

# Pillar 3 Disclosure 2017

## Contents

1. Executive Summary.....	5
1.1 Introduction .....	5
1.2 Table 1: Location of Pillar 3 disclosures within Annual Report and Pillar 3 Report.....	5
1.3 Summary of key metrics .....	6
1.4 Table 2: Key ratios.....	6
2. Scope of the application and disclosure policy.....	7
2.1. Background .....	7
2.2. Frequency.....	7
2.3. Reporting.....	7
2.4. Disclosure process and governance.....	7
2.5. Table 3: Pillar 3 disclosure topics where disclosures are omitted due to reasons of there being no values to report; immaterial values; or confidentiality.....	8
2.6. Location and verification.....	8
2.7. Declaration.....	8
2.8. Table 4: Accounting and regulatory scopes of consolidation - Entities.....	10
2.9. Table 5: Accounting and regulatory scopes of consolidation – Carrying values.....	11
2.10. Table 6: The main sources of differences between regulatory exposure amounts and carrying values in financial statements.....	12
3. Own funds.....	13
3.1. Total available capital .....	13
3.2. Reconciliation of statutory to regulatory capital .....	13
3.3. Capital Instruments - main features and terms .....	13
3.4. Table 7: Prudential filters and deductions.....	13
3.5. Restrictions applied to the calculations of own funds.....	13
3.6. Calculation of capital ratios.....	13
3.7. Transitional own funds disclosure .....	13
4. Capital requirements .....	14
4.1. Assessing the adequacy of internal capital to support current and future activities.....	14

4.2.	Table 8: Overview of Risk Weighted Assets (RWAs) .....	15
5.	Regulatory capital buffers.....	16
5.1.	Introduction .....	16
5.1.1.	Pillar 1.....	16
5.1.2.	Pillar 2.....	16
5.2.	Capital buffers.....	16
5.2.1.	Capital conservation buffer.....	16
5.2.2.	Countercyclical capital buffer (CCyB).....	16
5.3.	Table 9: Geographical distribution of exposures .....	17
5.4.	Table 10: Amount of institution-specific countercyclical capital buffer .....	17
6.	Risk management objectives and policies .....	18
6.1.	Statement and declaration .....	18
6.2.	Structure and organisation of the risk management function .....	18
6.2.1.	Attribution of responsibilities: BLME Board & Board Committees.....	18
6.2.2.	Attribution of responsibilities: Executive Committees .....	20
6.2.3.	Chart 1: Governance structure .....	22
6.2.4.	Structure of key functions.....	22
6.2.5.	Liquidity Risk .....	24
6.3.	The scope and nature of risk reporting and measurement systems .....	26
6.4.	Risk management strategies .....	26
6.5.	Policies for hedging and mitigating risk, and the strategies and processes for monitoring the continuing effectiveness of hedges and mitigants .....	27
7.	Governance Arrangements.....	28
7.1.	Table 14: External directorships .....	28
7.2.	Recruitment of directors.....	28
7.3.	Diversity of the board .....	29
8.	Credit risk.....	30
8.1.	Operating limits.....	30
8.1.1.	Residual value risk.....	30
8.2.	Policies relating to risk mitigant assessments concerning counterparty risk.....	31
8.3.	Policies relating to wrong way risk exposures .....	32
8.3.1.	Table 15: PRS & FX contract exposure .....	32
8.4.	Downgrade of own credit rating.....	32
8.5.	Past due and impaired transactions .....	32

8.6.	Specific, Collective and general credit risk adjustments.....	33
8.7.	Table 16: Performing and non-performing exposure analysis.....	33
8.8.	Table 17: Total and average net amount of exposures .....	34
8.9.	Table 18: Breakdown of net exposure amounts by geographical classification and exposure class .....	35
8.10.	Table 19: Breakdown of net exposure amounts by industrial classification and exposure class .....	36
8.11.	Table 20: Breakdown of net exposure amounts by residual maturity .....	37
8.12.	Table 21: Credit quality of exposures by exposure class and instrument .....	38
8.13.	Table 22: Credit quality of exposures by industry type .....	39
8.14.	Table 23: Credit quality of exposures by geography.....	40
8.15.	Table 24: Ageing of past due exposures .....	41
8.16.	Table 25: Changes in the stock of general and specific credit risk adjustments held against financing arrangements and debt securities that are defaulted or impaired .....	41
8.17.	Table 26: Changes in the stock of defaulted and impaired financing arrangements and debt securities .	42
8.18.	Use of External Credit Assessment Institutions (ECAI Ratings).....	43
8.18.1.	Table 27: The level and extent of the use of ECAI ratings as at 31st December 2017. ....	43
8.19.	Table 28: Breakdown of regulatory exposure values by risk weight .....	44
8.20.	Table 29: CCR exposure by approach.....	45
8.21.	Table 30: CCR exposure by regulatory portfolio and risk .....	46
8.22.	Table 31: CVA capital charge.....	47
8.23.	Table 32: Breakdown of exposures by qualifying and non-qualifying CCP.....	48
9.	Credit risk mitigation.....	49
9.1.	Policies and processes for, and an indication of the extent of, on- and off balance sheet netting .....	49
9.2.	Policies and processes for collateral valuation and management.....	49
9.3.	Main types of collateral taken .....	49
9.3.1.	Guarantees.....	49
9.3.2.	Tangible collateral.....	50
9.4.	Main types of guarantor and credit derivative counterparty and their creditworthiness .....	51
9.5.	Market or credit risk concentrations within the credit mitigation taken .....	51
9.6.	Table 33: CRM techniques – Overview .....	52
9.7.	Table 34: Credit risk exposure and CRM effects.....	52
10.	Unencumbered assets .....	53
10.1.	Table 35: Assets.....	53
11.	Table 36: Exposure to equities not included in the trading book.....	53
12.	Exposure to market risk .....	53

12.1.	Market Risk .....	53
12.2.	Table 37: Market risk under the standardised approach.....	54
13.	Exposure to Operational risk.....	54
14.	Exposure to interest rate risk on positions not included in the trading book .....	55
15.	Remuneration Policy .....	55
15.1.	Decision making process/body .....	55
15.2.	Link between Pay and Performance .....	56
15.3.	Table 38: Remuneration of senior management and members of staff whose actions have a material impact on the risk profile of the institution.....	56
15.4.	Table 39: Analysis of remuneration by business area.....	57
16.	Table 40: Leverage .....	57

## I. Executive Summary

### 1.1 Introduction

This document comprises BLME plc's Pillar 3 disclosures on capital and risk management as at 31 December 2017 and has the following two principal purposes:

- to provide useful information on the capital and risk profile of the BLME Group; and
- to meet the regulatory disclosure requirements under the Capital Requirements Regulation (EU) No 575/2013

("CRR"), Part 8 – Disclosure by institutions and the rules of the Prudential Regulation Authority ("PRA") set out in the Public Disclosure section of the PRA Rulebook and as the PRA has otherwise directed.

The principal activities of Bank of London and The Middle East plc (the "Bank" or "BLME") are providing Sharia'a compliant financing facilities and solutions for corporate clients; treasury services to financial institutions, organisations and corporate clients; and wealth management financing, investment and advisory services to a wide spectrum of clients.

