Bank. The Bank changed its name from CAPITAL G Bank Limited to Clarien Bank Limited effective April 17, 2014.

On February 9, 2015, Edmund Gibbons Limited (“EGL”) acquired 50% of CWH Limited, which when combined with its existing 20% interest in Clarien, resulted in EGL becoming the controlling shareholder of Clarien and the ultimate parent company of CBL.

The consolidated financial statements of Clarien Bank Limited as at and for the year ended December 31, 2014 comprise Clarien Bank Limited and its subsidiaries (together referred to as the “Bank” and individually as “Bank entities”). The Bank is involved in community banking and provides retail and private banking services to individuals, and commercial banking services to small and medium-sized businesses. The services offered include demand and term deposits, consumer, commercial and mortgage lending, credit and debit cards and letters of credit. The Bank also, through its subsidiary operations, engages in investment management, brokerage and advisory services and trust administration. The address of the Bank’s registered office is Strata G Building, 30A Church Street, Hamilton HM11, Bermuda. The Bank operates out of two locations in Bermuda.

The following lists all directly held subsidiaries of CBL, as well as their directly owned subsidiaries. All subsidiaries are wholly owned.

Legal entity	Activity
First Bermuda Group Ltd.	Holding company
First Bermuda Securities Ltd. formerly First Bermuda Securities (BVI) Ltd.	Brokerage services; subsidiary of First Bermuda Group Ltd.
Onshore Nominees Ltd.	Nominee entity of First Bermuda Group Ltd.
Offshore Nominees Ltd.	Nominee entity of First Bermuda Group Ltd.
Clarien Investments Limited (“CIL”), formerly CAPITAL G Investments Limited	Investment management
Clarien Brokerage Limited, formerly CAPITAL G Brokerage Limited	Brokerage services; subsidiary of CIL
Clarien Nominees Limited, formerly CGI Nominees Limited	Nominee entity of CIL
Clarien BSX Services Limited, formerly CAPITAL G BSX Services Limited	Trading member of Bermuda Stock Exchange; subsidiary of CIL
Clarien Trust Limited, formerly CAPITAL G Trust Limited	Trust administration

2. Basis of preparation

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRSs”) as issued by the International Accounting Standards Board (“IASB”).

The consolidated financial statements were authorized for issuance by the Board of Directors on March 12, 2015.

2. **Basis of preparation** (continued)

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis, except for available-for-sale investment securities and derivative instruments that have been measured at fair value.

(c) Functional and presentation currency

These consolidated financial statements are presented in Bermuda dollars, which is also the Bank's functional currency.

(d) Use of estimates and judgments

The preparation of financial information requires the use of estimates and assumptions. The use of available information and the application of judgement are inherent in the formation of estimates, actual results in the future may differ from estimates upon which financial information is prepared. Revisions to accounting estimates, if any, are recognized in the period in which the estimate is revised and in any future periods affected. Management believes that the critical accounting policies, where judgement is necessarily applied, are those which relate to the valuation of loans and advances, investment securities, intangible assets and investment property.

3. **Summary of significant accounting policies**

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and have been applied consistently by the Bank entities.

(a) Basis of consolidation

Entities that are controlled by the Bank are consolidated and are listed in Note 1. Subsidiaries are consolidated from the date the Bank gains control, until the date that control ceases. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The Bank manages and administers assets held in trusts and other investment vehicles on behalf of investors. The financial statements of these entities are not included in these consolidated financial statements, except when the Bank controls the entity.

All intra-group transactions and income and expenses (except for any foreign currency transaction gains and losses) arising from intra-group transactions are eliminated on consolidation. The consolidated financial statements have been prepared using uniform accounting policies for like transactions.

(b) New standards

Except for the changes below, the Bank has consistently applied the accounting policies to all periods presented in these financial statements.

The Bank has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of January 1, 2014.

(i) Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32).

As a result of the amendments to IAS 32, the Bank has changed its accounting policy for the offsetting of financial assets and financial liabilities. The amendments clarify when an entity currently has a legally enforceable right to set-off and when gross settlement is equivalent to net settlement.

The change did not have a material impact on the Bank's financial statements.

3. **Summary of significant accounting policies** (continued)

(c) *New standards and interpretations not yet adopted*

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after January 1, 2014, however, the Bank has not applied the following new or amended standards in preparing these consolidated financial statements.

(i) *IFRS 9 Financial Instruments*

IFRS 9, published in July 2014, replaces the existing guidance in IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.

IFRS 9 is effective for annual reporting periods beginning on or after January 1, 2018, with early adoption permitted.

The Bank is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 9.

Given the nature of the Bank's operations, this standard is expected to have a material impact on the Bank's financial statements. In particular, calculation of impairment of financial instruments on an expected credit loss basis is expected to result in an increase in the overall level of impairment allowances.

(ii) *IFRS 15 Revenue from Contracts with Customers*

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty Programmes*.

IFRS 15 is effective for annual reporting periods beginning on or after January 1 2017, with early adoption permitted.

The Bank is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 15.

(d) *Translation of foreign currencies*

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency, Bermuda dollars, at the spot rates of exchange prevailing at the reporting date, while associated revenues and expenses are translated into Bermuda dollars at the actual spot rates of exchange prevailing at the date of the transaction. Resulting gains or losses are included in foreign exchange income in the consolidated statement of comprehensive income.

(e) *Cash and cash equivalents*

Cash and cash equivalents are carried at amortized cost in the consolidated statement of financial position. For purposes of the consolidated statement of cash flows, the Bank considers all time deposits and interbank loans with an original maturity of 90 days or less, and short-term securities that are readily convertible to known amounts of cash, as equivalent to cash. Certain comparatives have been restated for comparability purposes.

3. **Summary of significant accounting policies** (continued)

(f) Customer funds

With the exception of amounts disclosed in Note 5, assets held in a trust, agency or fiduciary capacity for customers are not included in the consolidated statement of financial position, as they are not controlled by the Bank.

(g) Financial assets and liabilities

Initial recognition

The Bank initially recognizes loans, mortgages and credit card receivables classified as loans and advances and deposits classified as due to depositors on the date they originated. Regular way purchases and sales of financial assets are recognized on the trade date at which the Bank commits to purchase or sell the asset. All other financial assets and liabilities (including assets and liabilities designated at fair value through profit or loss) are initially recognized on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

For an item not carried at fair value through profit or loss, a financial asset or liability is measured at fair value plus transaction costs that are directly attributable to its acquisition or issue. For an item measured at fair value through profit or loss, transaction costs are recognized in profit or loss.

De-recognition

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred, or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for de-recognition that is created or retained by the Bank is recognized as a separate asset or liability in the consolidated statement of financial position. On de-recognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in other comprehensive income ("OCI") is recognized in profit or loss.

The Bank derecognizes a financial liability when its contractual obligations are discharged, cancelled or expire.

Offsetting

Financial assets and liabilities are offset and the net amount presented in the consolidated statement of financial position when, and only when, the Bank has a legal right to set off the recognized amounts and it intends to settle either on a net basis or to settle the asset and liability simultaneously.

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

Amortized cost measurement

The amortized cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between the initial amount recognized and the maturity amount, minus any reduction for impairment.

3. Summary of significant accounting policies (continued)

(g) *Financial assets and liabilities* (continued)

Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank estimates fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing such financial instruments. Inputs to valuation techniques represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e., the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When the transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognized in profit or loss on an appropriate basis over the life of the instrument but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Assets and long positions are measured at a bid price, liabilities and short positions are measured at an asking price. Where the Bank has positions with offsetting risks, mid-market prices are used to measure the offsetting positions and a bid or asking price adjustment is applied only to the net open position as appropriate. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Bank and the counterparty where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties, to the extent that the Bank believes a third-party market participant would take them into account in pricing a transaction.

The Bank makes loans to employees, and to employees of certain other related party companies, at interest rates below the comparable market rate. Such related party loans revert to market rate if the employee leaves the company.

December 31, 2014

*(Expressed in thousands of Bermuda dollars, except as noted)***3. Summary of significant accounting policies (continued)***(g) Financial assets and liabilities (continued)*

Reduced rate loans are financial assets and under IAS 39 are initially recognized at fair value and thereafter at amortized cost. For the Bank's employees, the difference between fair value and the amount of the loan is recorded as a prepaid benefit with a corresponding decrease in the carrying value of loans and advances. The benefit is recognized as an expense over the expected service life of the employee, with a corresponding increase in interest income on loans. For employees of related party companies, the difference between fair value and the amount of the loan is recorded as a related party receivable when reimbursement of the benefit provided by the Bank is agreed to by the related party or shareholder, or as a capital distribution where no reimbursement has been agreed to by the related party or shareholder, with a corresponding decrease in the carrying value of loans and advances. In addition, for employees of related party companies, the difference between fair value and the amount of the loan is recognized as interest income on loans over the expected service life of those employees, with a corresponding decrease in the carrying value of loans and advances.

Identification and measurement of impairment

At each reporting date, the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Bank considers evidence of impairment for loans and advances and debt securities classified as loans and receivables at both a specific asset and collective level. All individually significant loans and advances and debt securities classified as loans and receivables are assessed for specific impairment. All individually significant loans and advances and debt securities classified as loans and receivables found not to be specifically impaired are collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances and debt securities classified as loans and receivables that are not individually significant are collectively assessed for impairment by grouping together such loans and advances and debt securities classified as loans and receivables with similar characteristics.

Collective allowance for groups of homogeneous loans is established using statistical methods such as roll rate methodology or, for small portfolios with sufficient information, a formula approach based on historic loss rate experience. The roll rate methodology uses statistical analysis of historical data on delinquency to estimate the amount of loss. The estimate of loss arrived at on the basis of historical information is then reviewed to ensure that it appropriately reflects the economic conditions and product mix at the reporting date. Roll rates and loss rates are regularly benchmarked against actual loss experience.

3. **Summary of significant accounting policies** (continued)

(g) *Financial assets and liabilities* (continued)

Identification and measurement of impairment (continued)

Collective allowance for groups of assets that are individually significant but that were not found to be individually impaired cover credit losses inherent in portfolios of loans and advances with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired loans and advances, but the individual impaired items cannot yet be identified. In assessing the need for collective loss allowances, management considers factors such as credit quality, portfolio size, concentrations and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on the estimates of future cash flows for specific counterparties and the model assumptions and parameters used in determining collective allowances.

