Clarien Bank Limited

Consolidated Financial Statements

(With Independent Auditors' Report Thereon)

Year Ended December 31, 2017

CLARIEN

Table of Contents

CLARIEN

Clarien Bank Limited

Consolidated Financial Statements
(With Independent Auditors' Report Thereon)

Year Ended December 31, 2017

KPMG Audit Limited
Crown House
4 Par-la-Ville Road
Hamilton HM 08 Bermuda

Mailing Address:
P.O. Box HM 906
Hamilton HM DX Bermuda

Telephone +1 441 295 5063
Fax +1 441 295 9132
Internet www.kpmg.bm

Independent Auditor's Report
To the Shareholder of Clarien Bank Limited

Report on the Audit of the Consolidated Financial Statements

Opinion
We have audited the consolidated financial statements of Clarien Bank Limited and its subsidiaries (together the "Group"), which comprise the consolidated statement of financial position as at December 31, 2017, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at December 31, 2017, and its consolidated financial performance, consolidated changes in equity, and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion
We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Bermuda, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, 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.

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

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

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements
Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

© 2018 KPMG Audit Limited, a Bermuda limited liability company and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.
All rights reserved.

KPMG

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

KPMG Audit Limited

Chartered Professional Accountants
Hamilton, Bermuda
June 15, 2018

(Expressed in thousands of Bermuda dollars)

	Note(s)		2017		2016
Assets					
Cash and cash equivalents	5	$	221,045	$	192,259
Investment securities	6		180,889		161,633
Accounts receivable and prepaid expenses	7		3,929		3,941
Accrued interest on cash, deposits with banks and securities			914		683
Loans and advances	8,13		745,051		756,375
Due from related parties	13		1,303		7,739
Investment property	9		3,477		3,611
Property and equipment	10		15,660		16,818
Intangible assets	11		20,674		21,393
Total assets		$	1,192,942	$	1,164,452
Liabilities					
Due to depositors	12,13	$	1,074,843	$	1,053,698
Accounts payable and accrued liabilities	14		3,854		3,621
Due to clients			160		266
Deferred income			108		84
Total liabilities			1,078,965		1,057,669
Equity					
Preferred shares	15		–		20,000
Common shares	15		5,000		5,000
Contributed surplus	15		46,406		22,150
General reserve	15		10,000		10,000
Retained earnings			54,762		51,703
Accumulated other comprehensive loss			(2,191)		(2,070)
Total equity			113,977		106,783
Total liabilities and equity		$	1,192,942	$	1,164,452

See accompanying notes to consolidated financial statements

Signed on behalf of the Board

____________________ Director

____________________ Director

(Expressed in thousands of Bermuda dollars)

	Note(s)	2017	2016
Interest income	16	$ 55,534	$ 53,815
Interest expense	16	(11,193)	(10,799)
Net interest income		44,341	43,016
Fee and commission income	17	15,367	13,735
Fee and commission expense	17	(3,789)	(3,398)
Net fee and commission income		11,578	10,337
Net (losses) / gains on investment securities	6	(59)	853
Foreign exchange income		462	568
Rent		357	348
Revenue		56,679	55,122
Net impairment loss on financial assets	8	6,046	8,563
Loss on disposition of non performing loans		–	667
Net operating income		50,633	45,892
Personnel expenses	13,19	27,332	26,044
Depreciation and amortisation	9,10,11	4,552	4,609
Other expenses	13,18	14,860	14,025
Total other expenses		46,744	44,678
Profit for the year		$ 3,889	$ 1,214
Other comprehensive loss			
Items that may be reclassified subsequently to profit or loss:			
Net change in unrealized losses on available-for-sale securities		$ (180)	$ (934)
Net change in unrealized gains on equity shares		–	1
Reclassification to earnings of net realized losses / (gains) in the year		59	(853)
Other comprehensive loss for the year		(121)	(1,786)
Total comprehensive income / (loss) for the year		$ 3,768	$ (572)

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, 2017
(Expressed in thousands of Bermuda dollars)

	Note	Preferred shares	Common shares	Contributed surplus	General reserve	Retained earnings	Accumulated other comprehensive loss	Total
Balance at January 1, 2017		$ 20,000	$ 5,000	$ 22,150	$ 10,000	$ 51,703	$ (2,070)	$ 106,783
Total comprehensive income for the year								
Profit for the year		–	–	–	–	3,889	–	3,889
Total other comprehensive loss		–	–	–	–	–	(121)	(121)
Total comprehensive loss for the year, net of tax		–	–	–	–	3,889	(121)	3,768
Capital contribution	15	–	–	24,256	–	–	–	24,256
Redemption of preference shares	15	(20,000)	–	–	–	–	–	(20,000)
Preferred share dividends declared	15	–	–	–	–	(830)	–	(830)
Balance at December 31, 2017		$ –	$ 5,000	$ 46,406	$ 10,000	$ 54,762	$ (2,191)	$ 113,977

See accompanying notes to consolidated financial statements

(Expressed in thousands of Bermuda dollars)

	Note	Preferred shares	Common shares	Contributed surplus	General reserve	Retained earnings	Accumulated other comprehensive loss	Total
Balance at January 1, 2016		$ 20,000	$ 5,000	$ 9,550	$ 10,000	$ 51,267	$ (284)	$ 95,533
Total comprehensive income for the year								
Profit for the year		–	–	–	–	1,214	–	1,214
Total other comprehensive loss		–	–	–	–	–	(1,786)	(1,786)
Total comprehensive loss for the year, net of tax		–	–	–	–	1,214	(1,786)	(572)
Capital contribution	15	–	–	12,600	–	–	–	12,600
Preferred share dividends declared	15	–	–	–	–	(778)	–	(778)
Balance at December 31, 2016		$ 20,000	$ 5,000	$ 22,150	$ 10,000	$ 51,703	$ (2,070)	$ 106,783

See accompanying notes to consolidated financial statements

(Expressed in thousands of Bermuda dollars)