Further details on the scope of consolidation are provided in Section 3.8 of this document. Additional relevant information may be found in the 2017 BLME plc Annual Report and Accounts.

### 1.2 Table 1: Location of Pillar 3 disclosures within Annual Report and Pillar 3 Report

Pillar 3 disclosure topic	CRR Article	Annual Report location	Pillar 3 report location
Scope of disclosure requirements	431	Not mentioned	Section 3
Non-material, proprietary or confidential information	432	Not mentioned	Section 3.5
Frequency of disclosure	433	Not mentioned	Section 3.2
Means of disclosures	434	Not mentioned	Section 3.2
Risk management objectives and policies	435	Note 36	Section 7 Section 8
Scope of application	436	Note 1 & 2	Section 3
Own Funds	437	Note 33	Section 4
Capital requirements	438	Note 33	Section 5
Exposure to counterparty credit risk	439	Note 33	Section 9
Capital buffers	440	Note 33	Section 6
Indicators of global systemic importance	441	Not mentioned	Section 3.5
Credit risk adjustments	442	Note 14	Section 9.6
Unencumbered assets	443	Not mentioned	Section 11
Use of ECAIs	444	Note 33	Section 9.18 to 9.23
Exposure to market risk	445	Note 33	Section 13
Operational risk	446	Note 33	Section 14
Exposures in equities not included in the trading book	447	Not mentioned	Section 12
Exposure to profit rate risk on positions not included in the trading book	448	Not mentioned	Section 13
Exposure to securitisation positions	449	Not mentioned	Section 3.5
Remuneration policy	450	Note 13	Section 16
Leverage	451	Strategic Report	Section 17
Use of the IRB Approach to credit risk	452	Not mentioned	Section 3.5
Use of credit risk mitigation techniques	453	Note 33	Section 10

Use of the Advanced Measurement Approaches to operational risk	454	Not mentioned	Section 3.5
Use of Internal Market Risk Models	455	Note 33	Section 3.5

### 1.3 Summary of key metrics

At the end of 2016 BLME established a Wealth led strategy to deliver sustainable performance and create long-term value for our shareholders. The progress in implementing this strategy has had a positive impact on the Bank's financial performance as evidenced in a return to profit and a Balance Sheet that has stabilised at £1bn. These results have enhanced capital strength and the leverage ratio.

Full details of the financial position can be found within our Annual Report and Accounts 2017, while a summary of the changes in our key capital ratios are given in the following table.

### 1.4 Table 2: Key ratios

	31/12/2017 £m	31/12/2016 £m
Available capital		
Common Equity Tier 1 (CET 1)	216	216
Tier 1	216	216
Total regulatory capital resources	220	220
Risk-weighted assets	1,032	1,055
	%	%
Common Equity Tier 1 ratio (%)	20.95%	20.42%
Tier 1 ratio (%)	20.95%	20.42%
Total regulatory capital ratio	21.33%	20.81%
	£m/%	£m/%
Leverage ratio exposure measure	1,122	1,105
Leverage ratio	19.28%	19.55%
Liquidity coverage ratio (%)	403%	4,115%

## 2. Scope of the application and disclosure policy

### 2.1. Background

The Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRD) (together referred to as CRD IV) implement Basel III within the European Union and came into force on 1 January 2014. CRDIV, which is enforced in the UK, together with local implementing rules and guidance, by the Prudential Regulation Authority (PRA), has the objective to improve the banking sector's ability to absorb shocks arising from financial and/or economic stress, thus reducing the risk of spillover from the financial sector into the wider economy.

CRD IV also sets out disclosure requirements relevant to banks and building societies under CRR Part Eight. These are known as Pillar 3 disclosures because they complement the minimum capital requirements in Pillar 1 and the supervisory review and evaluation process in Pillar 2. The Pillar 3 disclosures are aimed at promoting market discipline by providing information on risk exposures and the management of those risks.

The Bank uses the standardised approach to calculating Pillar 1 capital requirements, using the capital risk weighting percentages set out under CRD IV.

### 2.2. Frequency

The Directors, having taken into account the size and complexity of the Bank's operations, believe that an annual disclosure is appropriate, and that these disclosures be made available on the Bank's website, [www.blme.com](http://www.blme.com). The frequency of disclosure will be reviewed should there be a material change in any approach used for the calculation of capital, business structure or regulatory requirements; BLME does not currently meet any of the indicators included within EBA Guidelines Title V – Considerations regarding the need to assess the disclosure of information more frequently than annually.

The capital position of BLME has remained consistently strong throughout 2017 and there have been no changes to the relevant characteristics of the Bank's business (such as scale of operations, range of activities, presence in different countries, involvement in different financial sectors, and participation in international financial markets and payment, settlement and clearing systems) to impact the position.

This document, in conjunction with the 31 December 2017 Annual Report and Accounts (available on the Bank's website), represents the Bank's annual public Pillar III disclosure for the financial year ended 31 December 2017.

### 2.3. Reporting

Capital is reported on a monthly basis within the Bank's management performance reporting packs. Specific analysis of capital by business stream is included within the packs as appropriate.

A range of Key Risk Indicators are routinely monitored by management to ensure that appropriate actions can be taken should triggers be breached.

### 2.4. Disclosure process and governance

BLME applies the Basel 3 capital framework for our risk exposures on the basis of the "Standardised Approach" for measuring credit risk and market risk and the "Basic Indicator Approach" for operational risk. For purposes of Article

431 CRR, we have adopted a formal risk disclosure policy aiming to support a conclusion that our risk disclosures are in compliance with the applicable legal, regulatory and accounting risk disclosure standards and are compiled based upon a set of internally defined principles and related processes. Senior representatives and subject matter experts from Finance and Risk assume responsibility for our risk disclosures and govern our respective risk disclosure processes. Based upon our assessment and verification we believe that our risk disclosures presented throughout this Pillar 3 report in conjunction with the Annual Report 2017 appropriately and comprehensively convey our overall risk profile and that no material disclosures have been omitted from this document.

**2.5. Table 3: Pillar 3 disclosure topics where disclosures are omitted due to reasons of there being no values to report; immaterial values; or confidentiality**

Pillar 3 disclosure topic	CRR Article	Management Comment
Indicators of global systemic importance	441	BLME is not identified as an institution of Global Systemic Importance
Exposure to securitization positions	449	BLME does not have exposures to securitisation positions and does not securitise any assets on the balance sheet
Use of the IRB Approach to credit risk	452	BLME calculates own funds requirements in accordance with the Standardised Approaches to credit risk
Use of the Advanced Measurement Approaches to operational Risk	454	BLME measures operational risk according to the Basic Indicator Approach
Use of Internal Market Risk Models	455	BLME calculates own funds requirements in accordance with the Standardised Approaches to Credit and Market risk and the Basic Indicator Approach to Operational Risk
Wrong way risk	439	BLME enters into very limited Sharia'a compliant trading book activities (primarily "Profit Rate Swap" and "FX" contracts) accordingly it has negligible exposure to wrong way risk which is considered an immaterial risk to the entity

**2.6. Location and verification**

These disclosures have been reviewed and approved by the Board and Executive Risk Committees on **20 March 2018**. The disclosures are not subject to external audit except where they are also included as accounting disclosure requirements in the Bank's Annual Report and Accounts.