Impairment losses on assets carried at amortized cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the loan's original effective interest rate. Impairment losses are recognized in profit or loss and reflected in an allowance account against loans, mortgages and credit card receivables. Interest on impaired assets continues to be recognized through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale investment securities are recognized by transferring the cumulative loss that has been recognized in OCI to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from OCI to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment previously recognized in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was initially recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognized in OCI.

The Bank writes off certain loans and advances and investment securities when they are determined to be

Credit card receivables that are contractually 180 days past due are automatically written off.

Designation at fair value through profit or loss

The Bank has designated financial assets and liabilities at fair value through profit or loss in the following circumstances:

- The assets or liabilities are managed, evaluated and reported internally on a fair value basis.
- The designation eliminates or significantly reduces an accounting mismatch which would otherwise arise.
- The asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

Note 4 sets out the amount of each class of financial asset or liability that has been designated at fair value through profit or loss. A description of the basis for each designation is set out in the note for the relevant asset or liability class.

December 31, 2014

*(Expressed in thousands of Bermuda dollars, except as noted)***3. Summary of significant accounting policies (continued)***(h) Investment securities*

Investment securities are initially measured at fair value, plus, in the case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as available-for-sale, or for certain debt securities as loans and receivables.

Debt securities classified as loans and receivables are non-derivative financial assets with fixed or determinable payments that the Bank does not intend to sell immediately or in the near term and that are not quoted in an active market. These securities are measured at amortized cost using the effective interest method. Interest income and amortization of premiums and discounts on debt securities classified as loans and receivables are recorded in interest income.

Available-for-sale investment securities are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. These include investment securities which may be sold in response to, or in anticipation of, changes in interest rates and resulting prepayment risk, changes in funding sources or terms, or to meet liquidity needs. Available-for-sale investment securities are measured at fair value with unrealized gains and losses recognized in OCI until the investment is sold or deemed to be impaired, whereupon the cumulative gains and losses previously recognized in OCI are reclassified to profit or loss as a reclassification adjustment. Interest income, including purchased premiums or discounts on available-for-sale investment securities amortized over the life of the security, is recognized in profit or loss using the effective interest method.

The Bank reviews its available-for-sale securities to identify and evaluate investments that show indications of possible impairment. An investment is considered impaired if its unrealized loss is considered to be other than temporary. In determining whether a loss is other than temporary, factors considered include the extent of the unrealized loss, the length of time that the security has been in an unrealized loss position, the financial condition and near-term prospects of the issuer, and management's ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery.

Where a decline in value of a security classified as available-for-sale is considered to be other than temporary, the security is written down to its realizable value, with the impairment loss being recognized in the consolidated statement of comprehensive income. A subsequent increase in fair value of such securities that can be objectively related to an event that occurred after the impairment was recognized will result in a reversal of the impairment loss in the period in which the event occurs.

(i) Derivative financial instruments

Derivative instruments are financial contracts whose value is derived from interest rates, foreign exchange rates, the prices of other instruments or other financial indices. The Bank enters into various derivative contracts in the ordinary course of business, including swaps and foreign exchange forward contracts. These derivative contracts may be exchange traded or privately negotiated in the over-the-counter market with international commercial and investment banks, which act as counterparties to the contracts.

Derivative financial instruments are held for risk management purposes and are measured at fair value in the consolidated statement of financial position with gains and losses being recognised in profit or loss.

The Bank may enter into interest rate swap contracts as part of its interest rate risk management program. Interest rate swap contracts are financial transactions in which two counterparties exchange fixed or floating interest payment streams over a period of time based on rates applied to a defined notional principal amount. Their value is derived from the interest rates specified in the contracts.

3. Summary of significant accounting policies (continued)

(i) *Derivative financial instruments* (continued)

The Bank enters into foreign exchange forward contracts as part of its asset and liability management program. Their value is derived from the price difference between the applicable forward rate and the exchange rates specified in the contracts.

(j) *Loans and advances*

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term.

Loans and advances are initially measured at fair value plus incremental direct third-party transaction costs, and subsequently measured at their amortized cost using the effective interest method less any allowance for impairment.

(k) *Business combinations*

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the Bank elects whether it measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. This accounting policy choice is applied consistently to all similar business combination transactions. Acquisition costs incurred are expensed and included in other expenses in the consolidated statement of comprehensive income.

When the Bank acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognized for non-controlling interest over the fair value of net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the consolidated statement of comprehensive income.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to the respective Bank cash-generating unit (CGU) that is expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to that unit.

Where goodwill forms part of a CGU and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the CGU retained.

(l) *Property and equipment and related depreciation*

Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset.

3. **Summary of significant accounting policies** (continued)

(l) *Property and equipment and related depreciation* (continued)

Recognition and measurement (continued)

The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition, the costs of dismantling and removing the items and restoring the site on which they are located and capitalized borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalized as part of the equipment. When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

The gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of the item of property and equipment, and is recognized in other income/other expenses in profit or loss.

When the use of an investment property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting purposes.

Subsequent costs

The cost of replacing a component of an item of property or equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in profit or loss as incurred.

Depreciation

Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Artwork and land are not depreciated. The estimated useful lives of the related assets for the current and comparative figures are as follows:

Buildings	30-40 years
Furniture and fixtures	5-15 years
Computer systems and equipment	2-10 years
Leasehold improvements	lesser of lease term or estimated useful life

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

(m) *Investment properties*

Investment properties are properties held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. A portion of a dual-use property is classified as an investment property only if the portion could be sold or leased out separately under a finance lease. When a portion of the property could not be sold or leased out under a finance lease separately, the entire property is classified as an investment property if the portion of the property held for the Bank's own use is insignificant.

3. Summary of significant accounting policies (continued)

(m) Investment properties (continued)

When the use of a property changes such that it is reclassified as an investment property, its fair value at the date of reclassification becomes its cost for subsequent accounting purposes.

Investment property is initially measured at cost. Subsequent to initial recognition, investment property is measured at cost less accumulated depreciation and any impairment losses.

Depreciation is recognized in profit or loss on a straight line basis over the estimated useful lives of investment properties which are considered to be as follows:

Buildings	30-40 years
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Depreciation methods, useful lives and residual values are reassessed at each financial year-end and adjusted if appropriate.

(n) Intangible assets and related amortization

(i) Goodwill

Goodwill that arises upon the acquisition of subsidiaries is included in intangible assets. See note 3(k) for further details on the accounting policy with respect to goodwill arising on business combinations upon acquisition. Goodwill is subsequently measured at cost less any impairment losses. An intangible asset is recognized only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Bank.

(ii) Customer relationships

Customer relationships with a finite useful life are measured at amortised cost. Customer relationships with an indefinite useful life are measured at cost less any impairment losses.

(iii) Computer software

Computer software is measured at cost less any accumulated amortization and any impairment loss. Computer software is amortised on a straight-line basis over its estimated useful life of between 2-10 years. Subsequent expenditure on software assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred. Amortization methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

Intangible assets are tested annually for impairment or more frequently if certain indicators of impairment are identified.

December 31, 2014

*(Expressed in thousands of Bermuda dollars, except as noted)***3. Summary of significant accounting policies (continued)***(o) Non-current assets held for sale*

Non-current assets are classified separately as held for sale in the consolidated statement of financial position when their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is met only when the sale is highly probable, the asset is available for immediate sale in its present condition, and management is committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification. Liabilities directly associated with the assets classified as held for sale and expected to be included as part of the sale transaction are correspondingly also classified separately. Property, plant and equipment and intangible assets once classified as held for sale are not subject to depreciation or amortisation. The net assets and liabilities of a disposal group classified as held for sale are measured at the lower of their carrying amount and fair value less cost to sell.

(p) Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill and indefinite-lived intangible assets are tested annually for impairment. An impairment loss is recognised if the carrying amount of an asset or cash generating unit (CGU) exceeds its recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessment of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. Subject to an operating segment ceiling test, CGUs to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU (group of CGUs), and then to reduce the carrying amounts of the other assets in the CGU (group of CGUs) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. For other assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3. Summary of significant accounting policies (continued)

(q) Interest income and expense

Interest income and expense for all interest-bearing financial instruments is recognised in 'interest income' and 'interest expense' in the consolidated statement of comprehensive income using the original effective interest rates of the financial assets or financial liabilities to which they relate. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the original effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but not future credit losses. The calculation includes all amounts paid or received by the Bank that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

Administration fees charged for the granting of mortgages and loans, net of directly attributable origination costs, are deferred and recognized over the contractual life of the mortgage or loan as an adjustment to yield using the effective interest method.

(r) Fee and commission income and expense

Fee and commission income includes administration fees, investment and trust management fees and card fees. Fee and commission income and expense is recognized on the accrual basis during the period in which the services are provided.

Investment management fees are based on the net asset value of funds under management. Prepaid fees are deferred until earned.

Card fees primarily include interchange income, annual fees and late fees. Card fees are recognized as services are provided.

Fee and commission expense includes sub-advisor fees, banking and credit related fees and commission expenses including the costs of the Bank's credit card rewards program, and brokerage fees.

(s) Comprehensive income

The consolidated statement of comprehensive income forms part of the Bank's consolidated financial statements and displays profit for the year and OCI. Accumulated OCI is a separate component of shareholder's equity. The consolidated statement of comprehensive income reflects changes in accumulated OCI, comprised of changes in unrealized gains and losses on financial assets classified as available-for-sale.

(t) Leases

Operating lease payments are recognized as an expense on a straight-line basis over the lease term and included in other expenses in the consolidated statement of comprehensive income.

3. Summary of significant accounting policies (continued)

(u) Tax

The Bank is not subject to corporate income taxes on profits or capital gains in Bermuda and no provision for tax has therefore been accrued.

(v) Dividends on common shares

Dividends on common shares are recognized as a liability and deducted from equity in the period in which they are declared.

(w) Defined contribution pension plan

The Bank operates a defined contribution pension plan. A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognized as an expense in profit or loss when they are due in respect of services rendered before the end of the reporting period.

(x) Share capital

Share issuance costs

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognized as a deduction from equity, net of any tax effects.

Preferred shares

Preference share capital is classified as equity if it is non-redeemable, or redeemable only at the Bank's option, and any dividends are discretionary. Dividends thereon are recognized as distributions within equity in the period in which they are declared.