	Note		2017		2016
Cash flows from operating activities					
Profit for the year		$	3,889	$	1,214
Adjustments to reconcile net profit for the year to net cash provided by operating activities:					
Depreciation and amortization			4,552		4,609
Amortization of premiums/discounts on fixed income securities			491		553
Net losses / (gains) on investment securities			59		(853)
Net impairment loss on financial assets			6,046		8,563
Loss on disposition of non performing loans			–		667
Net changes in non-cash balances relating to operations:					
Change in accounts receivable and prepaid expenses			12		555
Change in accrued interest on cash, deposits with banks and securities			(231)		(241)
Change in loans and advances			5,278		44,122
Change in due from related parties			6,436		624
Change in due to depositors			21,145		15,226
Change in accounts payable and accrued liabilities			233		1,234
Change in due to clients			(106)		160
Change in deferred income			24		(14)
Net cash provided by operating activities			47,828		76,419
Cash flows from investing activities					
Acquisition / reinvestment of available-for-sale securities			(113,823)		(171,033)
Proceeds / maturity of available-for-sale securities			93,896		182,676
Intangible assets acquired	11		(2,017)		(982)
Property and equipment purchased	10		(524)		(987)
Net cash (used in) / provided by investing activities			(22,468)		9,674
Cash flows from financing activities					
Preferred share dividends paid	15		(830)		(778)
Redemption of preference shares	15		(20,000)		–
Capital contribution	15		24,256		12,600
Net cash provided by financing activities			3,426		11,822
Net increase in cash and cash equivalents			28,786		97,915
Cash and cash equivalents, beginning of year			192,259		94,344
Cash and cash equivalents, end of year	5	$	221,045	$	192,259

See accompanying notes to consolidated financial statements

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

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"). The Bank changed its name from CAPITAL G Bank Limited to Clarien Bank Limited effective April 17, 2014. The Bank is wholly owned subsidiary of Clarien Group Limited ("Clarien").

On December 13, 2017, Clarien announced that it had entered into a formal agreement with NCB Financial Group Ltd ("NCB") whereby NCB became the majority shareholder of Clarien and therefore controlling shareholder of the Bank. Under the agreement, NCB subscribed for a 50.1% majority of the shares of Clarien. Funds managed by Portland Private Equity ("PPE") will hold 17.92% stake in Clarien and Edmund Gibbons Limited ("EGL") retains a 31.98% shareholding. Both NCB and PPE are part of the Michael Lee-Chin controlled Portland group of companies.

The consolidated financial statements of Clarien Bank Limited as at and for the year ended December 31, 2017 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 25 Reid 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 Limited	Holding company
First Bermuda Securities Limited	Brokerage services; subsidiary of First Bermuda Group Limited
Onshore Nominees Limited	Nominee entity of First Bermuda Group Limited
Offshore Nominees Limited	Nominee entity of First Bermuda Group Limited
Clarien Investments Limited ("CIL")	Investment management
Clarien Brokerage Limited	Brokerage services; subsidiary of CIL
Clarien Nominees Limited	Nominee entity of CIL
Clarien BSX Services Limited	Trading member of Bermuda Stock Exchange; subsidiary of CIL
Clarien Trust Limited	Trust administration
Clarien UK Limited	Inactive

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 June 15, 2018.

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. All amounts have been rounded to the nearest thousand, unless otherwise indicated.

(d) Use of estimates and judgments

The preparation of financial information requires the use of estimates and assumptions about future conditions. 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 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

The Bank did not adopt any new standards during the period that had a material impact on the consolidated financial statements.

(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, 2018, however, the Bank has not applied the following new or amended standards in preparing these consolidated financial statements.

3. Summary of significant accounting policies (continued)

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

(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, 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 de-recognition of financial instruments from IAS 39.

In October 2017, The IASB issued Prepayment Features with Negative Compensation (Amendments to IFRS 9). The amendments are effective for annual periods beginning on or after January 1, 2019, with early adoption permitted.

The Bank will apply IFRS 9 as issued in July 2014 on January 1, 2018 and will early adopt the amendments to IFRS 9 on the same date. Based on assessments undertaken to date, the total estimated adjustment of the adoption of IFRS 9 on the opening balance of the Bank's equity at January 1, 2018 is approximately a $2,000 increase. This is due to a decrease in the estimated impairment requirements, based on the new provisions of the standard as applied by the Bank's model.

This assessment is preliminary because not all transition work has been finalised. The actual impact of adopting IFRS 9 on January 1, 2018 may change because:

- although parallel runs were carried out in the second half of 2017, the new systems and associated controls in place have not been operational for a more extended period;

- the Bank is refining and finalising its models for ECL calculations; and

- the new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Bank finalises its first financial statements that include the date of initial application.

Classification and measurement

IFRS 9 introduces a principles-based approach to the classification of financial assets based on an entity's business model and the nature of the cash flows of the asset. These factors determine whether the financial assets are measured at amortised cost, fair value through other comprehensive income ('FVOCI') or fair value through profit and loss ('FVPL'). For financial liabilities, IFRS 9 includes the requirements for classification and measurement previously included in IAS 39. For certain liabilities measured at fair value, gains or losses relating to changes in the entity's own credit risk are to be included in other comprehensive income.

Impairment

The impairment requirements of IFRS 9 apply to financial assets measured at amortised cost and FVOCI, lease receivables and certain loan commitments and financial guarantee contracts. At initial recognition, an allowance (or provision in the case of commitments and guarantees) is required for expected credit losses ('ECL') resulting from default events that are possible within the next 12 months ('12 month ECL'). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognised are considered to be 'stage 1'; financial assets which are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment are considered to be in default or otherwise impaired are in 'stage 3'.

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

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

(i) IFRS 9 Financial Instruments (continued)

The assessment of whether credit risk has increased significantly since initial recognition is performed for each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument, rather than by considering an increase in ECL.

The assessment of credit risk, and the estimation of ECL, are required to be unbiased and probability-weighted, and should incorporate all available information which is relevant to the assessment including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money. As a result, the recognition and measurement of impairment is intended to be more forward-looking than under IAS 39 and the resulting impairment charge will tend to be more volatile.

Hedge accounting

The general hedge accounting requirements aim to simplify hedge accounting, creating a stronger link between it and risk management strategy and permitting the former to be applied to a greater variety of hedging instruments and risks. The standard does not explicitly address macro hedge accounting strategies, which are being considered in a separate project. To remove the risk of any conflict between existing macro hedge accounting practice and the new general hedge accounting requirements, IFRS 9 includes an accounting policy choice to remain with IAS 39 hedge accounting. The Bank does not currently use hedge accounting and is not anticipating any change in this policy. This section of IFRS 9 is, therefore, unlikely to apply to the Bank, at this present time.