**2.7. Declaration**

The Board of Directors is committed to a strong culture of risk management in order to protect the Bank's market reputation and its ongoing sustainability. It has therefore established governance and management structures, monitoring procedures and reporting for each type of risk that the Bank is exposed to. These risks are principally credit risk, market risk, liquidity risk, operational risk and conduct risk.

The responsibility for identifying and managing the principal risks ultimately rests with the Board of Directors. The Board has ultimate responsibility for setting the strategy, risk appetite and control framework.

The Board considers that, as at 31 December 2017, it had in place adequate systems and controls with regard to its risk profile and strategy and the credit, operational and prudential risks were within BLME's risk tolerances.

In accordance with Part VIII of the CRR and the Bank's Pillar III disclosure policy, the Bank is required to ensure that its external disclosures portray its risk profile comprehensively. The Directors have considered the adequacy of the Pillar III disclosures in relation to these requirements and are satisfied that they convey the risk profile of the Bank



comprehensively. The disclosures of risk management objectives and procedures within this Pillar III document are detailed further within the Risk Management Report of the Annual Report and Accounts.

**2.8. Table 4: Accounting and regulatory scopes of consolidation - Entities**

The differences between accounting and regulatory scopes of consolidation are briefly described below; full detail of the consolidation for accounting purposes is laid out in note **33** within the Annual Report and accounts:

Entity name	Method of accounting consolidation	Basis of accounting consolidation	Regulatory treatment of exposure				Description of the entity
			Consolidation		Risk weighted credit exposure due to no equity investment	Risk weighted temporary equity investment	
			Full	Proportional			
Bank of London and The Middle East plc	Full	Ownership of share capital	x				Credit Institution
BLME Holdings Employee Benefit Trust	Full		x				Employee benefit trust
Aspenway Limited Jersey	Full					x	The provision of Shariah Compliant real estate investment and financing arrangements
MKL Construction Equipment Finance Ltd	Proportional			x			Leasing company
Kalakane Transatlantic Investors II, Inc USA	Full	Pledge over shares and accounting treatment as Risks & rewards of ownership			x		Lease Administration Co
DMJ 2 LLC (USA)	Full				x		Lease Administration Co

The following dormant companies are consolidated for both accounting and regulatory purposes

BLME Asset Management Ltd

BLME Holdco Ltd

BLME Limited

BLME Umbrella Fund Management Sarl

Global Liquidity Solutions Ltd

Renaissance Property Finance Ltd

Full detail of the consolidation for accounting purposes is documented in note **33** within the Annual Report and Accounts. There are no current, or foreseen: material; practical; or legal impediments to the transfer of capital resources or the repayment of liabilities between consolidated entities. As of 31<sup>st</sup> December 2017, there was no capital shortfall at any of the companies included within the Bank's consolidation.

## 2.9. Table 5: Accounting and regulatory scopes of consolidation – Carrying values

The differences between accounting and regulatory scopes of consolidation and mapping of financial statements with regulatory risk categories:

	Carrying values within published financial statements	Carrying values under scope of regulatory consolidation	Carrying values of items £m				
			Subject to credit risk framework	Subject to counterparty credit risk framework	Subject to the securitisation framework	Subject to the market risk framework	Not subject to capital requirements or subject to decution from capital
<b>Assets</b>							
Cash and balances with banks	97	95	95				
Due from financial institutions	29	29	29				
Due from customers	9	9	9				
Investment securities	115	129	129				
Financing arrangements	568	556	556				
Finance lease receivables	171	171	171				
Operating lease assets	35	39	39				
Property and equipment	1	1	1				
Intangible assets	1	1					1
Other assets (inc. inventory)	5	25	25				
<b>Total assets</b>	<b>1,030</b>	<b>1,053</b>	<b>1,053</b>				<b>1</b>
<b>Liabilities</b>							
Due to financial institutions	514	514					514
Due to customers	277	277					277
Profit rate swaps	1	1					1
Other liabilities	11	11					11
<b>Total liabilities</b>	<b>803</b>	<b>803</b>					<b>803</b>

**2.10. Table 6: The main sources of differences between regulatory exposure amounts and carrying values in financial statements**

	Carrying values of items £m				
	Total	Items subject to:			
		Credit risk framework	Securitisation framework	Counterparty credit risk framework	Market risk framework
Asset carrying value amount under scope of regulatory consolidation	1,054	1,054			
Liabilities carrying value amount under regulatory scope of consolidation					
Total net amount under regulatory scope of consolidation	1,054	1,054			
Off-balance sheet amounts	120	120		2	
<i>Differences in valuations</i>					
<i>Differences due to different netting rules, other than those already included</i>					
<i>Differences due to consideration of provisions</i>					
<i>Differences due to prudential filters</i>					
<b>Exposure amounts considered for regulatory purposes</b>	<b>1,174</b>	<b>1,174</b>		<b>2</b>	

### 3. Own funds

#### 3.1. Total available capital

At 31<sup>st</sup> December 2017 and throughout the year, BLME complied with the capital requirements in force as set out by European and national legislation.

BLME has adopted the Standardised Approach to credit and market risk under the Directive; for operational risk BLME applies the Basic Indicator Approach.

All disclosures are on an end point basis as BLME has no grandfathered Additional Tier 1 or Tier 2 capital which would be subject to the transitional provisions.

#### 3.2. Reconciliation of statutory to regulatory capital

A table own funds disclosure information is given at appendix 1 to this document.

#### 3.3. Capital Instruments - main features and terms

A table detailing the main features and terms of the capital instruments issued by Bank of London and The Middle East plc and BLME Holdings plc is given at appendix 2 to this document.

#### 3.4. Table 7: Prudential filters and deductions

Description	£m
Adjustments to CET1 in accordance with CRR articles 32 - 35	
Cash flow hedge reserve	0
	0
Adjustments to CET1 in accordance with CRR articles 36; 56 & 66	
Losses for the current financial year	0
Direct, indirect and synthetic holdings of own CET1 instruments	0
Intangible assets	0
	0
Items not deducted in accordance with articles 47,48,56,66,& 79	
None	0
	0

#### 3.5. Restrictions applied to the calculations of own funds

There are no restrictions applied to the calculation of own funds.

#### 3.6. Calculation of capital ratios

The capital ratio calculations do not include any elements calculated on a basis other than that laid down within the CRR legislation.

#### 3.7. Transitional own funds disclosure

A table of transitional own funds disclosure information is given at appendix 3 to this document.

## 4. Capital requirements

### 4.1. Assessing the adequacy of internal capital to support current and future activities

In the first instance the Bank assesses the adequacy of its capital resources as part of its annual Budget and Business Planning process, where it looks at projected earnings, balance sheet growth and capital usage for the next 5 years. This capital requirement assessment is subsequently referenced to and qualified by the Bank's ICAAP. The ICAAP calculates BLME's internal (economic) capital for the following principal risk classes:-

- Credit risk
- Market risk (Trading Book and Banking Book)
- Liquidity risk
- Operational risk
- Conduct risk

The calculation of internal capital is the basis upon which the Bank proposes its Pillar II Individual Capital Guidance requirement. In undertaking the ICAAP, the Bank uses a number of economic risk methodologies and models that allow it to assess its internal capital requirements for all risk classes. The ICAAP is undertaken companywide and is coordinated by the Chief Risk Officer under the guidance of the Chief Executive Officer and it is reviewed and endorsed by EXCO before being submitted to BRC for further review and recommendation to the full Board. The latter is responsible for ensuring that the planned capital levels are sufficient to protect unsecured creditors from loss, having taken account of the Bank's risk appetite within the context of business strategy and plans, and having assessed the resilience of capital resources to extreme stress events and adverse scenario conditions. The most recent ICAAP also takes account of the Basel III changes in respect of capital adequacy, liquidity, leverage and trading book treatment.