4. Risk management

The Bank has exposure to the following risks from the financial instruments it holds:

- credit risk
- liquidity risk
- market risk
- operational risk

This note presents information about the Bank's material exposures to each of the above risks, the Bank's objectives, policies and procedures for measuring and managing risk, and the Bank's management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Audit, Finance and Governance, Risk and Compliance Committees, which are responsible for approving and monitoring Bank risk management policies in their respective areas. All Board Committees comprise only of non-executive members and report regularly to the Board of Directors on their activities. The Board Committees are supported by the management level Credit, Asset and Liability ("ALCO") and Risk Committees, which are responsible for developing risk management policies and related operational procedures, and reporting in their respective areas.

4. **Risk management** (continued)

Risk management framework (continued)

The Bank's risk management policies are established to identify and analyze the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and procedures are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and risk management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Governance, Risk and Compliance Committee has the delegated authority for reviewing the adequacy of the risk management framework in relation to the risks taken by the Bank. The Audit Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

Credit risk

Credit risk is the risk of loss arising from a customer or counterparty failing to meet their financial obligations to the Bank as they fall due. The Bank provides credit through residential and commercial mortgages, secured and unsecured loans and credit cards. Credit risk also arises through other activities not directly related to the provision of services to clients, such as short-term investments and interbank loans relating to liquidity management. Residential and commercial mortgages comprise 92% (December 31, 2013 - 91%) of outstanding loans. All mortgage lending is originated by the Bank and retained and serviced within its personal and business lending units.

Maximum credit risk exposure at December 31, 2014 and December 31, 2013 is the carrying value of financial assets as shown on the consolidated statement of financial position as well as the value of commitments, as set out in Note 21. The consolidated statement of financial position does not take into account any collateral held as security or other credit enhancements.

The types of financial instruments that are most exposed to credit risk are Cash and cash equivalents (Note 5), Investment securities (Note 6), Loans and advances (Note 8), and Due from related parties (Note 14).

Credit risk: loans and advances

The effective management of credit risk requires the establishment of an appropriate credit risk culture. Key credit risk policies and credit risk management strategies are important elements used to create this culture. The Bank has implemented internal processes and risk-oriented strategies for actively identifying, managing, monitoring and reporting credit risk on its mortgage and non-mortgage portfolios which the Bank considers are suitable to the nature, scale and complexity of the business. This is supported by policies and internal limits or thresholds with key controls.

The Board of Directors, either directly or through the Governance, Risk and Compliance Committee of the Board, reviews and approves the Bank's credit risk strategy and credit risk policy on a quarterly basis.

4. **Risk management** (continued)**Credit risk** (continued)Credit risk: loans and advances (continued)

The objectives of the credit risk strategy are to seek to ensure that:

- The risk parameters for new underwritings and for the portfolios as a whole are clearly specified;
- Target markets and product offerings are well defined at both the enterprise-wide and business line levels;
- Transactions and limits are managed in a manner that is consistent with the Bank's risk appetite;
- Loans are priced on a risk adjusted basis;
- Loans are appropriately collateralized and collateral is maintained and valued periodically;
- Credit risk is managed from concentration and country risk perspectives; and
- Maintain sufficient information and data to be able to track and monitor changes over time.

The credit risk policy articulates the credit risk management framework, including:

- Aggregate limits for all lenders, beyond which credit applications must be escalated to the Bank's Credit Committee for approval; and
- Single name/aggregation exposures, beyond which exposures must be reported and reviewed by the Credit Committee, with Board oversight.

The table below provides further information on the Bank's loans and advances, gross of allowances, to retail and commercial customers by payment due status:

	<u>2014</u>		<u>2013</u>	
Not impaired:				
Neither past due or impaired	\$ 740,784	82%	\$ 822,538	86%
Past due, but not individually impaired:				
From 7 days up to 3 months	48,487	5%	23,718	2%
3 to 6 months	9,503	1%	15,338	2%
6 to 12 months	15,047	2%	21,933	2%
Over 12 months	22,964	3%	24,907	3%
Individually impaired loans				
Up to 3 months	2,013	-	2,890	-
3 to 6 months	1,426	-	2,591	-
6 to 12 months	9,576	1%	5,488	1%
Over 12 months	<u>49,362</u>	<u>6%</u>	<u>39,040</u>	<u>4%</u>
Total (Note 8)	<u>\$ 899,162</u>	<u>100%</u>	<u>\$ 958,443</u>	<u>100%</u>

Given the Bank's credit policies and procedures, management does not consider loans past due less than seven days as delinquent.

Restructured loans are loans whose terms have been renegotiated due to deterioration in the borrower's financial position. The Bank undertakes such restructuring to maximize collection opportunities and minimize the risk of default. Upon restructuring such loans are no longer considered past due, but are treated as up to date loans for measurement purposes. The revised terms usually include extending maturity, changing the timing of interest payments, amendments to the terms of loan covenants and taking additional collateral, including third party guarantees where needed. Both retail and corporate loans are subject to this policy.

4. Risk management (continued)

Credit risk (continued)

For the year-ended December 31, 2014, loans amounting to \$48,366 (December 31, 2013 - \$33,789), that would otherwise be in arrears and impaired based on the present value of collateral related cash flows only, have been restructured.

A substantial portion of the loans and mortgages receivable is due from residents of Bermuda and is secured by residential property in Bermuda. The Bermuda economy is largely dependent upon tourism and international business services and the health of these sectors depends to a large extent upon the strength of the United States and European economies. Therefore an adverse change in these sectors in future periods may have a material adverse impact on the carrying value of the Bank's loans and mortgages receivable.

The type of collateral held can include, but is not limited to: residential real estate, commercial properties, other properties, land, and debentures covering business assets such as receivables and equipment, automobiles, securities portfolios, other chattels and cash deposits. Guarantees from third parties are also taken, however the Bank does not rely extensively on guarantees.

Aggregate undiscounted fair value of collateral held:

	<u>2014</u>	<u>2013</u>
Past due but not impaired loans	\$ 201,856	\$ 156,118
Impaired loans	<u>48,207</u>	<u>44,473</u>
	<u>\$ 250,063</u>	<u>\$ 200,591</u>

Credit risk: interbank lending and investment securities

The Bank engages in short-term lending to other bank counterparties and investments in securities as part of its ongoing liquidity management program. Risks are managed within specific counterparty limits approved by the Credit Committee and limits, asset quality plans and criteria set out in the Bank's Investment Policy Statement, which is approved by the Finance Committee of the Board of Directors. The Bank uses external credit agency ratings supplemented by internal analysis to manage the risks associated with interbank lending and investment activities.

The table below shows the relative concentrations of the Bank's cash, cash equivalents and interbank loans placed with other banks, excluding the cash in vaults.

	<u>2014</u>		<u>2013</u>	
Concentration by credit grading				
AAA	\$ -	-	\$ -	-
AA	87,763	87%	135,744	84%
A	10,277	10%	13,273	8%
Other	<u>3,145</u>	<u>3%</u>	<u>13,233</u>	<u>8%</u>
	<u>\$ 101,185</u>	<u>100%</u>	<u>\$ 162,250</u>	<u>100%</u>
Concentration by region				
North America (including Bermuda)	<u>\$ 101,185</u>	<u>100%</u>	<u>\$ 162,250</u>	<u>100%</u>

4. **Risk management** (continued)**Credit risk** (continued)

The table below shows the relative concentrations of the Bank's investment securities.

	<u>2014</u>		<u>2013</u>	
Concentration by credit grading				
AAA	\$ 45,391	33%	\$ 25,472	18%
AA	90,117	67%	118,276	81%
A	503	-	566	-
Other	<u>168</u>	<u>-</u>	<u>950</u>	<u>1%</u>
	<u>\$ 136,179</u>	<u>100%</u>	<u>\$ 145,264</u>	<u>100%</u>
Concentration by region				
North America (including Bermuda)	\$ 136,179	100%	\$ 134,216	92%
Europe	-	-	10,040	7%
Australasia	<u>-</u>	<u>-</u>	<u>1,008</u>	<u>1%</u>
	<u>\$ 136,179</u>	<u>100%</u>	<u>\$ 145,264</u>	<u>100%</u>

US Treasuries, which are rated AA are the largest portfolio holding at December 31, 2014. The remainder of the Bank's investment portfolio are holdings in sovereigns, supra-nationals bonds and high grade corporates.

As at December 31, 2014, 100% (December 31, 2013 - 100%) of the investment securities portfolio was paying interest as expected.

Collateral held as security for investment securities is determined by the nature of the instrument. Debt securities and Treasuries are generally unsecured whereas asset-backed securities and similar instruments are secured by pools of financial assets. The carrying value of asset-backed securities at December 31, 2014 is \$101 (December 31, 2013 - \$117).

Liquidity risk

Liquidity risk is the risk that the Bank is not able to meet its financial obligations as they fall due, or can only do so at excessive cost. The Bank's policy is to ensure that sufficient funds are available to meet its ongoing commitments to customers and counterparties, both with respect to the demand for loans and the repayment of deposits, and to maintain the confidence of the marketplace in which the Bank operates.

This is achieved by (i) adhering to a Board approved loan to deposit targets, which may have temporary exceptions approved by the Bank's Asset and Liability Committee ("ALCO"), (ii) adherence to regulatory mandated liquidity mismatch guidelines with respect to the amount of potential projected cash outflow, looking out one month, as a percentage of total deposits, (iii) maintaining holdings of high quality liquid assets and short maturity interbank placements and (iv) maintaining external counterparty repurchase. The Bank has an uncommitted repurchase facility with an S&P A- rated financial institution, which was undrawn at December 31, 2014 and December 31, 2013.

4. **Risk management** (continued)

Liquidity risk (continued)

The development and implementation of the Bank's liquidity policy is the responsibility of ALCO and is approved by the Finance Committee. The day to day monitoring and management of liquidity is the responsibility of the Treasury Department. The Treasury Department prepares liquidity reports and performs stress tests on a monthly basis and reports the results to ALCO and the Finance Committee.

The Bank transacts only a small number of foreign currency trades, predominantly in GBP, CAD, CHF and EUR, and solely for customer flow purposes. These are mostly foreign exchange spot transactions and are usually fully covered. Again, this mismatch does not represent material market or liquidity risk.

Notes to Consolidated Financial Statements

December 31, 2014

(Expressed in thousands of Bermuda dollars, except as noted)



4. Risk management (continued)

Liquidity risk (continued)

Maturity analysis of financial liabilities

The table below details the Bank's financial liabilities based on liquidity.