Transition

The classification and measurement and impairment requirements are to be applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirement to restate comparative periods. The mandatory application date for the standard as a whole is January 1, 2018 and the Bank intends to adopt the Standard on this date.

IFRS 9 Implementation

Within the Bank, significant preparatory, design and implementation work has taken place focused on the introduction of an IFRS 9 compliant impairment calculation model. The documentation of the Bank's accounting policy, the development of operating and risk modelling methodologies and an impact assessment of the classification and measurement requirements have also been included in the process. This work was largely completed in 2017 and since completion the model has been running in parallel with the Bank's current processes, in order to assess its impact and enhance its effectiveness.

(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, 2018, with early adoption permitted.

The Bank has assessed the impact of IFRS 15 and it expects that the standard will have no significant effect on the consolidated financial statements.

3. Summary of significant accounting policies (continued)

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

(iii) IFRS 16 Leases (continued)

IFRS 16 introduces a new single lessee accounting model and requires a lessee to recognize all assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. IFRS 16 contains expanded disclosure requirements and is effective for annual reporting periods beginning on or after January 1, 2019.

The Bank is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 16.

(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.

(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.

3. Summary of significant accounting policies (continued)

(g) Financial assets and liabilities (continued)

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.

Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

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 generally accepted methodologies for pricing such financial instruments.

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

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

Fair value measurement (continued)

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 did make 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. The employee loan scheme is no longer offered and loans to employees are now underwritten on an arms-length basis.

Reduced rate loans are financial assets and under IAS 39, they 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. 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 re-imbursement 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.

3. Summary of significant accounting policies (continued)

(g) Financial assets and liabilities (continued)

Identification and measurement of impairment (continued)

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 with indicators of impairment are assessed for specific impairment. Loans and advances and debt securities classified as loans and receivables that are not individually significant or that do not have indicators of impairment, are collectively assessed for impairment by grouping together such loans and advances and debt securities classified as loans and receivables with similar characteristics.

A collective allowance for groups of homogeneous loans is established using a formula approach based on historic data. The methodology uses statistical analysis of historical data on delinquency and collateral trends to estimate the probability of default and expected collateral values respectively. The loss given default is then estimated based on the expected collateral values. 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. Default rates and loss factors are regularly benchmarked against actual loss experience.

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 allowance 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 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.

3. Summary of significant accounting policies (continued)

(g) Financial assets and liabilities (continued)

Identification and measurement of impairment (continued)

The Bank writes off certain loans and advances and investment securities when they are determined to be uncollectible (see Note 8).

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.

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.

3. Summary of significant accounting policies (continued)

(h) Investment securities

Where a decline in the 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 profit and loss 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.

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 when control is transferred to the Bank. 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.

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

(k) Business combinations (continued)

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 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.

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.

3. Summary of significant accounting policies (continued)

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

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 are as follows:

Buildings	30-40 years
Furniture and fixtures	5-15 years
Computer systems and equipment	1-10 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 property

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.

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

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.

3. Summary of significant accounting policies (continued)

(n) Intangible assets and related amortization (continued)

(ii) 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 1-10 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.

(o) 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.

(p) 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.

3. Summary of significant accounting policies (continued)

(p) Interest income and expense (continued)

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.

(q) 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.

Banking fees primarily include interchange income, annual fees and late fees. Banking 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.

(r) 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.

(s) 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.

(t) 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.

(u) 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.

(v) 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 the consolidated statement of comprehensive income when they are due in respect of services rendered before the end of the reporting period.

3. Summary of significant accounting policies (continued)

(w) Share capital

Share issuance costs

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares 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, Risk, and Governance and Human Resource Committees, which are responsible for approving and monitoring Bank risk management policies in their respective areas. All Board Committees are comprised of the appropriate mix of both independent and non-independent members and report regularly to the Board of Directors on their activities. The Board Committees are supported by management level committees, namely; the Executive Committee, the Credit Committee, the Asset and Liability Committee ("ALCO"), the Compliance Committee, the Operational Risk Committee and the New Products Committee. Each of these management level committees are directly responsible for defined areas of risk, developing related risk management policies and procedures and quarterly reporting to the Risk Committee.

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 Risk 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.

4. Risk management (continued)

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 91% (December 31, 2016 - 92%) 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, 2017 and December 31, 2016 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 13).

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 intended to actively identify, manage, monitor and report credit risk on its mortgage and non-mortgage portfolios. The Bank considers these to be suitable for 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 Risk Committee of the Board, reviews and approves the Bank's credit risk strategy and credit risk policy on a quarterly basis.

The objectives of the credit risk strategy are 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 to
- 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.

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

4. Risk management (continued)

Credit risk (continued)

Credit risk: loans and advances (continued)

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:

	2017		2016	
Not impaired:				
Neither past due or impaired	$ 648,447	83%	$ 636,489	81%
Past due, but not individually impaired:				
From 7 days up to 3 months	25,140	3%	32,881	4%
3 to 6 months	6,075	1%	4,941	1%
6 to 12 months	4,054	1%	11,286	2%
Over 12 months	18,981	2%	23,506	3%
	54,250	7%	72,614	10%
Individually impaired loans				
Up to 3 months	8,449	1%	9,291	1%
3 to 6 months	4,120	1%	1,400	–
6 to 12 months	839	–	2,801	–
Over 12 months	62,365	8%	65,516	8%
	75,773	10%	79,008	9%
Total (Note 8)	$ 778,470	100%	$ 788,111	100%

Under 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.

For the year-ended December 31, 2017, loans amounting to $61,213 (December 31, 2016 - $56,709), that would otherwise be considered 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 would 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.

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

4. Risk management (continued)

Credit risk (continued)

Credit risk: loans and advances (continued)

Aggregate undiscounted fair value of collateral held:

		2017		2016
Past due but not impaired loans	$	58,709	$	124,352
Impaired loans		77,961		65,100
	$	136,670	$	189,452

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 Risk Committee of the Board of Directors. The Bank uses the external credit agency ratings by Standard & Poor's ("S&P"), 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 held in local and foreign banks and sovereign securities.