On a more routine level, BLME reports its capital adequacy to the PRA on a quarterly basis. For internal management purposes it is calculated daily, and is used by Finance Department to present to EXCO the Bank's financial performance against budget. The Board reviews these financial and business performance indicators on a quarterly basis.

4.2. Table 8: Overview of Risk Weighted Assets (RWAs)

	£m		
	Risk weighted assets		Minimum capital requirements
	31/12/17	31/12/16	31/12/17
Credit risk (excluding counterparty credit risk) (CCR)	943	956	75
Of which standardised approach (SA)	943	956	75
Of which the foundation IRB (FIRB) approach			
Of which the advanced IRB (AIRB) approach			
Of which equity IRB under the simple risk-weighted approach or the IMA			
Counterparty credit risk	0	3	0
Of which mark to market	0	3	0
Of which original exposure			
Of which the standardised approach			
Of which internal model method (IMM)			
Of which risk exposure amount for contributions to the default fund of a CCP			
Settlement risk			
Market risk	1	8	0
Of which standardised approach	1	8	0
Operational risk	88	87	7
Of which basic indicator approach	88	87	7
Amounts below the thresholds for deduction (subject to 250% risk weight)			
<b>Total</b>	<b>1,032</b>	<b>1,054</b>	<b>83</b>

## 5. Regulatory capital buffers

### 5.1. Introduction

#### 5.1.1. Pillar 1

Under CRD IV, institutions are required to meet the following own funds requirements: CET1 ratio of 4.5%; Tier 1 ratio of 6% and a total capital ratio of 8%.

#### 5.1.2. Pillar 2

The Pillar 2 framework includes an Internal Capital Adequacy Assessment Process (ICAAP) carried out by firms to analyse and conclude on the additional amount of capital required, and the regulators review of that process, the Supervisory Review and Evaluation Process. Pillar 2A addresses risks to firms that are not adequately covered within Pillar 1. Pillar 2B addresses risks to which the firm may become exposed over a forward-looking planning horizon.

### 5.2. Capital buffers

#### 5.2.1. Capital conservation buffer

The capital conservation buffer is designed to ensure that institutions build up capital buffers outside of times of stress that can be drawn upon if required. The requirement is set as 1.25% @ 31<sup>st</sup> Dec 2017 (this will rise incrementally until fully implemented at 2.5% in 2019).

#### 5.2.2. Countercyclical capital buffer (CCyB)

The countercyclical capital buffer requires institutions to hold additional capital to reduce the build-up of systemic risk during a positive credit cycle. Institution's specific rates are calculated as the weighted average of the countercyclical capital buffers that apply in those jurisdictions where the relevant credit exposures exist. In the UK responsibility for setting the CCyB rests with the Financial Policy Committee, which has confirmed rates of 0% until 06/18; 0.5% from 06/18 – 11/18 and 1% from 11/18.

No further capital buffers are applicable to BLME.



5.3. Table 9: Geographical distribution of exposures

	£m										Own funds requirements	Countercyclical capital buffer rate
	General credit exposures		Trading book exposures		Securitisation exposures		Own funds requirements					
	Exposure value for		Sum of long and short positions of trading book exposures for SA	Value of trading book exposures for internal models	Exposure value for		of which: General credit exposures	of which: Trading book exposures	of which: Securitisation exposures	Total		
SA	IRB	SA			IRB							
Jurisdiction	SA	IRB			SA	IRB						
United Kingdom	833						63			63	0	0
Switzerland	1						0			0	0	0
Jersey	11						1			1	0	0
Bahrain	8						1			1	0	0
Abu Dhabi	1						0			0	0	0
Dubai	15						1			1	0	0
Kuwait	96						5			5	0	0
O UAE	3						0			0	0	0
Jordan	1						0			0	0	0
Qatar	14						1			1	0	0
Saudi Arabia	22						1			1	0	0
United States	36						1			1	0	0
Cayman Islands	6						1			1	0	0
Multilateral	71						0			0	0	0
<b>Total</b>	<b>1,122</b>						<b>75</b>			<b>75</b>	<b>0</b>	<b>0</b>

5.4. Table 10: Amount of institution-specific countercyclical capital buffer

	Total
Total risk exposure amount	0
Institution specific countercyclical capital buffer rate	0
Institution specific countercyclical capital buffer requirement	0

## 6. Risk management objectives and policies

### 6.1. Statement and declaration

The Board of Directors is committed to a strong culture of risk management in order to protect the Bank's market reputation and its ongoing sustainability. It has therefore established governance and management structures, monitoring procedures and reporting for each type of risk that the Bank is exposed to. These risks are principally credit risk, market risk, liquidity risk, operational risk and conduct risk.

The responsibility for identifying and managing the principal risks ultimately rests with the Board of Directors. The Board has ultimate responsibility for setting the strategy, risk appetite and control framework.

The Board considers that, as at 31 December 2017, it had in place adequate systems and controls with regard to its risk profile and strategy and the credit, operational and prudential risks were within BLME's risk tolerances.

No material transactions exist between the group, affiliates and related parties.

### 6.2. Structure and organisation of the risk management function

#### 6.2.1. Attribution of responsibilities: BLME Board & Board Committees

##### 6.2.1.1. BLME Board of Directors

The responsibility for the operating framework for risk governance rests with the Board of Directors. This extends to determining risk appetite in line with the Bank's strategy, establishing Board and executive committee structures to oversee risks, and ensuring that there is a clearly defined risk management structure with distinct roles and responsibilities that allow risks to be monitored, controlled and reported effectively. Risk governance is underpinned by ensuring that the Board and its committees are provided with transparent and risk sensitive reporting to facilitate their accountabilities and decision making. The Board and its committees have reviewed the Terms of Reference that govern: BLME's Board; Board committee; and executive committee structures, with a view to ensuring that the Bank operates under the best practices for corporate governance.

The Board is responsible for ensuring that an effective framework is in place to identify, monitor and report on the risks faced by BLME. At Board level BLME defines its risk philosophy using four main risk steering mechanisms:-

- A clear definition of Risk Appetite is set by Board Risk Committee and cascaded into operating procedures in relevant departments
- A risk categorisation that defines the governance of risk within BLME's committee structure. This provides a definition of the risk, the responsible committee and the regularity that the committees review each risk type. In addition, it includes an assessment of the materiality of each risk category, including the impact of any mitigating factors.
- A Stress Testing and Scenario Analysis Policy which defines the programme for the stress testing for the major categories of risk.
- Sector based Risk Limits and Commercial Guidelines that define credit risk appetite in terms of deal size, client rating, tenor, country risk and collateral considerations.