December 31, 2014

	Carrying amount	Gross nominal inflow / (outflow)	Repayable on demand	Up to 3 mths	3-6 mths	6-12 mths	1-5 years	>5 years
Financial liabilities								
Due to depositors	\$ 1,081,406	\$ (1,086,889)	\$ (436,477)	\$ (207,072)	\$ (49,587)	\$ (176,601)	\$ (217,152)	\$ -
Accounts payable and accrued liabilities	3,461	(3,461)	(3,461)	-	-	-	-	-
Due to clients	29	(29)	(29)	-	-	-	-	-
Deferred income	109	(109)	(109)	-	-	-	-	-
	\$ 1,085,005	\$ (1,090,488)	\$ (440,076)	\$ (207,072)	\$ (49,587)	\$ (176,601)	\$ (217,152)	\$ -
Unrecognized loan commitments	-	(7,644)	-	(2,456)	(434)	(214)	(612)	(3,928)
Financial guarantees and letters of credit	-	(1,751)	-	(970)	(555)	(226)	-	-
Total financial liabilities	\$ 1,085,005	\$ (1,099,883)	\$ (440,076)	\$ (210,498)	\$ (50,576)	\$ (177,041)	\$ (217,764)	\$ (3,928)

Notes to Consolidated Financial Statements

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4. Risk management (continued)

Liquidity risk (continued)

December 31, 2013

Financial liabilities

	Carrying amount	Gross nominal inflow / (outflow)	Repayable on demand	Up to 3 mths	3-6 mths	6-12 mths	1-5 years	>5 years
Due to depositors	\$ 1,223,333	\$ (1,239,039)	\$ (477,346)	\$ (200,338)	\$ (97,084)	\$ (206,740)	\$ (257,531)	\$ -
Accounts payable and accrued liabilities	4,502	(4,502)	(4,502)	-	-	-	-	-
Due to clients	225	(225)	(225)	-	-	-	-	-
Deferred income	106	(106)	(106)	-	-	-	-	-
	\$ 1,228,166	\$ (1,243,872)	\$ (482,179)	\$ (200,338)	\$ (97,084)	\$ (206,740)	\$ (257,531)	\$ -
Unrecognized loan commitments	-	(13,344)	-	(7,397)	(5)	(136)	(720)	(5,086)
Financial guarantees and letters of credit	-	(1,635)	-	(80)	(405)	(500)	(650)	-
Total financial liabilities	\$ 1,228,166	\$ (1,258,851)	\$ (482,179)	\$ (207,815)	\$ (97,494)	\$ (207,376)	\$ (258,901)	\$ (5,086)

4. **Risk management** (continued)

Market risk

Market risk is the potential adverse change in Bank income or in the value of the Bank's holdings of financial instruments arising from movements in interest rates, foreign exchange rates or equity prices. The objective of market risk management is to manage and control market risk exposure within acceptable parameters, while optimizing the return on risk.

The Bank's exposure to market risk is governed by a policy approved by the ALCO and ratified by the Finance Committee. The policy sets out the nature of risks which may be taken, and the applicable maximum risk limits. Compliance with risk limits and the Bank's exposure to market risks are reviewed at monthly meetings of the ALCO and quarterly meetings of the Finance Committee. Since the Bank does not engage in proprietary trading activities, its market risk exposure principally arises from its banking activities.

Day to day monitoring and management of market risk is undertaken by the Treasury Department. Exposure to market risk is managed by using hedging instruments or by utilizing natural hedges existing within the variety of financial instruments the Bank holds.

Interest rate risk

The principal market risk factor faced by the Bank is interest rate risk. The net interest income and market value of the Bank's assets is exposed to movements in interest rates. Primarily, risk arises when asset and liability principal and interest cash flows have different payment, repricing or maturity dates. Interest rate risk exposure is managed on a continuous basis using a combination of derivative instruments such as interest rate swaps and cash instruments such as loans and deposits.

Periodically, the Bank enters into interest rate swap contracts to manage the risks associated with certain of its deposit products. The Bank hedges selected interest rate exposures through interest rate swap contracts, which are linked to and adjust the interest rate sensitivity of specific deposit liabilities. These hedges may be in the form of modifying exposure to interest rate risk by converting fixed rate deposit liabilities to a floating rate. Any decrease in the value of the contracts is mitigated by a decrease in the fair value of the deposit obligations being hedged under an effective hedge.

The Treasury Department uses a variety of reporting and measurement tools to monitor interest rate risk within the Bank, including Asset-Liability Management ("ALM") analysis of the impact on net interest income and expense for given movements in interest rates and gap analysis in relation to various repricing and maturity scenarios covering the Bank's deposit products.

The ALCO and the Finance Committee review market risk limits, on a regular basis, to ensure there are no breaches.

December 31, 2014

*(Expressed in thousands of Bermuda dollars, except as noted)***4. Risk management (continued)****Interest Rate Sensitivity**

Interest rate risks are monitored by way of sensitivity analysis. These show the estimated effects of changes in market interest rates that management believes would be reasonably possible over the next twelve months, on net interest income and shareholders' equity as at December 31, 2014. The interest rate sensitivity analysis is based on the assumption that volumes remain stable over the analysis period and that management responds to changes in market interest rates and other risk factors. The interest rate sensitivity analysis does not reflect the movement in the fair value of investment securities from changes in market interest rates, which would be recorded as OCI within equity. In light of the current low interest rate environment, the Bank does not believe it is reasonably possible for there to be a substantial decrease in interest rates.

December 31, 2014

	Increase in net interest <u>income and equity</u>
100 basis point increase	\$ 3,746
200 basis point increase	\$ 7,508

December 31, 2013

	Increase in net interest <u>income and equity</u>
100 basis point increase	\$ 4,274
200 basis point increase	\$ 8,560

The tables on the following page summarizes the repricing periods for assets, liabilities and off-balance-sheet instruments. Items are allocated to time band categories by reference to the earlier of the next contractual interest rate repricing date and the maturity date. Use of this table to derive information about the Bank's interest rate risk position is limited by the fact that customers and other counterparties may choose to terminate their financial instruments at a date earlier than contractual maturity or repricing date. Examples of this include loans, which are shown at the earlier of the next contractual interest rate repricing date and the maturity date, but which may pre-pay earlier, and certain term deposits, which are shown at contractual maturity but which may be withdrawn before their contractual maturity and asset-backed securities which have call or pre-payment features.

December 31, 2014

(Expressed in thousands of Bermuda dollars, except as noted)

4. **Risk management (continued)****December 31, 2014 Interest rate repricing table**

	Carrying amount	Within 3 mths	After 3 mths but within 6 mths	After 6 mths but within 1 year	After 1 year but within 5 years	After 5 years	Non Interest bearing funds
Cash and cash equivalents	\$107,135	\$ 87,844	\$ -	\$ -	\$ -	\$ -	19,291
Investment securities	136,179	-	10,000	-	122,566	2,100	1,513
Accounts receivable and prepaid expenses	5,397	-	-	-	-	-	5,397
Accrued interest on cash, deposits with banks and securities	470	-	-	-	-	-	470
Loans and advances	876,457	846,360	4,840	15,423	-	-	9,834
Due from related parties	7,885	296	-	-	-	-	7,589
Assets held for sale	1,500	-	-	-	-	-	1,500
Investment property	3,880	-	-	-	-	-	3,880
Property and equipment	19,181	-	-	-	-	-	19,181
Intangible assets	24,192	-	-	-	-	-	24,192
Total assets	1,182,276	934,500	14,840	15,423	122,566	2,100	92,847
Due to depositors	1,081,406	652,410	48,845	172,970	207,181	-	-
Accounts payable and accrued liabilities	3,461	-	-	-	-	-	3,461
Due to clients	29	-	-	-	-	-	29
Deferred income	109	-	-	-	-	-	109
Equity	97,271	-	-	-	-	-	97,271
Total liabilities and equity	1,182,276	652,410	48,845	172,970	207,181	-	100,870
 Interest rate sensitivity gap	 \$ -	 \$ 282,090	 \$ (34,005)	 \$ (157,547)	 \$ (84,615)	 \$ 2,100	 \$ (8,023)
 Cumulative interest rate sensitivity gap	 \$ -	 \$ 282,090	 \$ 248,085	 \$ 90,538	 \$ 5,923	 \$ 8,023	 \$ -

4. Risk management (continued)

December 31, 2013 Interest rate repricing table

	Carrying amount	Within 3 mths	After 3 mths but within 6 mths	After 6 mths but within 1 year	After 1 year but within 5 years	After 5 years	Non Interest bearing funds
Cash and cash equivalents	\$168,032	\$161,074	\$-	\$-	\$-	\$-	6,958
Investment securities	145,264	13,000	38,000	39,000	43,500	9,100	2,664
Accounts receivable and prepaid expenses	6,821	-	-	-	-	-	6,821
Accrued interest on cash, deposits with banks and securities	698	-	-	-	-	-	698
Loans and advances	942,624	916,188	6,377	17,861	24	-	2,174
Due from related parties	8,457	347	-	-	-	-	8,110
Assets held for sale	1,500	-	-	-	-	-	1,500
Investment property	4,543	-	-	-	-	-	4,543
Property and equipment	27,021	-	-	-	-	-	27,021
Intangible assets	27,034	-	-	-	-	-	27,034
Total assets	1,331,994	1,090,609	44,377	56,861	43,524	9,100	87,523
Due to depositors	1,223,333	676,625	94,247	203,056	249,405	-	-
Accounts payable and accrued liabilities	4,502	-	-	-	-	-	4,502
Due to clients	225	-	-	-	-	-	225
Deferred income	106	-	-	-	-	-	106
Equity	103,828	-	-	-	-	-	103,828
Total liabilities and equity	1,331,994	676,625	94,247	203,056	249,405	-	108,661
 Interest rate sensitivity gap	 \$ -	 \$ 413,984	 \$ (49,870)	 \$ (146,195)	 \$ (205,881)	 \$ 9,100	 \$ (21,138)
 Cumulative interest rate sensitivity gap	 \$ -	 \$ 413,984	 \$ 364,114	 \$ 217,919	 \$ 12,038	 \$ 21,138	 \$ -

4. **Risk management** (continued)

Fair values

Fair value amounts represent estimates of the consideration that would currently be agreed upon between knowledgeable, willing parties who are under no compulsion to act and are best evidenced by a quoted market price, if one exists. Some of the Bank's financial instruments lack an available trading market. Therefore, the fair values of these instruments have been estimated using present value or other valuation techniques and may not necessarily be indicative of the amounts realisable in an immediate settlement of the instruments. In addition, the calculation of estimated fair value is based on market conditions at a specific point in time and may not be reflective of future fair values.