	2017		2016	
Concentration by credit grading				
AA	174,504	82%	162,780	89%
A	30,513	15%	12,937	7%
Other	6,867	3%	7,678	4%
	$ 211,884	100%	$ 183,395	100%
Concentration by region				
North America (including Bermuda)	$ 211,884	100%	$ 183,395	100%
	$ 211,884	100%	$ 183,395	100%

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

	2017		2016	
Concentration by credit grading				
AAA	$ 90,736	50%	$ 59,934	37%
AA	62,503	35%	84,086	52%
A	26,955	15%	16,908	11%
Other	695	–	705	–
	$ 180,889	100%	161,633	100%

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

4. Risk management (continued)

Credit risk (continued)

Credit risk: interbank lending and investment securities (continued)

	2017		2016	
Concentration by region				
North America (including Bermuda)	$ 161,163	89%	$ 151,688	94%
Europe	9,970	6%	9,945	6%
Asia	9,756	5%	–	–
	$ 180,889	100%	$ 161,633	100%

US Treasuries, which are rated AA are the largest portfolio holding at December 31, 2017. The remainder of the Bank's investment portfolio are holdings in sovereigns, supra-nationals bonds and high grade corporates.

As at December 31, 2017, 100% (December 31, 2016 - 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, 2017 is $57 (December 31, 2016 - $71).

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 coverage ratio (LCR) guidelines, to ensure the Bank has a sufficient level of high-quality liquid assets (HQLA) to survive a significant liquidity stress event over a 30 day time horizon; the LCR is calculated by dividing the total of HQLA over the total net cash outflows of the next 30 days, (iii) maintaining holdings of high quality liquid assets and short maturity interbank placements and (iv) maintaining external counterparty repurchase agreements.

The development and implementation of the Bank's liquidity policy is the responsibility of ALCO and is approved by the Risk 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 Risk Committee.

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

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

4. **Risk management** (continued)

Liquidity risk (continued)

Contractual Cashflow analysis of financial liabilities

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

December 31, 2017

	Carrying amount	Gross nominal inflow / (outflow)	Repayable on demand	Up to 3 mnths	3-6 mnths	6-12 mnths	1-5years	>5 years
Financial liabilities								
Due to depositors	$ 1,074,843	$ (1,082,582)	$ (517,094)	$ (259,187)	$ (80,029)	$ (147,612)	$ (78,660)	$ –
Accounts payable and accrued Liabilities	3,854	(3,854)	(3,854)	–	–	–	–	–
Due to clients	160	(160)	(160)	–	–	–	–	–
Deferred income	108	(108)	(108)	–	–	–	–	–
	$ 1,078,965	$ (1,086,704)	$ (521,216)	$ (259,187)	$ (80,029)	$ (147,612)	$ (78,660)	$ –
Unrecognized loan commitments	–	(29,906)	–	(7,536)	(16)	(686)	(19,681)	(1,987)
Financial guarantees and letters of credit	–	(1,391)	–	(890)	(325)	(176)	–	–
Total financial liabilities	$ 1,078,965	$ (1,118,001)	$ (521,216)	$ (267,613)	$ (80,370)	$ (148,474)	$ (98,341)	$ (1,987)

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

4. **Risk management** (continued)

Liquidity risk (continued)

December 31, 2016

	Carrying amount	Gross nominal inflow / (outflow)	Repayable on demand	Up to 3 mnths	3-6 mnths	6-12 mnths	1-5years	>5 years
Financial liabilities								
Due to depositors	$ 1,053,698	$ (1,062,110)	$ (464,661)	$ (220,777)	$ (53,906)	$ (160,453)	$ (162,313)	$ –
Accounts payable and accrued liabilities	3,621	(3,621)	(3,621)	–	–	–	–	–
Due to clients	266	(266)	(266)	–	–	–	–	–
Deferred income	84	(84)	(84)	–	–	–	–	–
	$ 1,057,669	$ (1,066,081)	$ (468,632)	$ (220,777)	$ (53,906)	$ (160,453)	$ (162,313)	$ –
Unrecognized loan commitments	–	(17,880)	–	(9,170)	(395)	–	(4,409)	(3,906)
Financial guarantees and letters of credit	–	(1,521)	–	(890)	(325)	(306)	–	–
Total financial liabilities	$ 1,057,669	$ (1,085,482)	$ (468,632)	$ (230,837)	$ (54,626)	$ (160,759)	$ (166,722)	$ (3,906)

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 Risk 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 Risk 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 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 Risk Committee review market risk limits, on a regular basis, to ensure there are no breaches.

(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 shareholder's equity as at December 31, 2017. 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.

December 31, 2017

	Increase in net interest income and equity
100 basis point increase	$ 1,224
200 basis point increase	$ 2,453
100 basis point decrease	$ (4,491)
200 basis point decrease	$ (9,196)

December 31, 2016

	Increase in net interest income and equity
100 basis point increase	$ 1,696
200 basis point increase	$ 3,401
100 basis point decrease	$ (4,175)
200 basis point decrease	$ (9,925)

The tables on the following page summarize 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.

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

4. Risk management (continued)

December 31, 2017 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	$221,045	$ 182,150	$ -	$ -	$ -	$ -	$ 38,895
Investment securities	180,889	23,059	18,000	12,933	121,100	6,000	(203)
Accounts receivable and prepaid expenses	3,929	–	–	–	–	–	3,929
Accrued interest on cash, deposits with banks and securities	914	–	–	–	–	–	914
Loans and advances	745,051	719,032	5,904	20,115	–	–	–
Due from related parties	1,303	–	–	–	–	–	1,303
Investment property	3,477	–	–	–	–	–	3,477
Property and equipment	15,660	–	–	–	–	–	15,660
Intangible assets	20,674	–	–	–	–	–	20,674
Total assets	1,192,942	924,241	23,904	33,048	121,100	6,000	84,649
Due to depositors	1,074,843	716,684	50,986	101,395	205,778	–	–
Accounts payable and accrued liabilities	3,854	–	–	–	–	–	3,854
Due to clients	160	–	–	–	–	–	160
Deferred income	108	–	–	–	–	–	108
Equity	113,977	–	–	–	–	–	113,977
Total liabilities and equity	1,192,942	716,684	50,986	101,395	205,778	–	118,099
Interest rate sensitivity gap	$ –	$ 207,557	$ (27,082)	$ (68,347)	$ (84,678)	$ 6,000	$ (33,450)
Cumulative interest rate sensitivity gap	$ –	$ 207,557	$ 180,475	$ 112,128	$ 27,450	$ 34,450	$ –