#### 6.2.1.2. Board Risk Committee (BRC)

BRC is a non-executive committee that is responsible for the oversight of the risk profile of the Bank and for providing guidance, advice and recommendations to the Board on credit, market, liquidity, direct investment and operational risks with a view to re-enforcing a culture that encourages good stewardship of risk. Within this mandate it reviews risk levels in consideration of the Group’s overall risk appetite, market conditions and business strategy. It also overviews BLME’s Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) and assesses the adequacy of stress testing and risk policy.

Ultimate responsibility for risk rests with the Board which, with advice and recommendations from BRC, approves the risk appetite for each major class of risk in line with BLME’s business model and strategic priorities and also approves the annual ICAAP and ILAAP. Board Credit Committee is a sub-committee of BRC established to review and opine on decisions made by the Counterparty Credit Risk Committee (CCRC) that meet the escalation criteria.

The management of risk is delegated to the Chief Executive Officer who in turn delegates the day-to-day management of risk to the Executive Committee and, in particular, to the Executive Risk Committee which oversees the three sub-committees of the Bank responsible for risk oversight (being ALCO, CCRC and ERC). The day-to-day independent oversight of risk is performed by the Bank’s Risk Department. This process is supported by the finance department’s internal control role in monitoring adherence to risk limits, management action triggers and regulatory limits.

#### 6.2.1.3. Board Audit Committee

This is a non-executive committee that meets at least quarterly and reports to the Board. It is responsible for reviewing any reports from management, the internal auditor and the external auditor regarding the accounts, the internal control systems and processes implemented throughout the Bank.

Board Audit Committee also provides guidance and recommendations to the Board on all matters affecting the accuracy and appropriateness of the Bank’s Annual Report and Accounts, including the qualifications and role of its auditors, and the performance of the internal audit function. It works with the management and employees of the Bank, the auditors and other professional advisors to provide assurance that all statutory and regulatory reporting is submitted in an accurate and timely fashion. It also receives regular reports from Compliance, and the Audit Committee Chairman is responsible for apprising the Board of any relevant issues raised by Compliance.

#### 6.2.1.4. Board Remuneration Committee (RemCo)

As a non-executive committee that reports to the Board, this body ensures that employee, management and executive compensation is appropriately aligned to business and individual performance, and is consistent with shareholder interests. It performs these duties within a framework that takes account prevailing market conditions, best market practice and regulatory compensation guidelines. RemCo has appointed Mercer as an independent professional advisor.

#### 6.2.1.5. Board Nominations Committee (NomCo)

This non-executive committee is responsible for matters relating to the composition of the Board, including the appointment of new Directors, and making recommendations to the Board as appropriate. NomCo identifies qualified candidates to be Directors, through a robust and prudent process, with the use of external consultants as necessary.

#### 6.2.1.6. Table 11: Board and committee meetings 2017

Committee	Board	BRC	Audit	RemCo	NomCo
-----------	-------	-----	-------	-------	-------

No of meetings	7	9	7	6	4
----------------	---	---	---	---	---

## 6.2.2. Attribution of responsibilities: Executive Committees

### 6.2.2.1. The Executive Committee (EXCO)

The CEO is responsible for the executive management of the Bank. He is assisted by EXCO which ensures that all BLME internal committees are working effectively and is supported by the CFO. EXCO is additionally responsible for the strategic, legal, reputational, regulatory and business affairs of the Bank, including its operational and financial performance. The CEO reports directly to the Board on behalf of EXCO.

### 6.2.2.2. Executive Risk Committee (ERC)

ERC is responsible for communicating the risk appetite, overseeing the design and implementation of the risk management framework (including setting risk limits), overseeing the measurement and monitoring of market risks across all asset classes and risk types in the Bank's trading and banking book businesses, overseeing the preparation and reporting of the ICAAP, ILAAP and Recovery and Resolution Plan (RRP) to BRC and ensuring that management information is effective to support risk modelling, stress testing and the associated decision making.

### 6.2.2.3. Assets and Liabilities Committee (ALCO)

ALCO is responsible for managing the balance sheet of the Bank, and the optimisation of the asset/liability structure and capital allocation. Within this, it is responsible for the operational and structural liquidity of the Bank, and its adherence to regulatory limits and prudential internal guidelines. It has responsibility for ensuring the adequacy of the Bank's policies and processes covering stress testing and managing the Banks investments.

### 6.2.2.4. Counterparty Credit Risk Committee (CCRC)

CCRC is responsible for the approval of individual obligor risks using the Commercial Guidelines, as approved by ERC, that govern the credit risk appetite of the Bank. It also oversees country and sector risks and undertakes periodic reviews and assessments of portfolio, collateral, residual value and concentration risks. CCRC escalates matters to BCC for review where they are outside of stated risk appetite and/or meet other escalation criteria. This committee reports directly to ERC.

### 6.2.2.5. Wealth Management Investment Committee (WMIC)

WMIC provides input and oversight of the investment activities within BLME's wealth management business. These responsibilities, which take account of the Bank's fiduciary responsibility to third party clients, include investment strategy and risk; fund management; trade execution; broker and counterparty risk; controls and regulatory compliance; and product development and marketing. This committee reports to ERC.

### 6.2.2.6. Change Implementation Committee (CIC)

CIC is responsible for overseeing all bank wide strategic projects and new product development (once approved by the Product Committee) and ensuring that they are aligned with BLME's Board approved business strategy. It also oversees the allocation and prioritisation of resources and ensures that products and projects are in accordance with Sharia'a. CIC reports to EXCO.

### 6.2.2.7. Product Committee (PC)

Proposals for new products or material changes to existing products supported by EXCO are delegated to the PC for processing. The purpose of PC is to support product proposal sponsors to launch new products, and execute material

changes to existing products. The committee is also responsible for undertaking periodic risk-based reviews of BLME's existing products, as recorded on the Bank's Product Register. In particular the committee will balance the commercial aspirations of BLME with its regulatory responsibilities, risk management obligations, and obligations to its clients and the markets within which it operates.