The following methods and assumptions were used in the determination of the fair value of financial instruments.

Cash and cash equivalents

The fair values of cash and deposits with banks approximate their carrying value as they are short-term in nature.

Investment securities

The fair values of equities and US Treasuries are based upon quoted market prices and the fair values of fixed income securities are based on bid prices, observable market inputs and matrix pricing for less liquid securities. Further information on the fair value of securities is given in Note 6.

Loans and advances

Fair values have been estimated by performing a discounted cash flow calculation using market rates for similar loans made at the reporting date. Other pertinent information relating to the principal characteristics of loans, mortgages and credit card receivables can be found in Note 8.

Due to depositors

The fair value of fixed rate deposits has been estimated by discounting the contractual cash flows, using market interest rates offered at the reporting date for deposits with similar terms. The fair values of deposits with no stated maturity date are considered equal to their carrying value as the customer can choose to call these deposits at any time.

Derivative instruments

The fair values of over-the-counter swap, equity index and foreign exchange forward contracts are calculated as the net present value of contractual cash flows using prevailing market rates or the quoted market price, if one exists.

Other

The fair values of other financial assets and liabilities approximate their carrying amounts as they are generally due on demand or otherwise earn interest at market interest rates.

4. Risk management (continued)

The aggregate of the estimated fair value amounts presented does not represent management's estimate of the underlying value of the Bank, in part because the fair values disclosed exclude property and equipment and certain other assets and liabilities, as these are not financial instruments.

December 31, 2014

	Fair value through profit or loss	Fair value through comprehensive income	Amortised cost	Total carrying amount	Fair value
Cash and cash equivalents	\$ -	\$ -	\$ 107,135	\$ 107,135	\$ 107,135
Investment securities	-	136,078	101	136,179	136,173
Loans and advances	-	-	876,457	876,457	877,090
Other assets	-	-	11,247	11,247	11,247
	<u>\$ -</u>	<u>\$ 136,078</u>	<u>\$ 994,940</u>	<u>\$ 1,131,018</u>	<u>\$ 1,131,645</u>
Deposits	\$ -	\$ -	\$ 1,081,406	\$ 1,081,406	\$ 1,085,580
Other liabilities	-	-	3,599	3,599	3,599
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,085,005</u>	<u>\$ 1,085,005</u>	<u>\$ 1,089,179</u>

December 31, 2013

	Fair value through profit or loss	Fair value through comprehensive income	Amortised cost	Total carrying amount	Fair value
Cash and cash equivalents	\$ -	\$ -	\$ 168,032	\$ 168,032	\$ 168,032
Investment securities	-	145,147	117	145,264	145,255
Loans and advances	-	-	942,624	942,624	943,831
Other assets	-	-	14,818	14,818	14,818
	<u>\$ -</u>	<u>\$ 145,147</u>	<u>\$ 1,125,591</u>	<u>\$ 1,270,738</u>	<u>\$ 1,271,936</u>
Deposits	\$ -	\$ -	\$ 1,223,333	\$ 1,223,333	\$ 1,227,481
Other liabilities	-	-	4,833	4,833	4,833
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,228,166</u>	<u>\$ 1,228,166</u>	<u>\$ 1,232,314</u>

4. Risk management (continued)

Fair value of assets and liabilities classified using the fair value hierarchy

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs, either directly (i.e., as prices) or indirectly (i.e., derived from prices). 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: Valuation techniques using significant unobservable inputs. 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. Level 3 measurements require significant amounts of judgement on the part of management and involve greater degrees of measurement uncertainty.

The following table presents financial instruments measured at fair value classified by the fair value hierarchy.

	December 31, 2014			
	Fair value measurements			Assets / liabilities
	Level 1	Level 2	Level 3	at fair value
Financial Assets				
Securities - available-for-sale				
US Government and agency:				
	\$			
- US government treasuries	60,228	\$ -	\$ -	\$ 60,228
- US government agencies	-	5,016	-	5,016
Other OECD government & government guaranteed debt and international organizations	-	32,632	-	32,632
Corporate debt securities	-	38,135	-	38,135
Equity securities - shares in mutual fund	-	67	-	67
Total available-for-sale securities	\$ 60,228	\$ 75,850	\$ -	\$ 136,078

4. Risk management (continued)

Fair value of assets and liabilities classified using the fair value hierarchy (continued)

	December 31, 2013			
	Fair value measurements			Assets / liabilities at fair value
	Level 1	Level 2	Level 3	
Financial Assets				
Securities - available-for-sale				
US Government and agency:				
- US government treasuries	\$ 65,287	\$ -	\$ -	\$ 65,287
- US government agencies	-	7,029	-	7,029
Other OECD government & government guaranteed debt and international organizations	-	27,747	-	27,747
Corporate debt securities	-	44,188	-	44,188
Equity securities - shares in mutual fund	-	845	51	896
Total available-for-sale-securities	\$ 65,287	\$ 79,809	\$ 51	\$ 145,147

There were no significant transfers between Levels 1, 2 and 3 during the year ended December 31, 2014 (2013-nil).

The effect of changing one or more inputs used in the measurement of fair value of these securities to another reasonably possible assumption would not be significant and no further analysis has been performed.

4. Risk management (continued)

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events (including legal risk but excluding strategic and reputational risk). The Bank seeks to manage operational risk so as to balance the avoidance of financial losses and damage to its reputation with overall cost effectiveness by implementing suitable control procedures.

The Basel Committee on Banking Supervision's report on "*Sound Practices for the Management and Supervision of Operational Risk*" and the Bermuda Monetary Authority ("BMA")'s May 2007 guidance paper "*The Management of Operational Risk*" heightened the awareness of operational risk and provided a set of minimum quantitative and qualitative standards and risk management practices that a financial institution should have in place to address these risks, thereby establishing an effective operational risk management framework. The Bank's framework is based on this guidance and has been approved by the Audit Committee of the Board and is subject to periodic review and update. In line with the Bank's Enterprise Risk Management ("ERM") framework the primary responsibility for operational risk management is assigned to senior management within each business unit. A centralized risk management function exists to oversee this process and provide regular reporting to the Bank's Governance Risk and Compliance Committee and Audit Committee.

Key components of the design of the Bank's Operational Risk Management framework are:

- Clearly defined Bank strategies;
- Oversight by the Board of Directors and senior management;
- Appropriate segregation of duties, including the independent authorization of transactions;
- Requirements for the reconciliation and monitoring of transactions;
- Compliance with regulatory and other legal requirements;
- Investments in appropriate processing technology and information technology ("IT") security;
- A strong operational risk and internal controls culture;
- Documentation of key policies and procedures;
- Training and professional development;
- Effective requirements for internal reporting;
- Periodic business level risk assessments conducted under the ERM framework; and
- Insurance and robust business contingency planning.

Compliance with Bank standards is supported by a program of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews and Operational Risk reports are discussed at various levels of management and by the Audit Committee.

Capital management

Capital is held to provide a cushion for unexpected losses. The Board sets the internal level of capital with the aim of ensuring minimum regulatory capital levels are always exceeded whilst allowing for growth in the business.

The BMA sets and monitors capital requirements for the Bank. The Bank's regulatory capital is allocated into two tiers:

- Tier 1 capital, which includes ordinary and preferred share capital, share premium (contributed surplus), retained earnings and reserves created by appropriations of retained earnings
- Tier 2 capital is comprised of collective allowance for credit losses, fixed asset revaluation reserves and unrealised gains on equity securities.

4. Risk management (continued)

Capital management (continued)

The BMA implemented the Basel II capital framework in Bermuda with effect from January 1, 2009, and set out the rules for adoption in the “*Revised Framework for Regulatory and Capital Assessment*” (‘Framework’). Basel II is structured around three ‘pillars’.

Pillar 1 – Describes the calculation for minimum regulatory capital for Credit, Operational and Market risk. The Bank has adopted the Standardised approach to both Credit and Operational risk with a *de minimis* exemption from the BMA from holding market risk capital due to the nature of its operations.

Regulatory ratios for Pillar 1 are calculated by dividing total capital by risk weighted assets (“RWA”). RWA are determined according to the varying levels of risk attached to assets and off-balance-sheet exposures.

At December 31, 2014, the minimum regulatory capital target established by the BMA for Pillar 1 for risk taking institutions is a total capital ratio of 8% of RWA (December 31, 2013 - 8%).

Pillar 2 – The Supervisory review process. Management of the Bank assesses risks not captured under Pillar 1, its governance and internal control environment and strategic and capital planning considerations in its Capital Assessment and Risk Profile document (“CARP”) which is submitted annually to the BMA. The BMA assesses the Bank’s CARP and determines its adequacy against standards required under the Basel II Accord Statement of Principles, resulting in a final capital requirement. This is expressed as a ratio of Pillar 2: Pillar 1 capital or at any point in time as an absolute dollar figure. The BMA expects the Bank to operate with a capital level above that minimum.

Pillar 3 – Market discipline. This is designed to promote market discipline by providing market participants with key information about the Bank’s risk exposures and risk management processes. Pillar 3 also aims to complement the minimum capital requirements described under Pillar 1, as well as the supervisory processes of Pillar 2.

In addition to the annual CARP process, the Bank’s Pillar 1 capital requirements are regularly monitored and are formally reported on a quarterly basis to the BMA.

The Bank has complied with all externally imposed minimum capital requirements throughout the current and prior years.

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December 31, 2014

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4. Risk management (continued)

Capital management (continued)

The Bank reports its regulatory capital position to the BMA as a consolidated legal entity each calendar quarter. The position, as reported to the BMA, at December 31 was as follows.