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

4. Risk management (continued)

December 31, 2016 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	$ 192,259	$ 153,719	$ –	$ –	$ –	$ –	$ 38,540
Investment securities	161,633	10,071	9,066	25,000	111,100	6,000	396
Accounts receivable and prepaid expenses	3,941	–	–	–	–	–	3,941
Accrued interest on cash, deposits with banks and securities	683	–	–	–	–	–	683
Loans and advances	756,375	715,526	5,777	18,895	–	–	16,177
Due from related parties	7,739	–	–	–	–	–	7,739
Investment property	3,611	–	–	–	–	–	3,611
Property and equipment	16,818	–	–	–	–	–	16,818
Intangible assets	21,393	–	–	–	–	–	21,393
Total assets	1,164,452	879,316	14,843	43,895	111,100	6,000	109,298
Due to depositors	1,053,698	662,760	32,111	64,283	294,544	–	–
Accounts payable and accrued liabilities	3,621	–	–	–	–	–	3,621
Due to clients	266	–	–	–	–	–	266
Deferred income	84	–	–	–	–	–	84
Equity	106,783	–	–	–	–	–	106,783
Total liabilities and equity	1,164,452	662,760	32,111	64,283	294,544	–	110,754
Interest rate sensitivity gap	$ –	$ 216,556	$ (17,268)	$ (20,388)	$ (183,444)	$ 6,000	$ (1,456)
Cumulative interest rate sensitivity gap	$ –	$ 216,556	$ 199,288	$ 178,900	$ (4,544)	$ 1,456	$ –

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.

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

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, 2017

	Fair value through profit or loss	Fair value through comprehensive income	Amortised cost	Total carrying amount	Fair value
Cash and cash equivalents	$ –	$ –	$ 221,045	$ 221,045	$ 221,045
Investment securities	–	180,832	57	180,889	180,889
Loans and advances	–	–	745,051	745,051	746,150
Other assets	–	–	5,176	5,176	5,176
	$ –	$ 180,832	$ 971,329	$ 1,152,161	$ 1,153,260
Deposits	$ –	$ –	$ 1,074,843	$ 1,074,843	$ 1,076,631
Other liabilities	–	–	4,122	4,122	4,122
	$ –	$ –	$ 1,078,965	$ 1,078,965	$ 1,080,753

December 31, 2016

	Fair value through profit or loss	Fair value through comprehensive income	Amortised cost	Total carrying amount	Fair value
Cash and cash equivalents	$ –	$ –	$ 192,259	$ 192,259	$ 192,259
Investment securities	–	161,562	71	161,633	161,633
Loans and advances	–	–	756,375	756,375	757,761
Other assets	–	–	11,691	11,691	11,691
	$ –	$ 161,562	$ 960,396	$ 1,121,958	$ 1,123,344
Deposits	$ –	$ –	$ 1,053,698	$ 1,053,698	$ 1,058,737
Other liabilities	–	–	3,971	3,971	3,971
	$ –	$ –	$ 1,057,669	$ 1,057,669	$ 1,062,708

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

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, 2017			
	Level 1	Level 2	Level 3	Total
Financial Assets				
Securities - available-for-sale				
US government and agency				
- Treasuries	$ 49,510	$ –	$ –	$ 49,510
- Agency debt	–	9,960	–	9,960
Other OECD government & government guaranteed and international organizations	–	102,678	–	102,678
Corporate debt securities	–	18,046	–	18,046
Equities	–	638	–	638
Total available-for-sale securities	**$ 49,510**	**$131,322**	**$ –**	**$180,832**

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

4. Risk management (continued)

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

	December 31, 2016			
	Level 1	Level 2	Level 3	Total
Financial Assets				
Securities - available-for-sale				
US government and agency				
- Treasuries	$ 59,938	$ –	$ –	$ 59,938
- Agency debt	–	15,057	–	15,057
Other OECD government & government guaranteed and international organizations	–	56,773	–	56,773
Corporate debt securities	–	29,160	–	29,160
Equities	–	634	–	634
Total available-for-sale securities	**$ 59,938**	**$ 101,624**	**$ –**	**$161,562**

There were no significant transfers between Levels 1, 2 and 3 during the year ended December 31, 2017 (2016- nil).

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.

4. Risk management (continued)

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.

The Bank's operational risk framework is intended to provide:

- 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.

Basel III superseded Basel II and took effect on January 1, 2015 with transitional arrangements until full implementation in 2019. The three pillar framework of Basel II is unchanged but there have been changes to the detailed requirements within each pillar. Pillar 3 has more detailed disclosure requirements and will adopt generic templates over the course of the transition to allow improved comparability and transparency between institutions covered by Basel accords.

The key elements of Basel III changes to capital requirements are as follows:

Changes to the definition of capital and the introduction of common equity Tier 1 (CET1). Over the transition period there will be changes and additions to capital deductions from CET1 and Tier 2 capital, including the available-for-sale reserve.

Higher thresholds for all forms of capital will be required with an increased focus on CET1. A capital conservation buffer of 2.5% will be introduced and phased in over the implementation period. Additionally, a capital surcharge for Domestic Systematically Important Banks ('D-SIB') ranging between 0.5% and 3.0% for all Bermuda Banks has also been implemented.

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

4. Risk management (continued)

Capital management (continued)

Introduction of a non-risk based Leverage Ratio, being a measure of Tier 1 capital held against total assets, including certain off-balance sheet financial commitments. The Bank's unaudited leverage ratio was 9.06% as at December 31, 2017, which is above the minimum proposed by the Bermuda Monetary Authority of 5.0%.

The Bank has complied with all externally imposed minimum capital requirements throughout the current year.

The new Basel rules also address areas of liquidity. The authority has adopted a Liquidity Coverage Ratio ('LCR') with phased-in implementation consistent with that published by the Basel Committee. The LCR aims to ensure Banks have sufficient stock of unencumbered highly liquid assets to survive a high liquidity stressed scenario lasting 30 days. Further information regarding the implementation of Basel III can be found on the Bermuda Monetary Authority's website (www.bma.bm).