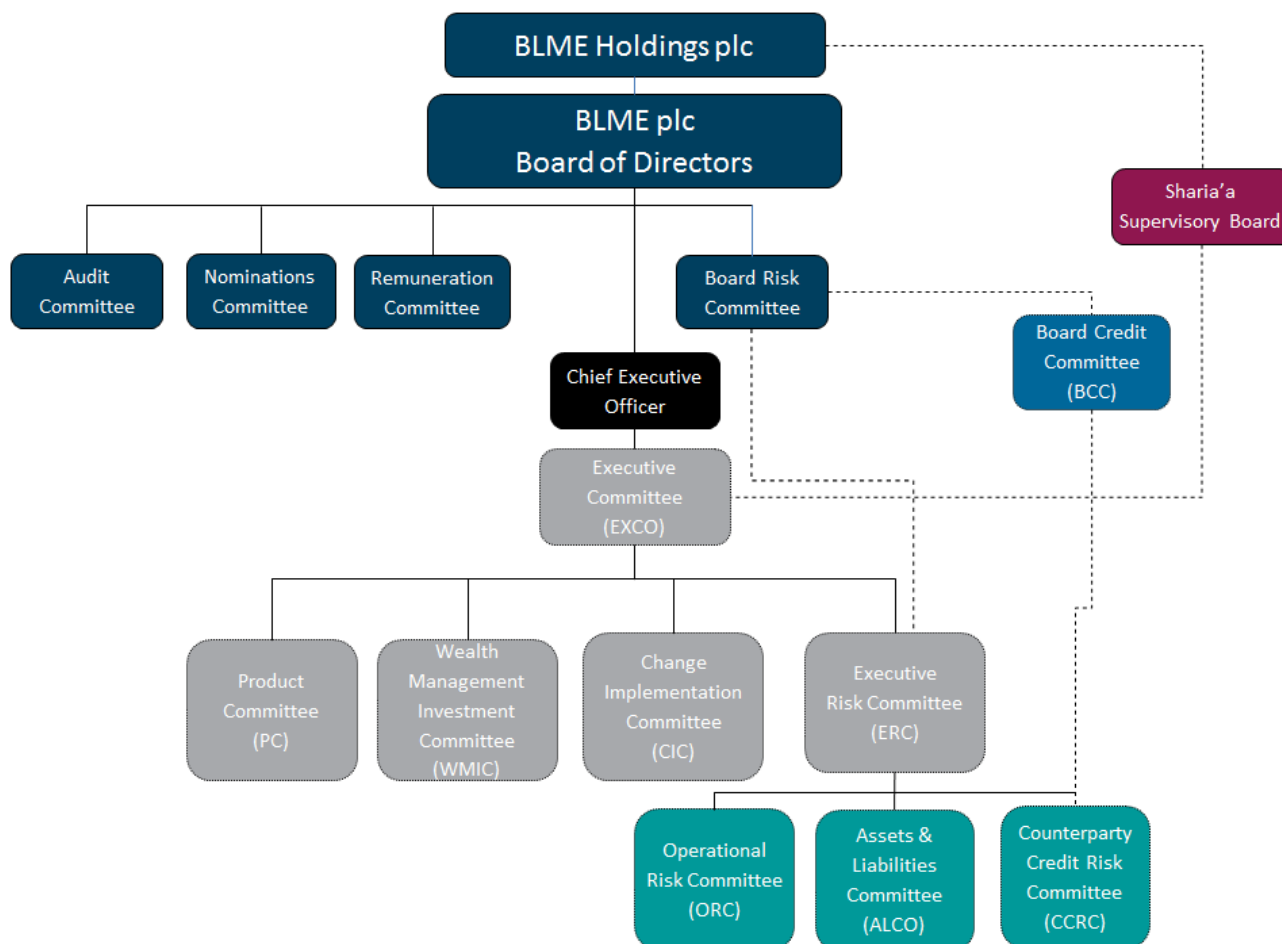
#### 6.2.2.8. Operational Risk Committee (ORC)

**The purpose of the Committee is to assist EXCO (via Executive Risk Committee) in fulfilling its oversight of responsibilities related to operational aspects of resource and cost allocations, alignment to transformation strategy, notable upcoming events and key challenges. The Committee also serves as the oversight body responsible for ensuring active engagement between departmental heads on operational risk issues affecting multiple areas of the Bank.**

#### 6.2.2.9. Sharia'a Supervisory Board (SSB)

This independent body is responsible for ensuring that BLME's activities are in compliance with the principles of the Sharia'a. In this regard the Sharia'a Supervisory Board reviews relevant template documents and new deal structures and provides advice and guidance upon request from BLME's internal Sharia'a Compliance function. On an annual basis it conducts a Sharia'a audit of BLME's activities and reports to the Shareholders as part of the annual report and accounts. Sharia'a compliance is the responsibility of all employees of BLME and is managed by the Sharia'a Compliance function that forms part of BLME's Legal Department.

### 6.2.3. Chart 1: Governance structure



Note: The Group operates with a dual board structure with mirror image Audit, Nominations, Remuneration and Board Risk Committees for both BLME Holdings plc and Bank of London and The Middle East plc ("BLME plc").

### 6.2.4. Structure of key functions

#### 6.2.4.1. Risk management

The Risk Management Department is an independent function. It is managed by the Chief Risk Officer and reports to the Chief Executive Officer with a reporting line also to the Chair of the Board Risk Committee. The department is divided into two areas:-

- Counterparty Credit Risk Management is responsible for the approval and review of individual obligor risks, the development of credit policy and the oversight of portfolio, country, sector, residual value and collateral risk concentrations.
- Risk Management Department covers capital risk, market risk, liquidity risk and operational risk and also manages the Bank's Risk Management Framework (RMF).

The New Product Approval process involves the assessment of the risks inherent in a new product and how these risks can be managed and mitigated. It covers the review and approval of all relevant risks, including legal, regulatory and Sharia'a aspects. The approval process involves and requires a formal sign off by all relevant back office and front office areas, including the Risk Management Department.

The Risk Management Department supports ALCO in the management of the Bank's regulatory and economic capital.

#### 6.2.4.2. Risk categorisation

BLME's Pillar 1 risks cover:

- Credit Risk, including Counterparty Risk
- Market Risk in the Trading Book
- Operational Risk

In addition, within its regular ICAAP and ILAAP processes, BLME assesses a number of Business and Consequential Risks as part of determining its Pillar II capital requirement. The assessment of Business Risk includes Market Risk in the Banking Book, Concentration Risk and Liquidity Risk, whereas Consequential Risks cover Insurance Risk, Pension Obligation Risk, Residual Risk, Securitisation Risk and Group Risk. The risk evaluation also includes an impact analysis of a series of adverse market, political, regulatory, legal and reputational factors on the Bank's business model.

#### 6.2.4.3. Compliance

The Compliance Department, which reports to the CEO, is an independent function. Its role is to identify, manage and mitigate the risk of legal or regulatory sanctions and financial or reputational damage which could arise as a result of the Bank and/or its employees failing to comply with applicable rules, regulations, codes of conduct, and standards of good practice.

It seeks to make a significant contribution to the generation of business by promoting the culture and practice of compliance within the spirit of and by the letter of regulatory, ethical and Sharia'a requirements and standards. To fulfil these duties Compliance:

- is independent from the business activities;
- has direct access to senior management;
- has direct access to any director, officer or employee;
- has access to all relevant data and records; and
- will intervene in any transaction where it has reason to believe that a breach of legal, regulatory or Sharia'a requirements, or internal policies and standards, has occurred or may occur.
- is represented on committees which are key to the Compliance governance framework e.g. Product Committee.

The Compliance function produces regular reports for the Executive Committee and the Audit Committee.

#### 6.2.4.4. Financial Crime

The Financial Crime unit is in place to ensure that the bank and its employees observe regulatory requirements and do not have any involvement in:

- receiving proceeds of crime;
- money laundering;
- fraud;
- bribery and corruption;
- tax evasion;
- cyber-crime;
- financing of terrorism.

#### 6.2.4.5. Internal Audit

The Internal Audit function is outsourced to PricewaterhouseCoopers (PwC) who report directly to the Bank's Audit Committee. Under the oversight of the Audit Committee, PwC conduct a risk assessed programme of internal audits, assessments of audit findings and actions taken, and on a quarterly basis report key issues to the Audit Committee. BLME's nominated Head of Internal Audit assists the Audit Committee in managing the outsourced Internal Audit function by facilitating the internal coordination of resources and communication of the Internal Audit plan.

#### 6.2.5. Liquidity Risk

Liquidity risk is the risk that the Bank, even if it has sufficient capital, does not have sufficient cash to meet its obligations as they fall due.