	Unaudited 2014	Unaudited 2013
Tier 1 capital		
Preferred share capital	\$ 20,000	\$ 20,000
Common share capital	5,000	5,000
Contributed surplus	7,200	6,617
General reserve	10,000	10,000
Current year's retained profit, reviewed by external auditors, after current year dividends	523	3,604
Retained earnings and other reserves	52,159	48,053
Goodwill	(7,456)	(7,456)
Total Tier 1 capital	\$ 87,426	\$ 85,818
Tier 2 capital		
Fixed assets revaluation reserves	\$ 1,049	\$ 6,078
Collective allowance for credit losses	4,716	4,185
Total Tier 2 capital	\$ 5,765	\$ 10,263
Total Tier 1 and 2 capital	\$ 93,191	\$ 96,081
Capital ratios		
Tier 1 capital	14.56%	13.26%
Total capital	15.52%	14.84%

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5. Cash and cash equivalents

	<u>2014</u>	<u>2013</u>
Cash in vault	\$ 5,950	\$ 5,782
Cash at local banks	10,652	6,919
Cash at foreign banks	<u>40,533</u>	<u>35,331</u>
	\$ 57,135	\$ 48,032
Other cash equivalents (all denominated in US dollars)	\$ <u>50,000</u>	\$ <u>120,000</u>
Total Cash and cash equivalents	\$ <u>107,135</u>	\$ <u>168,032</u>

Cash at foreign banks of \$40,533 (2013 - \$35,331) includes \$22,182 (2013 - \$21,121) held in US dollars and \$18,351 (2013 - \$14,210) held in other foreign currencies. The average effective interest rate earned on cash and deposits with banks for the year ended December 31, 2014 was 0.09% (2013 - 0.06%).

Cash and deposits with banks includes \$32 (2013 - \$215) of funds restricted in use as they are held in escrow on behalf of customers.

As at December 31, 2014, foreign currency interest bearing deposits with banks of \$41,979 includes \$19,382 denominated in foreign currencies other than US dollar (2013: \$37,276 included \$15,241). As at December 31, 2014 and December 31, 2013 all other cash and deposits with banks are denominated in Bermuda dollars or in US dollars.

Other cash equivalents in both years relate to US Treasuries with an original maturity date of less than 90 days.

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6. Investment securities

The fair value of the Bank's securities may be affected by changes in the level of prevailing interest rates. In the event that interest rates rise then the fair value of fixed income instruments would decrease. The tables below indicate the carrying value, fair value and remaining term to maturity of the Bank's fixed income securities at December 31, 2014 and December 31, 2013.

No investment securities have been pledged (2013: nil) as collateral to third parties.

	December 31, 2014					
	Maturing Within 1 year	Maturing in 1 to 5 years	Maturing after 5 years	With no specific maturity	Carrying Amount	Fair value
Available-for-sale						
Fixed Income						
US government and agency						
- Treasuries	\$ -	\$ 60,228	\$ -	\$ -	\$ 60,228	\$ 60,228
- Agency debt	-	5,016	-	-	5,016	5,016
Other OECD government & government guaranteed and international organizations	10,085	20,240	2,307	-	32,632	32,632
Corporate debt securities	-	38,135	-	-	38,135	38,135
Equity						
Equities	-	-	-	67	67	67
Total – available-for-sale	\$ 10,085	\$ 123,619	\$ 2,307	\$ 67	\$ 136,078	\$ 136,078
Debt securities classified as loans and receivables						
Asset-backed securities	\$ -	\$ -	\$ 101	\$ -	\$ 101	\$ 95
Total investment securities	\$ 10,085	\$ 123,619	\$ 2,408	\$ 67	\$ 136,179	\$ 136,173
Average effective interest rate	0.13%	0.95%	0.06%	-%	0.67%	

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6. Investment securities (continued)

	December 31, 2013					
	Maturing Within 1 year	Maturing in 1 to 5 years	Maturing after 5 years	With no specific maturity	Carrying Amount	Fair value
Available-for-sale						
Fixed Income						
US government and agency						
- Treasuries	\$ 65,287	\$ -	\$ -	\$ -	\$ 65,287	\$ 65,287
- Agency debt	2,004	5,025	-	-	7,029	7,029
Other OECD government & government guaranteed and international organizations	8,197	10,286	9,264	-	27,747	27,747
Corporate debt securities	15,061	29,127	-	-	44,188	44,188
	90,549	44,438	9,264	-	144,251	144,251
Equity						
Equities	-	-	-	896	896	896
Total – available-for-sale	\$ 90,549	\$ 44,438	\$ 9,264	\$ 896	\$ 145,147	\$ 145,147
Debt securities classified as loans and receivables						
Asset-backed securities	\$ -	\$ -	\$ 117	\$ -	\$ 117	\$ 108
Total investment securities	\$ 90,549	\$ 44,438	\$ 9,381	\$ 896	\$ 145,264	\$ 145,255
Average effective interest rate	0.47%	0.39%	1.28%	-%	0.49%	

6. Investment securities (continued)

Actual maturities may differ from the stated maturities reflected above because certain securities may have call or prepayment features. Asset-backed securities are shown at their legal final maturity and not their estimated weighted average life.

Total investment securities, at carrying value, included \$136,011 (2013 - \$143,249) of fixed rate securities and \$101 (2013 - \$1,119) of floating rate securities. The remaining carrying value of \$67 (2013 - \$896) represented equities. The approximate yield on the fixed rate securities at December 31, 2014 was 1.15% (2013 0.80%), while the approximate yield on the floating rate securities was 1.07% (2013 - 0.57%).

The Bank held asset-backed securities all of which are rated BBB or above by Standard & Poor's with an amortized cost totalling \$101 and fair value totalling \$95 (2013 - \$117 and \$108 respectively). The Bank recorded net impairment losses of \$nil during the year (2013 - \$nil) on its asset-backed securities.

Depending on market conditions, the Bank could incur additional realized and unrealized investment losses in future periods. However, given that the asset backed securities are investment-grade and management has the ability and intent to hold these investments until there is a recovery of the unrealized loss, which may be at maturity, management believes it is probable that the Bank will be able to collect the principal amount of these securities according to the original contractual terms of the investments. As such, management does not consider any of these investments to be impaired as at December 31, 2014.

Fair values for fixed income securities are obtained from independent pricing services. The independent pricing services obtain actual transaction prices for securities that have quoted prices in active markets and have their own proprietary methods for determining the fair value of securities that are not actively traded. In general, the independent pricing services use "matrix pricing" which utilises observable market inputs including, but not limited to, broker quotes, interest rates, yield curves, prepayment speeds, default rates and such other inputs as are available from market sources to determine a reasonable fair value.

Net gains (losses) on investment securities were:

	<u>2014</u>	<u>2013</u>
Net realized gains (losses) on sale of:		
Available for sale securities	\$ 591	\$ (50)
Debt securities classified as loans and receivables	<u>-</u>	<u>(4)</u>
Total	<u>\$ 591</u>	<u>\$ (54)</u>

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7. Accounts receivable and prepaid expenses

The Bank's accounts receivable and prepaid expenses, are as follows:

	<u>2014</u>	<u>2013</u>
Prepaid staff loan benefit	\$ 1,276	\$ 2,877
Management fees, trail commissions and custody fees receivable	1,992	1,509
Other prepaid expenses	1,901	1,826
Accounts receivable	<u>228</u>	<u>609</u>
Total	<u>\$ 5,397</u>	<u>\$ 6,821</u>

8. Loans and advances

The Bank's loans and advances, net of unamortized deferred administration fees and the allowance for credit losses, are as follows:

	<u>2014</u>	<u>2013</u>
Residential mortgages	\$ 734,464	\$ 780,493
Commercial mortgages	91,805	91,629
Loans and advances - secured	64,457	76,501
Loans and advances – unsecured	1,717	2,431
Credit card receivables	<u>6,719</u>	<u>7,389</u>
	899,162	958,443
Allowance for credit losses on loans, mortgages and credit card receivables	<u>(22,705)</u>	<u>(15,819)</u>
	<u>\$ 876,457</u>	<u>\$ 942,624</u>

The following table provides an analysis of remaining contractual maturities of loans and advances to customers:

	<u>2014</u>		<u>2013</u>	
	<u>Amortized cost</u>	<u>Fair value</u>	<u>Amortized cost</u>	<u>Fair value</u>
Maturity analysis				
One year or less	\$ 77,825	\$ 78,771	\$ 99,022	\$ 99,103
More than one year	<u>798,632</u>	<u>800,064</u>	<u>843,602</u>	<u>844,728</u>
	<u>\$ 876,457</u>	<u>\$ 878,835</u>	<u>\$ 942,624</u>	<u>\$ 943,831</u>

The loan fair values disclosed above are based on weighted average estimated remaining maturities and are determined using a valuation technique supported by observable market rates. Additional information about the interest rate risk exposure pertaining to loans and advances to customers are presented in Note 4.

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8. Loans and advances (continued)

The Bank had the following loans and advances that are considered to be impaired.

	<u>2014</u>	<u>2013</u>
Residential and commercial mortgages		
Gross loans	\$ 54,222	\$ 46,655
Specific allowance	<u>(14,858)</u>	<u>(9,312)</u>
Net mortgages	<u>39,364</u>	<u>37,343</u>
Loans and chattel mortgages		
Gross loans	8,155	3,354
Specific allowance	<u>(3,132)</u>	<u>(2,322)</u>
Net loans and chattel mortgages	<u>5,023</u>	<u>1,032</u>
	<u>\$ 44,387</u>	<u>\$ 38,375</u>

The majority of mortgages are secured by Bermuda residential property. Mortgages receivable are repayable in monthly or periodic instalments generally over periods not exceeding 30 years (2013 - 30 years). At December 31, 2014 the weighted average time remaining to maturity for mortgages was 18 years (2013 - 19 years). At December 31, 2014 loans and chattel mortgages are repayable in monthly or periodic instalments generally over periods not exceeding 6 years (2013 - 7 years), and may be amortized or may be payable in total at maturity with interest being paid monthly. The Bank holds deeds on properties, guarantees and other assets in connection with certain loans and mortgages. Other loans receivable are in the form of unsecured promissory notes. Credit card receivables bear interest at 12% to 18% (2013 - 12% to 18%) and are unsecured.

The average effective interest rate on total loans and mortgages receivable at December 31, 2014 is 5.83% (2013 - 5.90%).

Total loans include \$61,233 (2013 - \$68,351) denominated in US dollars.