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

	Unaudited 2017	Unaudited 2016
Tier 1 capital		
Preferred share capital	$ –	$ 20,000
Common share capital	5,000	5,000
Contributed surplus	42,806	18,550
General reserve	10,000	10,000
Current year's retained profit, reviewed by external auditors, after dividends	3,889	1,214
Retained earnings and other reserves	54,903	52,771
Goodwill	(7,456)	(7,456)
Total Tier 1 capital	$ 109,142	$ 100,079
Tier 2 capital		
Fixed assets revaluation reserves	$ –	$ –
Collective allowance for credit losses	5,861	5,626
Total Tier 2 capital	$ 5,861	$ 5,626
Total Tier 1 and 2 capital	$ 115,003	$ 105,705
Capital ratios		
Tier 1 capital	18.72%	16.53%
Total capital	19.72%	17.46%

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

5. Cash and cash equivalents

	2017	2016
Cash in vault	$ 9,161	$ 8,864
Cash at local banks	11,712	12,923
Cash at foreign banks	27,074	55,499
	$ 47,947	$ 77,286
Other cash equivalents	$ 173,098	$ 114,973
Total Cash and cash equivalents	**$ 221,045**	**$ 192,259**

Cash at foreign banks of $27,074 (2016 - $55,499) includes $12,130 (2016 - $40,419) held in US dollars and $14,944 (2016 - $15,080) held in other foreign currencies. The average effective interest rate earned on cash and deposits with banks for the year ended December 31, 2017 was 0.12% (2016 - 0.03%).

Cash and deposits with banks includes $160 (2016 - $266) of restricted funds held in escrow on behalf of customers, and $5,030 (2016 - $5,005) pledged to collateralise standby letters of credit issued on behalf of customers.

As at December 31, 2017, foreign currency interest bearing deposits with banks of $23,557 includes $14,944 denominated in foreign currencies other than US dollar (2016: $38,719 included $15,080). As at December 31, 2017 and December 31, 2016, all other cash and deposits with banks are denominated in Bermuda dollars or in US dollars.

Other cash equivalents include highly-liquid sovereign securities with a term to maturity of 90 days or less from the date of acquisition.

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

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, 2017 and December 31, 2016.

No investment securities have been pledged (2016 - $0) as collateral to third parties.

	December 31, 2017					
	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	$ –	$ 49,509	$ –	$ –	$ 49,509	$ 49,509
- Agency debt	–	9,960	–	–	9,960	9,960
Other OECD government & government guaranteed and international organizations	45,877	50,776	6,026	–	102,679	102,679
Corporate debt securities	5,000	10,013	3,033	–	18,046	18,046
Total – fixed income	50,877	120,258	9,059	–	180,194	180,194
Equities						
Equities	–	–	–	638	638	638
Total – available-for-sale	**$ 50,877**	**$ 120,258**	**$ 9,059**	**$ 638**	**$ 180,832**	**$ 180,832**
Debt securities classified as loans and receivables						
Asset-backed securities	$ –	$ –	$ 57	$ –	$ 57	$ 57
Total investment securities	**$ 50,877**	**$ 120,258**	**$ 9,116**	**$ 638**	**$ 180,889**	**$ 180,889**
Average effective interest rate	0.94%	1.39%	2.55%	– %	1.32%	

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

6. Investment securities (continued)

	December 31, 2016					
	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	$ 14,934	$ 45,004	$ –	$ –	$ 59,938	$ 59,938
- Agency debt	5,015	10,042	–	–	15,057	15,057
Other OECD government & government guaranteed and international organizations	–	51,119	5,654	–	56,773	56,773
Corporate debt securities	19,098	10,062	–	–	29,160	29,160
Total – fixed income	39,047	116,227	5,654	–	160,928	160,928
Equities						
Equities	–	–	–	634	634	634
Total – available-for-sale	**$ 39,047**	**$ 116,227**	**$ 5,654**	**$ 634**	**$ 161,562**	**$ 161,562**
Debt securities classified as loans and receivables						
Asset-backed securities	$ –	$ –	$ 71	$ –	$ 71	$ 68
Total investment securities	**$ 39,047**	**$ 116,227**	**$ 5,725**	**$ 634**	**$ 161,633**	**$ 161,630**
Average effective interest rate	1.09%	1.14%	3.55%	– %	1.21%	

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

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.

The Bank held asset-backed securities all of which are rated B or above by Standard & Poor's with an amortized cost totalling $57 and fair value totalling $57 (2016 - $71 and $68 respectively).

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 high-quality 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, 2017.

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 (losses) / gains on investment securities are made up of:

	2017	2016
Net realized (losses) / gains on sale of:		
Available for sale securities	$ (59)	$ 811
Recoveries on:		
Debt Securities classified as loans	$ –	$ 42
Total	**$ (59)**	**$ 853**

7. Accounts receivable and prepaid expenses

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

	2017	2016
Prepaid staff loan benefit	$ 749	$ 863
Management fees, trail commissions and custody fees receivable	1,895	1,926
Other prepaid expenses	984	672
Accounts receivable	301	480
Total	$ 3,929	$ 3,941

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

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:

	2017	2016
Residential mortgages	$ 615,803	$ 640,120
Commercial mortgages	93,627	87,925
Loans and advances - secured	61,111	52,026
Loans and advances - unsecured	1,673	1,555
Credit card receivables	6,256	6,485
	778,470	788,111
Allowance for credit losses on loans, mortgages and credit card receivables	(33,419)	(31,736)
	$ 745,051	$ 756,375

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

	2017			2016		
	Amortized cost		Fair value	Amortized cost		Fair value
Maturity analysis						
One year or less	$ 25,547	3%	$ 25,772	$ 19,524	3%	$ 19,571
More than one year	719,504	97%	720,378	736,851	97%	738,190
	$ 745,051	100%	746,150	$ 756,375	100%	$ 757,761

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 is presented in Note 4.

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

8. Loans and advances (continued)

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

	2017	2016
Residential and commercial mortgages:		
Gross loans	$ 68,867	$ 71,934
Specific allowance	(24,591)	(22,714)
Net mortgages	44,276	49,220
Loans and chattel mortgages:		
Gross loans	6,906	7,074
Specific allowance	(2,967)	(3,396)
Net loans and chattel mortgages	3,939	3,678
	$ 48,215	$ 52,898

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 (2016 - 30 years). At December 31, 2017 the weighted average time remaining to maturity for mortgages was 16 years (2016 - 17 years). At December 31, 2017 loans and chattel mortgages are repayable in monthly or periodic instalments generally over periods not exceeding 6 years (2016 - 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 22.75% (2016 - 12% to 22.75%) and are unsecured.