##### 6.2.5.1. Strategies and processes in the management of the liquidity risk

Liquidity planning and strategy are evaluated as part of the overall annual budget process, within which detailed balance sheet and liquidity planning is undertaken for each business area. It is further guided by the annual ILAAP. The latter lays out the Bank's liability gathering strategy, its internal prudential liquidity ratios and targets, and the stress testing results that underpin its Individual Liquidity Guidance and the resultant Liquidity Contingency Plan.

Due to the importance of the maintenance of adequate liquidity for the prudent management of the Bank, the Board, represented by the Board Risk Committee ("BRC"), is significantly involved in the strategy and policy for the measurement, monitoring and management of liquidity risk, which is subject to review and updates on at least an annual basis. The Bank's Liquidity Risk Management Framework and Funds Transfer Pricing Policy are appendices to this ILAAP document.

Following review by ALCO, ERC and BRC approves:

- Risk Appetite;
- The strategies, policies, processes and systems relating to the management of liquidity risk for BLME (including the Liquidity Risk Management Framework);
- The Liquidity Contingency Plan;
- The ILAAP.

Additionally, the Board reviews regularly:

- Liquidity risk items submitted by the Chairman of the BRC;
- The Bank's funding strategy as updated from time to time (not less frequently than annually);
- The Bank's CFP; and
- The liquidity stress-testing methodology and scenarios

##### 6.2.5.2. Structure and organisation of the liquidity risk management function

Liquidity risk is managed by the Treasury desk which in conjunction with Finance Department and Risk Management ensures that BLME is compliant on an intra-day basis with its regulatory liquidity ratios.

##### 6.2.5.3. Scope and nature of liquidity risk reporting and measurement systems

Daily reports are circulated to Senior Management showing BLME's actual and projected liquidity profile, and confirmation that BLME is compliant with both its regulatory and internal liquidity limits. This assessment additionally takes account of the Bank's secondary market assets, which could be sold in extreme circumstances to provide emergency liquidity.



ALCO reviews these liquidity measures and ratios on a monthly basis. These ratios also link into the Stress Testing and Scenario Analysis Policy, particularly the ability of BLME to withstand and adapt to an extreme liquidity squeeze. Detailed liquidity reports and assessments are provided to ERC and BRC on a quarterly basis.

#### 6.2.5.4. Policies for hedging and mitigating liquidity risk

The KRI and the respective limits are set with regard to the most material risks that BLME faces within each principal risk. For Liquidity and Funding Risk these are aligned to the key risk drivers as outlined in section 5.6 of the ILAAP document. The key funding vulnerabilities exist due to the relatively small set of funding options available to an Islamic Finance institution. The KRI therefore focus on the relative stickiness of these deposits as BLME uses the term nature of its deposits as a key risk mitigation to Liquidity and funding risks, with KRIs for each of the main sources of funding for BLME, in addition to the continuous monitoring of the key stress scenario results.

#### 6.2.5.5. Adequacy of liquidity risk management arrangements

The Board considers that, as at 31 December 2017, it had in place adequate systems and controls with regard to its liquidity risk profile and strategy and that the prudential risks were within BLME's risk tolerances.

#### 6.2.5.6. Risk profile statement

BLME's liquidity risk profile includes a determination of whether certain potential sources of liquidity risk are considered to be of Low, Medium or High relevance and importance to the Bank. For those risks assessed as Medium or High), the assessment also contains an intuitive measure of the risk, and gives the 'normal' position or range of that measure, as well as our consideration of what would be the stressed position or range; this value naturally establishes an Early Warning Signal (EWS), and finally our limit, i.e. the most adverse level we will foreseeably tolerate.

#### 6.2.5.7. Table 12:LCR Metrics

The following table includes LCR ratios as reported at the end of each calendar quarter of 2017

		31/03/2017	30/06/2017	30/09/2017	31/12/2017
21	Liquidity buffer (£m)	98.2	107.9	107.4	106.3
22	Total net cash outflows (£m)	5.9	8.3	20.2	26.3
23	Liquidity coverage ratio	1,649%	1,289%	531.3%	402.6%

#### 6.2.5.8. LCR qualitative information

Management remains cognisant of the high degree to which the Bank continues to hold deposits from two Kuwaiti government entities who are long-standing shareholders in BLME. In recognition of this depositor concentration risk the Bank has successfully undertaken to reduce this concentration from 75% in 2016 to 59% at 31<sup>st</sup> December 2017. BLME will continue to diversify its depositor base through a combination of increased retail, fixed term and notice accounts, as well as gaining a wider range of wholesale interbank counterparties.

Derivative exposures and potential collateral calls are considered low risk due to the small number of hedging derivative contracts employed at 31<sup>st</sup> December 2017. In future years with a larger balance sheet, and in an environment where market interest rates are expected to normalise some fixed to floating rate swaps may be undertaken. In such circumstances collateralised support deeds will be used with full two-way margin obligations. In any case these risks are still expected to remain extremely small.

Currency mismatch in the LCR. There is no regulatory requirement for the Bank to meet LCR on a material currency basis. It should of course be noted that due to the paucity of suitable Sharia'a compliant sterling denominated HQLA

that in concert with a significant proportion of our liabilities being denominated in USD so too must be our HQLA, where the AAA rated issuer Islamic Development Bank is the main constituent of our HQLA portfolio.

Treasury is the sole business unit within BLME providing the management of liquidity and market risk. Real-time access to pipeline funding requirements and the close proximity of asset generating areas to the Treasury ensures a regular and active dialogue between those sourcing liquidity and those utilising it is maintained at all times.

6.2.5.9. Table 13: Business and consequential risks

The management of Business and Consequential Risks is formally and principally undertaken within the ICAAP. On a more regular basis the following other risks are managed through the BLME committee and governance structures:-

Risk	Board Committee	Executive/Sub Committee
Liquidity	Risk	ERC/ALCO
Market		ERC
Credit		BCC/ERC/CCRC
Operational		ERC/ORC
Financial Crime	Audit	EXCO
Conduct Risks	Board Committee	Executive/Sub Committee
Sharia'a compliance	Board	EXCO
Reputational risk		
All other conduct risks	Audit	

6.2.5.10. Changes of the heads of internal control, risk management, compliance and internal audit

In October 2017 Mr Tim Wilson was appointed Chief Compliance Officer

**6.3. The scope and nature of risk reporting and measurement systems**

The Risk Management Framework lays out systematic processes to identify, evaluate, mitigate, report, and manage risk:

- Risk Identification - Ensure there is a clear definition of each risk entered into by the Bank with an identified Risk Owner;
- Risk Assessment - Agree and implement appropriate, effective risk measurement and reporting standards for each identified risk. Set metrics together with reporting monitoring controls, processes and standards;
- Risk Mitigation - Establish key control processes and practices, including limit structures, impairment allowance criteria and reporting requirements. Ensure all frameworks and policies are regularly reviewed and kept relevant and up to date;
- Execution & Monitoring - The Second Line of Defence (2LoD) is responsible for monitoring the operation of the controls and adherence to risk direction and limits;
- Manage and Challenge - Review and challenge all aspects of the Bank's risk profile.
- The roles of each line of defence.