December 31, 2014

*(Expressed in thousands of Bermuda dollars, except as noted)***8. Loans and advances (continued)**

At December 31, 2014, loans, mortgages and credit card receivables included \$213 (2013 - \$215) receivable from directors, and \$79,808 (2013 - \$100,696) receivable from employees of the Bank or employees of the related party companies. Mortgages and loans receivable from directors and employees are part of the Bank's staff loan program, which offers interest rates ranging from 4.50% to 11.25% (2013 - 2.25% to 11.25%), which are below those offered to unrelated parties but above the cost of funds. All other terms of staff loans are the same as those granted to unrelated parties.

Allowance for credit losses

The allowance for credit losses is deducted from loans, mortgages and credit card receivables in the consolidated statement of financial position. Changes in the allowance for credit losses are comprised of the following:

	<u>2014</u>	<u>2013</u>
Specific allowances for impairment:		
Balance at 1 January	\$ 11,634	\$ 12,696
Impairment loss for the year:		
Charge for the year, net	9,290	7,234
Write-offs, net	<u>(2,934)</u>	<u>(8,296)</u>
Balance at 31 December	<u>17,990</u>	<u>11,634</u>
Collective allowances for impairment:		
Balance at 1 January	4,185	3,759
Impairment loss for the year:		
Charge for the year, net	<u>531</u>	<u>426</u>
Balance at 31 December	<u>4,716</u>	<u>4,185</u>
	<u>\$ 22,706</u>	<u>\$ 15,819</u>

Write-offs during the years ended December 31, 2014 and 2013 relate primarily to charge-offs of principal and suspended accrued interest on impaired loans. Such amounts are initially provided for in the consolidated Statement of Comprehensive Income in "net impairment loss on financial assets" and subsequently written off as incurred.

9. Investment property

Cost

At January 1, 2013	\$ 8,162
Reclassification to assets held for sale	(1,500)
Reclassification to property and equipment	(1,211)
Improvements capitalised	<u>57</u>

At December 31, 2013	\$ 5,508
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At December 31, 2014	\$ 5,508
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Amortization and impairment losses

At January 1, 2013	\$ 446
Reclassification to property and equipment	(216)
Amortization for the year	222
Impairment charge for the year	<u>513</u>

At December 31, 2013	\$ 965
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Amortization for the year	\$ 192
Impairment charge for the year	<u>471</u>

At December 31, 2014	\$ 1,628
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Carrying value

At December 31, 2013	\$ 4,543
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At December 31, 2014	\$ 3,880
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The fair value of investment property as at December 31, 2014 is \$3,880 (2013 - \$4,915). Investment property consists of one property with a carrying value of \$3,880 (2013 - \$4,543). One floor of this property, which has been independently assessed as 18% of the leasable area of the building, was reclassified to property and equipment, due to the Bank using it as corporate offices, from 2013. Prior to reclassification, an impairment charge of \$513 was recognized on this property as the recoverable amount was assessed as less than the carrying amount.

Management has tested the carrying value of investment property at December 31, 2014 for impairment and, except as noted above, found the recoverable amount to be greater than the carrying value. In determining the recoverable amounts, independent appraisals and value-in-use models were used. In accordance with an independent appraisal a discount factor of 7% (2013 - 7%) was applied to the value-in-use cash flow projections to determine their net present value.

Notes to Consolidated Financial Statements

December 31, 2014

(Expressed in thousands of Bermuda dollars, except as noted)



10. Property and equipment

Property and equipment held by the Bank are as follows:

	<u>Buildings</u>	<u>Furniture and fixtures</u>	<u>Computer hardware and equipment</u>	<u>Artwork</u>	<u>Leasehold improvements</u>	<u>Total</u>
Cost						
Balance at January 1, 2013	19,311	5,101	13,747	606	11,532	50,297
Additions	-	447	345	-	482	1,274
Reclassification from investment property	995	-	-	-	-	995
Write-offs	-	-	-	-	(456)	(456)
Balance at December 31, 2013	20,306	5,548	14,092	606	11,558	52,110
Balance at January 1, 2014	20,306	5,548	14,092	606	11,558	52,110
Additions	3	417	224	-	62	706
Disposals	(6,712)	-	-	-	-	(6,712)
Write-offs	-	-	(46)	-	-	(46)
Balance at December 31, 2014	13,597	5,965	14,270	606	11,620	46,058
Accumulated depreciation						
Balance at January 1, 2013	4,225	4,521	10,436	-	3,765	22,947
Write-offs	-	-	-	-	(456)	(456)
Depreciation charge for the year	483	129	1,263	-	723	2,598
Balance at December 31, 2013	4,708	4,650	11,699	-	4,032	25,089
Balance at January 1, 2014	4,708	4,650	11,699	-	4,032	25,089
Disposals	(590)	-	-	-	-	(590)
Write-offs	-	-	(28)	-	-	(28)
Depreciation charge for the year	501	220	978	-	604	2,303
Impairment charge for the year	103	-	-	-	-	103
Balance at December 31, 2014	4,722	4,870	12,649	-	4,636	26,877
Carrying amounts						
Balance at December 31, 2013	\$ 15,598	\$ 898	\$ 2,393	\$ 606	\$ 7,526	\$ 27,021
Balance at December 31, 2014	\$ 8,875	\$ 1,095	\$ 1,621	\$ 606	\$ 6,984	\$ 19,181

On November 30, 2014, the Bank distributed its wholly owned subsidiary, Kenwood Club Limited, at its carrying value of \$6,122 to the Bank's parent company, Clarien, due to it being a common control transaction. The only asset held by Kenwood Club Limited was a building, which the Bank no longer intended to use in its ongoing operations. This building is therefore reflected within disposals in the table above.

11. Intangible assets

Intangible assets are as follows:

	Computer software	Goodwill / customer relationships	Total
Cost			
Balance at January 1, 2013	\$ 24,011	\$ 7,456	\$ 31,467
Additions	<u>987</u>	<u>-</u>	<u>987</u>
Balance at December 31, 2013	<u>\$ 24,998</u>	<u>\$ 7,456</u>	<u>\$ 32,454</u>
Balance at January 1, 2014	\$ 24,998	\$ 7,456	\$ 32,454
Additions	<u>143</u>	<u>-</u>	<u>143</u>
Write-offs	<u>(492)</u>	<u>-</u>	<u>(492)</u>
Balance at December 31, 2014	<u>\$ 24,649</u>	<u>\$ 7,456</u>	<u>\$ 32,105</u>
Accumulated amortization			
Balance at January 1, 2013	\$ 2,904	\$ -	\$ 2,904
Amortization charge for the year	<u>2,516</u>	<u>-</u>	<u>2,516</u>
Balance at December 31, 2013	<u>\$ 5,420</u>	<u>\$ -</u>	<u>\$ 5,420</u>
Balance at January 1, 2014	\$ 5,420	\$ -	\$ 5,420
Write-offs	<u>(335)</u>	<u>-</u>	<u>(335)</u>
Amortization charge for the year	<u>2,828</u>	<u>-</u>	<u>2,828</u>
Balance at December 31, 2014	<u>\$ 7,913</u>	<u>\$ -</u>	<u>\$ 7,913</u>
Carrying amounts			
Balance at December 31, 2013	\$ 19,578	\$ 7,456	\$ 27,034
Balance at December 31, 2014	<u>\$ 16,736</u>	<u>\$ 7,456</u>	<u>\$ 24,192</u>

There are customer relationships of \$5,970 (2013 - \$5,970) relating to CIL, which do not have a finite contractual term and as such are unamortised.

Capitalised software is amortised when the assets become available for use and is accounted for on a straight line basis over the expected useful life of the asset.

Assets no longer in use included in computer software, with a cost of \$492 and a net book value of \$157, were written off in December 2014.

11. **Intangible assets** (continued)

The Bank performs analyses of unamortised intangible assets on an annual basis or more frequently if indicators of impairment exist. If actual results are not consistent with management's assumptions and estimates, the Bank may be exposed to an additional impairment charge associated with unamortised intangible assets.

Impairment is measured as the excess of the carrying amount over the estimated recoverable amount, being the higher of fair value or value in use.

The test methods employed in performing the analyses involve assumptions concerning interest and discount rates, growth projections and other assumptions of future business conditions. The assumptions employed are based on management's judgment using internal and external data. Management utilizes independent valuation experts, if needed.

Management completed its annual impairment testing for intangible assets using the methodology described herein. The impairment test for the Bank's CGU's goodwill/customer relationships is based on management's business forecast in a detailed planning period of three years. For impairment testing, a growth rate of nil% was assumed for the period after the end of the detailed planning period. A discount rate of 10%, being the Bank's estimated cost of capital, was used to determine the net present value of the estimated cash flows.

Accordingly, it was ascertained that no impairment was needed for the intangible assets carried in the financial statements.

The key assumptions described above may change as economic and market conditions change.

12. **Assets held for sale**

On December 31, 2013 the Bank reclassified an investment property to assets held for sale, due to the expected sale of the property to a related party associated through significant influence. The property was conditionally sold on January 28, 2014 for \$1,500. In March 2015, the property was transferred to the Bank's parent company, Clarien, for consideration of \$1,500 in anticipation of final settlement with the acquirer. Clarien has assumed all settlement risks associated with the ultimate acquirer.

13. Due to depositors

Total deposits include \$342,603 (2013 - \$354,119) denominated in US dollars and \$20,514 (2013 - \$15,147) denominated in other foreign currencies. All deposits are originated in Bermuda.

The following is a summary of interest bearing deposits classified by period remaining to maturity as at December 31:

	<u>2014</u>		<u>2013</u>	
	<u>Average effective interest rate</u>	<u>Amount</u>	<u>Average effective interest rate</u>	<u>Amount</u>
Demand	0.04%	\$ 436,854	0.09%	\$ 477,463
Up to 3 months	0.71%	206,224	0.71%	183,437
3 - 6 months	0.85%	48,844	1.92%	94,247
6 - 12 months	1.40%	172,971	1.97%	203,056
1 - 5 years	2.26%	<u>207,181</u>	2.22%	<u>249,581</u>
Total		1,072,074		1,207,784
Accrued interest		<u>9,332</u>		<u>15,549</u>
Total		<u>\$ 1,081,406</u>		<u>\$ 1,223,333</u>

14. Related party transactions and balances

Related parties include the Parent entity, companies associated through significant influence and directors and their affiliates.

All related party transactions are in the normal course of operations and are measured at the exchange amount, which is on an arm's length basis as agreed to by the related parties.

Amounts listed in the consolidated statement of financial position as due from related parties have no stated maturity date or repayment terms, are unsecured and carry interest at 5% (2013 - 5%).