The average effective interest rate on total loans and mortgages receivable at December 31, 2017 is 6.43% (2016 - 6.31%).

Total loans include $74,942 (2016 - $45,907) denominated in US dollars.

At December 31, 2017, loans, mortgages and credit card receivables included $301 (2016 - $343) receivable from directors, and $47,850 (2016 - $54,866) 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 4.5% to 6% (2016 - 1.99% to 6.00%), 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.

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

8. Loans and advances (continued)

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:

	2017	2016
Specific allowances for impairment:		
Balance at 1 January	$ 26,110	$ 20,674
Impairment loss for the year:		
Charge for the year, net	5,811	8,839
Write-offs	(4,846)	(3,710)
Recoveries	483	307
Balance at 31 December	27,558	26,110
Collective allowances for impairment:		
Balance at 1 January	5,626	5,902
Impairment loss for the year:		
(Release) / charge for the year, net	235	(276)
Balance at 31 December	5,861	5,626
	$ 33,419	$ 31,736

Write-offs during the years ended December 31, 2017 and 2016 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.

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

9. Investment property

Cost		
At January 1, 2016	$	4,994
At December 31, 2016	$	4,994
At December 31, 2017	$	4,994
Amortization and impairment losses		
At January 1, 2016	$	1,249
Amortization for the year		134
At December 31, 2016	$	1,383
Amortization for the year	$	134
At December 31, 2017	$	1,517
Carrying value		
At December 31, 2016	$	3,611
At December 31, 2017	$	3,477

The fair value of investment property as at December 31, 2017 is $4,082 (2016 - $3,880). Investment property consists of one property with a carrying value of $3,477 (2016 - $3,611). One floor of this property, which has been independently assessed as 18% of the total leasable area of the building, was reclassified to property and equipment, due to the Bank using it as corporate offices, from 2013.

Management has tested the carrying value of investment property at December 31, 2017 for impairment and found the recoverable amount to be greater than the carrying value. In determining the recoverable amount an independent appraisal and value-in-use model was used. In accordance with an independent appraisal a discount factor of 7% (2016 - 7%) was applied to the value-in-use cash flow projections to determine the net present value.

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

10. Property and equipment

Property and equipment held by the Bank are as follows:

	Buildings	Furniture and fixtures	Computer hardware and equipment	Artwork	Leasehold improvements	Total
Cost						
Balance at January 1, 2016	13,597	6,052	14,726	606	11,982	46,963
Additions	7	39	810	–	131	987
Balance at December 31, 2016	13,604	6,091	15,536	606	12,113	47,950
Balance at January 1, 2017	13,604	6,091	15,536	606	12,113	47,950
Additions	–	149	375	–	–	524
Balance at December 31, 2017	13,604	6,240	15,911	606	12,113	48,474
Accumulated depreciation						
Balance at January 1, 2016	5,068	5,113	13,651	–	5,476	29,308
Depreciation charge for the year	345	248	600	–	631	1,824
Balance at December 31, 2016	5,413	5,361	14,251	–	6,107	31,132
Balance at January 1, 2017	5,413	5,361	14,251	–	6,107	31,132
Depreciation charge for the year	345	252	453	–	632	1,682
Balance at December 31, 2017	5,758	5,613	14,704	–	6,739	32,814
Carrying amounts						
Balance at December 31, 2016	$ 8,191	$ 730	$ 1,285	$ 606	$ 6,006	$ 16,818
Balance at December 31, 2017	$ 7,846	$ 627	$ 1,207	$ 606	$ 5,374	$ 15,660

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

11. Intangible assets

Intangible assets are as follows:

		Computer software		Goodwill		Total
Cost						
Balance at January 1, 2016	$	26,339	$	7,456	$	33,795
Additions		982		–		982
Write-offs		(26)		–		(26)
Balance at December 31, 2016	$	27,295	$	7,456	$	34,751
Balance at January 1, 2017	$	27,295	$	7,456	$	34,751
Additions		2,017		–		2,017
Balance at December 31, 2017	$	29,312	$	7,456	$	36,768
Accumulated amortization						
Balance at January 1, 2016	$	10,733	$	–	$	10,733
Write-offs		(26)		–		(26)
Amortization charge for the year		2,651		–		2,651
Balance at December 31, 2016	$	13,358	$	–	$	13,358
Balance at January 1, 2017	$	13,358	$	–	$	13,358
Amortization charge for the year		2,736		–		2,736
Balance at December 31, 2017	$	16,094	$	–	$	16,094
Carrying amounts						
Balance at December 31, 2016	$	13,937	$	7,456	$	21,393
Balance at December 31, 2017	$	13,218	$	7,456	$	20,674

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.

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 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 11.41%, 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. The Bank estimates that reasonably possible changes in these assumptions are not expected to cause the recoverable amount of the Bank's CGU's to decline below the carrying amount.

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

12. Due to depositors

Total deposits include $390,958 (2016 - $353,624) denominated in US dollars and $15,719 (2016 - $16,096) denominated in other foreign currencies. In 2017, the average effective interest rate paid on demand deposits increased, compared to 2016, reflecting the US Federal Reserve increase in the federal funds rate during December 2017. The Bank has $148,701 (2016 - $106,477) of deposits bearing interest rates linked to the federal funds rate, all denominated in US dollars.

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

	2017		2016	
	Average effective interest rate	Amount	Average effective interest rate	Amount
Demand	0.37%	517,416	0.18%	$ 464,309
Up to 3 months	1.09%	182,800	1.05%	183,924
3 - 6 months	1.37%	50,986	0.80%	32,362
6 - 12 months	2.15%	147,160	1.35%	64,283
1 - 5 years	2.20%	160,013	2.32%	294,544
Total	1.06%	1,058,375	1.03%	1,039,422
Accrued interest		16,468		14,276
Total		$ 1,074,843		$ 1,053,698

13. 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% (2016 - 5%).

The work force of the Bank included 19 key management employees in 2017 (2016 - 16). During the year ended December 31, 2017, salaries, benefits and directors fees totalling $4,812 (2016 - $4,325) were paid to key management employees of the Bank. In addition there are 9 (2016 - 8) directors who are considered key management personnel.

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

13. Related party transactions and balances (continued)

Consolidated Statement of Comprehensive Income

		2017		2016
Interest income	$	1,945	$	1,611
Interest expense	$	503	$	562
Fee and commission income	$	4,062	$	3,799
Personnel expenses	$	5,431	$	4,886
Other expenses	$	2,807	$	2,960
Rent	$	344	$	205

Included in other expenses are $363 (2016 - $366) paid to key management employees. Personnel expenses includes $4,449 (2016 - $3,959) 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, 2017, the Bank recharged $95 (2016 - $95) to companies associated through significant influence, representing portions of certain expenses provided by the Bank. Of this amount, $48 (2016 - $78) has been included in personnel expenses and $47 (2016 - $47) has been included in other expenses in the consolidated statement of comprehensive income.

Consolidated Statement of Financial Position

		2017		2016
Related party balances - Included in assets				
Loans and advances (Key management personnel)	$	14,907	$	8,509
Loans and advances (Entities with significant influence)	$	16,933	$	17,094
Loans and advances (Companies associated through significant influence)	$	100	$	463
Accounts receivable and prepaid expenses (Companies associated through significant influence)	$	50	$	3
Due from related parties (Parent)	$	–	$	6,206
Due from related parties (Companies associated through significant influence)	$	1,303	$	1,533
Related party balance - Included in liabilities				
Due to depositors (Key management personnel)	$	8,928	$	4,130
Due to depositors (Companies associated through significant influence)	$	76,991	$	77,390
Accounts payable and accrued liabilities (Companies associated through significant influence)	$	52	$	87

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.

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

14. Accounts payable and accrued liabilities

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

	2017	2016
Accounts payable	$ 406	$ 353
Accrued liabilities	2,296	2,881
Bonus payable	696	–
Foreign currency tax payable	299	294
Visa rewards payable	157	93
Total	$ 3,854	$ 3,621

15. General reserve, retained earnings and contributed surplus

The total authorized, issued and fully paid Bermuda dollar common share capital is 4,999,999 (2016 - 4,999,999) with a par value of $1 per share. Common shares carry no right to regular dividends. In December 2017, the Bank has redeemed 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. The preferred shares were redeemed and converted to contributed surplus on December 13, 2017.

During the year ended December 31, 2017, dividends of $nil (2016 - $nil) were declared and paid to the Bank's shareholders of common shares. The Bank paid dividends of $830 on its preferred shares (2016 - $778) 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.

In 2016 the Bank's parent company, Clarien Group Limited, contributed a further $12,600 in cash into the Bank as contributed surplus. The movement in contributed surplus in 2015 represented a $1,250 payment to the shareholder.

On December 13, 2017, the Bank's parent company, Clarien Group Limited, contributed a further $6,281 of capital into the Bank as contributed surplus. $2,025 of transaction fees were paid from this contribution.

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

16. Net interest income

Interest income is comprised of:		2017		2016
Loans and advances	$	51,730	$	51,977
Available for sale investments		2,872		1,753
Cash equivalents		839		–
Other interest income		93		85
Total interest income	$	55,534	$	53,815

Interest expense is comprised of:				
Customer accounts	$	11,193	$	10,799
Total interest expense	$	11,193	$	10,799

17. Net fee and commission income

Fee income is comprised of:		2017		2016
Investment Management	$	6,623	$	6,296
Banking		6,423		5,239
Brokerage		637		664
Trust		681		624
Advisory		334		241
Other		669		671
Total fee income	$	15,367	$	13,735

Fee expense is comprised of:				
Banking	$	2,766	$	2,506
Investment Management		746		676
Other		277		216
Total	$	3,789	$	3,398

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

18. Other expenses

		2017		2016
Information technology expenses	$	3,503	$	4,134
Office expenses		1,819		2,003
Professional fees		2,592		1,988
Rent expenses		957		953
Advertising		726		831
Recruitment, training and travel		707		653
License and insurance costs		2,446		1,659
Bank charges		481		360
Directors' fees and expenses		363		366
Miscellaneous expenses		1,266		1,078
Total other expenses	$	14,860	$	14,025

19. Pension expense

The Bank's employees participate in a defined contribution pension plan sponsored by a company associated through sigifncant influence. During the year ended December 31, 2017, contributions amounting to $859 (2016 - $835) 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, 2017, were contributions amounting to $171 (2016 - $144), which were made by the Bank on behalf of its key management personnel.

20. 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 (excluding credit-card commitments), 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.

		2017		2016
Commitments to extend credit:				
Original term to maturity of one year or less	$	8,239	$	9,565
Original term to maturity of more than one year		21,667		8,315
Total credit commitments	$	29,906	$	17,880

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

20. Commitments, guarantees and contingent liabilities (continued)

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 $1,391 (2016 - $1,521). Of this amount, $741 (2016 - $871), is supported by collateral, 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 (2016 - $650).

The remaining terms of all guarantees and letters of credit range from 1 month to 12 months (2016 - 1 month to 12 months).

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 can be adjusted based on either market values, or the movement in the consumer price index. Future minimum lease payments under the non-cancellable operating leases are as follows:

Fiscal Year		2017		2016
2017	$	–	$	952
2018		952		952
2019		822		822
2020		822		822
2021		822		822
2022		822		822
Thereafter		281		281
	$	4,521	$	5,473

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, 2017, the Bank has contractually committed to incur costs for I.T. systems of $2,544 (2016 - $2,801) within one year and $1,016 (2016 - $1,972) after more than one year.

21. 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, 2017 (2016: No specific disclosures).

22. Comparative Information

Certain prior-year figures have been restated to conform to current year presentation.

CLARIEN

Clarien Bank Limited

Principal Offices and Subsidiaries

Registered Office
25 Reid Street
Hamilton HM 11
Bermuda

Main Branch
19 Reid Street
Hamilton HM 11

Paget Plaza
161 South Road
Paget DV04

Clarien Investments Limited
25 Reid Street
Hamilton HM 11

Clarien Trust Limited
19 Reid Street
Hamilton HM 11

Tel + 441.296.6969 | Fax + 441.294.3165 | www.clarienbank.com

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