The work force of the Bank included 16 key management employees in 2014 (2013 - 12). During the year ended December 31, 2014, salaries and benefits totalling \$5,001 (2013 - \$3,916) were paid to key management employees of the Bank of which \$nil (2013 - \$127) was deferred under long-term incentive scheme arrangements. In addition there are 9 (2013 - 5) directors who are considered key management personnel.

14. Related party transactions and balances (continued)

Consolidated Statement of Comprehensive Income

	<u>2014</u>	<u>2013</u>
Interest income	\$ 1,635	\$ 2,010
Interest expense	\$ 669	\$ 950
Fee and commission income	\$ 3,684	\$ 3,659
Fee and commission expense	\$ 105	\$ 143
Personnel expenses	\$ 5,413	\$ 5,002
Other expenses	\$ 1,790	\$ 1,048
Rent	\$ 86	\$ 77

Included in other expenses are \$105 (2013 - \$143) paid to Gibbons Management Services Limited ("GMSL") for group-allocated administrative overheads, and \$803 (2013 - \$270) paid to key management employees. GMSL is ultimately owned by one of the Bank's shareholders. Personnel expenses includes \$4,198 (2013 - \$3,646) paid to key management personnel. The remainder of other expenses relates to transactions with companies associated through significant influence. In the summary above, all fee and commission income, fee and commission expense, personnel expenses and rent relate to transactions with companies associated through significant influence.

During the year ended December 31, 2014, the Bank recharged \$115 (2013 - \$489) to companies associated through significant influence, representing portions of certain expenses provided by the Bank. Of this amount, \$69 (2013 - \$452) has been included in personnel expenses and \$46 (2013 - \$37) has been included in other expenses in the consolidated statement of comprehensive income.

Consolidated Statement of Financial Position

	<u>2014</u>	<u>2013</u>
Included in assets		
Loans and advances (Key management personnel)	\$ 8,955	\$ 12,877
Loans and advances (Entities with significant influence)	\$ 17,535	\$ 17,700
Loans and advances (Companies associated through significant influence)	\$ 16	13
Accounts receivable and prepaid expenses (Companies associated through significant influence)	\$ 294	\$ 787
Due from related parties (Parent)	\$ 5,072	\$ 4,487
Due from related parties (Companies associated through significant influence)	\$ 2,813	\$ 3,970
Included in liabilities		
Due to depositors (Key management personnel)	\$ 38,101	\$ 38,400
Due to depositors (Companies associated through significant influence)	\$ 26,958	\$ 44,544
Accounts payable and accrued liabilities (Key management personnel)	\$ -	\$ 46
Accounts payable and accrued liabilities (Companies associated through significant influence)	\$ 192	\$ 83

The deposits are taken as part of the Bank's ordinary course of business and on the same terms as deposits held for unrelated parties.

15. Accounts payable and accrued liabilities

The Bank's accounts payable and accrued liabilities are as follows:

	<u>2014</u>	<u>2013</u>
Accounts payable	\$ 633	\$ 445
Accrued liabilities	1,914	1,966
Bonus payable	600	1,742
Foreign currency tax payable	233	222
Visa rewards payable	<u>81</u>	<u>127</u>
Total	<u>\$ 3,461</u>	<u>\$ 4,502</u>

16. General reserve, retained earnings and contributed surplus

The total authorized, issued and fully paid Bermuda dollar common share capital is 4,999,999 (2013 - 4,999,999) with a par value of \$1 per share. Common shares carry no right to regular dividends. The Bank also has 20,000,000 (2013 - 20,000,000) authorized, issued and fully paid US dollar redeemable, floating rate preferred shares with non-cumulative dividends with a par value of \$1 per share.

During the year ended December 31, 2014, dividends of \$nil (2013 - \$nil) were declared and paid to the Bank's shareholders of common shares. The Bank paid dividends of \$657 on its preferred shares (2013 - \$659) during the year.

A general reserve of \$1,000 was established by the directors at January 31, 1995. Over time, this reserve has been increased to \$10,000 through transfers from retained earnings. Transfers back to retained earnings from the general reserve can be made at the discretion of the Board of Directors.

The movement in contributed surplus in 2014 represents the distribution of the Kenwood Club Limited (Note 10) to the Bank's parent Clarien at its carrying value of \$6,122. The movement in contributed surplus in 2013 represents a \$1,250 cash contribution from the Bank's sole shareholder.

Notes to Consolidated Financial Statements

December 31, 2014

(Expressed in thousands of Bermuda dollars, except as noted)



17. Net interest income

Interest income is comprised of:	<u>2014</u>	<u>2013</u>
Loans and advances	\$ 58,542	\$ 61,697
Available for sale investments	1,304	1,119
Held to maturity investments	1	3
Other interest income	<u>68</u>	<u>49</u>
Total interest income	<u>\$ 59,915</u>	<u>\$ 62,868</u>

Interest expense is comprised of:

Customer accounts	<u>\$ 11,172</u>	<u>\$ 14,190</u>
Total interest expense	<u>\$ 11,172</u>	<u>\$ 14,190</u>

18. Net fee and commission income

Fee income is comprised of:	<u>2014</u>	<u>2013</u>
Investment management fees	\$ 6,812	\$ 6,439
Banking and credit related fees and commissions	5,379	4,488
Other investment fees	2,507	2,696
Brokerage fees	<u>56</u>	<u>44</u>
Total fee income	<u>\$ 14,754</u>	<u>\$ 13,667</u>

Fee expense is comprised of:

Credit and debit card expenses	\$ 1,493	\$ 1,520
Investment expenses and sub advisor fees	814	840
Other fee and commission expenses	<u>762</u>	<u>790</u>
Total	<u>\$ 3,069</u>	<u>\$ 3,150</u>

Notes to Consolidated Financial Statements

December 31, 2014

(Expressed in thousands of Bermuda dollars, except as noted)



19. Other expenses

	<u>2014</u>		<u>2013</u>
Information technology expenses	\$ 4,137	\$	4,412
Office expenses	2,153		2,658
Professional fees	4,736		2,130
Rent expenses	955		1,137
Advertising	1,306		1,114
Recruitment, training and travel	1,470		1,006
License and insurance costs	893		925
Bank charges	168		143
Directors' fees and expenses	746		333
Miscellaneous expenses	<u>848</u>		<u>1,844</u>
Total other expenses	<u>\$ 17,412</u>	\$	<u>15,702</u>

20. Pension expense

The Bank's employees participate in a defined contribution pension plan sponsored by a company associated through significant influence. During the year ended December 31, 2014 contributions amounting to \$911 (2013 - \$816) equating to the service cost for the year, were made to the plan by the Bank on behalf of its employees and are included in personnel expenses in the consolidated statement of comprehensive income.

Included in these contributions made during the year ended December 31, 2014, were contributions amounting to \$246 (2013 - \$143), which were made to the plan by the Bank on behalf of its key management personnel.

21. Commitments, guarantees and contingent liabilities
Credit commitments

In the normal course of business the Bank enters into commitments to meet the credit requirements of its customers. These credit arrangements, representing undertakings to make credit available in the form of new loans and mortgages and drawdown facilities, are subject to the Bank's normal credit standards, controls and collateral requirements. The values set out in the table below represent the maximum amount of additional credit that the Bank could be obligated to extend, should such contracts be fully utilized.

	<u>2014</u>	<u>2013</u>
Commitments to extend credit:		
Original term to maturity of one year or less	\$ 3,104	\$ 7,537
Original term to maturity of more than one year	<u>4,540</u>	<u>5,807</u>
Total credit commitments	<u>\$ 7,644</u>	<u>\$ 13,344</u>

Guarantees

The Bank issues letters of credit and guarantees at the request of customers in order to secure the customer's payment or performance obligations to a third party. These guarantees represent an irrevocable obligation of the Bank to pay the third party beneficiary upon presentation of the guarantee and satisfaction of the documentary requirements stipulated therein. The Bank is contingently liable for customer letters of credit and guarantees amounting to \$1,751 (2013 - \$1,635). Of this amount, \$280 (2013 - \$280), is supported by security, which may include cash, securities, and other assets pledged.

The Bank has issued a guarantee to the Bermuda Stock Exchange on behalf of Clarien BSX Services Limited in the amount of \$650 (2013 - \$650).

The remaining terms of all guarantees and letters of credit range from 1 month to 12 months (2013 - 1 month to 12 months).

21. **Commitments, guarantees and contingent liabilities** (continued)

Lease commitments

The Bank has obligations under operating leases for three buildings that expire on December 31, 2018, January 31, 2023 and on February 3, 2033 respectively.

Leases typically run for a period of up to 20 years, with an option to renew the lease after that period. Lease payments are adjusted every five years to reflect market rentals. Future minimum lease payments under the non-cancellable operating leases are as follows:

<u>Fiscal Year</u>	<u>2014</u>	<u>2013</u>
2014	\$ -	\$ 954
2015	954	954
2016	954	954
2017	954	954
2018	954	954
2019	824	824
Thereafter	<u>2,768</u>	<u>2,768</u>
	<u>\$ 7,408</u>	<u>\$ 8,362</u>

Legal Proceedings

In the normal course of business, the Bank is routinely engaged in a number of pending and threatened legal proceedings. Management does not expect the ultimate resolution of any threatened or actual legal proceedings involving the Bank, to have a material adverse effect on the consolidated financial statements.

Other commitments

As at December 31, 2014, the Bank has contractually committed to incur costs for I.T. systems of \$2,473 (2013 - \$1,381) within one year and \$2,429 (2013 - \$2,008) after more than one year.

22. **Seasonality of the Bank's transactions**

Given the activities in which the Bank and its subsidiaries engage, their transactions are not cyclical or seasonal in nature. Accordingly, no specific disclosures are provided in these explanatory notes to the consolidated financial statements for the year ended December 31, 2014 (2013: No specific disclosures).

23. **Subsequent Events**

On February 9, 2015, Edmund Gibbons Limited ("EGL") acquired 50% of CWH Limited, which when combined with its existing 20% interest in Clarien, resulted in EGL becoming the controlling shareholder of Clarien and the ultimate parent company of CBL.



Clarien Bank Limited

Principal Offices and Subsidiaries

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Hamilton HM CX
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Clarien Investments Limited

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Hamilton HM 11

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Clarien Bank Limited through its wholly owned subsidiary companies is licensed to conduct bank, investments and trust business by the Bermuda Monetary Authority.