**6.4. Risk management strategies**

Risk strategies connect the Board's 5 year plan and risk appetite with practical and detailed strategies, controls and limits to ensure that risk appetite is not compromised. The strategies focus on how risks are managed within the Board appetite for Risk and set out:-

- Actions being taken to manage the risk considering both inherent risk and Board Risk Appetite
- Metrics used to measure risk
- Measurements used to judge success of actions taken
- Risks and challenges to delivering strategy

**6.5. Policies for hedging and mitigating risk, and the strategies and processes for monitoring the continuing effectiveness of hedges and mitigants**

The Bank has two transactions that have associated guarantees that are utilised as credit mitigation for regulatory capital purposes, the effect of which, in the context of its total assets, is not considered to be material to BLME's capital requirement. The bank is in receipt of further guarantees that are not recognised for regulatory credit risk mitigation under CRDIV due to the small size of the transactions involved.

The bank benefits from no other forms of credit risk mitigation for regulatory capital purposes.

## 7. Governance Arrangements

### 7.1. Table 14: External directorships

The number of external directorships and partnerships held by the Executive and Non-Executive Directors who served on the Board as at 31 December 2017 are detailed below.

Name	Position	Number of Directorships or partnerships
Adel Abdul Wahab Al-Majed	Chairman	1
Sheikh Abdullah Jaber Al-Ahmed Al-Sabah	Vice Chairman	2
Giles Cunningham	C.E.O.	0
Chris Power	C.F.O.	0
Jabra Ghandour	N.E.D.	1
Neil Holden	N.E.D.	3
Calum Thomson	N.E.D.	7
David Williams	N.E.D.	1
Michael Williams	N.E.D.	2

The number of directorships shown excludes the Company and its subsidiaries and counts external directorships held within the same group of companies as a single directorship. Directorships of non-commercial organisations and advisory positions are excluded.

### 7.2. Recruitment of directors

#### Appointment of Executive Directors

A new Executive Director would be recruited on terms which are in accordance with the Remuneration Policy at that time. The Remuneration Policy balances the need to have appropriate remuneration levels with the ability to attract high-performing individuals to the organisation. In setting the remuneration package for a new Executive director, the Board Remuneration Committee will take into account market levels, the individual's knowledge and experience.

#### Appointment of Non-Executive Directors

A new Non-Executive Director would be recruited on terms in accordance with the approved Non-Executive Directors' Remuneration Policy at that time. The Board has delegated specific powers and authority to the Nominations Committee to lead the appointment process for Board vacancies. It is also responsible for keeping the size, structure and composition of the Board under regular review, and for making recommendations to the Board for any changes necessary. The Nomination Committee also formulates succession plans for the Chairman and the Non-Executive Directors.

Before an appointment is made by the Board, the Nomination Committee evaluates the balance of skills, knowledge and experience on the Board and, in the light of this evaluation, prepares a description of the role and capabilities required for a particular appointment. In identifying suitable candidates, the Nominations Committee will:

- use open advertising or the services of external advisers to facilitate the search;
- consider candidates from a wide range of backgrounds; and
- consider candidates on merit and against objective criteria, including reference to the Financial Conduct Authority ("FCA") and PRA's "fit and proper" test and the competence and capability criteria set out as

part of their approach to approving individuals. Care is also taken to ensure appointees have enough time available to devote to the position on an ongoing basis.

Responsibility for determining the individual remuneration and benefits package of each of the Group's Executive Directors and the Chairman lies with the Remuneration Committee. The remuneration of Non-Executive Directors is set by the Board. No Director or senior manager is involved in any decisions as to their own remuneration.

### **7.3. Diversity of the board**

The Group is committed to diversity and ensuring that all employees are offered equal opportunities throughout their career. Further, the Group ensures that employees are not discriminated against, directly or indirectly, on the basis of age, ethnic or national origin, religion or beliefs, sexual orientation, gender, marital status or disability. This commitment applies equally to members of the Board. The Board strongly supports the principle of boardroom diversity, of which gender is one aspect. However, the Board does not have a measurable target for gender representation or any other diversity element on the Board. The Bank wishes to maintain a balance on the Board and all Board appointments are made on merit, in the context of the skills, experience, independence and knowledge.

## 8. Credit risk

### 8.1. Operating limits

Credit risk is the principal risk to BLME. It is reported to the PRA for capital adequacy purposes using the Standardised Approach. Credit risk is the potential for loss caused by a client or counterparty failing to meet its obligations on the date that they become due. This includes obligations under guarantees and letters of credit, as well as pre-settlement exposures under Islamic derivative contracts. Credit risks are managed by the Credit Risk Management Department which reports exposures to ERC and BRC on a quarterly basis by sector, region, country, rating and asset type. Large and concentrated exposures are also reported.

BLME's principal credit risks relate to Commercial Finance and Wealth Management financing activities, and its Money Market activities. By comparison, the Bank's limited foreign exchange activities give rise to relatively small amounts of settlement risk. In addition, BLME incurs some amount of pre-settlement risk as a result of undertaking Profit Rate Swaps to hedge fixed rate exposures and FX contracts for client and funding purposes. Credit limit structures exist for all of the afore-mentioned risks, and these are monitored on a regular basis by Credit Risk Management Department.

Credit risk limits are guided by the Risk Limits and Guidelines within the Bank's Risk Management Framework and specifically the Credit Risk Management Policy. These align strategic priorities with the risk appetite of the Bank such that a suitable level of portfolio diversification is achieved. Risk Limits and Commercial Guidelines also provide guidance on counterparty and collateral quality, industries, transaction criteria as well as pricing in line with the Bank's risk appetite.

The Bank also monitors its portfolio in terms of industry, collateral type and country concentration, as well as residual value risk on Leases.

Credit ratings are determined by a combination of the BLME Internal Rating Methodology and a validation of major ECAI (External Credit Assessment Institution) ratings, such as Moody's and Fitch, where such ratings exist. Where ECAI ratings are used and more than one such rating exists, the more conservative rating is adopted. This rating validation takes into account the transactional and collateral attributes of the credit proposal. Non-rated obligors are assessed using the BLME Internal Rating Methodology and approved at CCRC prior to commitment.

BLME's policy is to review all limits on at least an annual basis. BLME underpins its credit risk appetite by applying high levels of due diligence and rigorous adherence to Know Your Customers best market practice at the origination stage of new business. It also undertakes ongoing active risk management to keep abreast of developments within an obligor's business as well as the impact of any wider market events.

As an additional risk discipline, the Bank's Stress Testing and Scenario Analysis Policy requires at least semi-annual credit risk stress tests to be undertaken, and sets limits to measure the ability of BLME's capital resources to withstand a series of extreme credit shocks covering both portfolio and concentration risks. The latter are presented to the ERC and BRC for monthly review as part of regular assessment of portfolio and collateral risks via the Bank's Key Risk Indicator reporting

#### 8.1.1. Residual value risk

Whilst not necessarily being Credit Risk related from a technical interpretation point of view, Residual value risk has been identified within the Credit Risk Capital component.

BLME carries residual value risk through its leasing activity. This risk is on the residual value of the underlying assets on Leases. BLME uses independent professional valuation agents to advise on the residual value of equipment and monitors the development of these values through the life of the leases. As part of its residual value management process, the portfolio of assets where BLME is potentially exposed to a fall in residual value is also monitored for concentrations in particular types of asset. Stress tests of residual value risk are also performed every six months. Overall, BLME takes a conservative stance to residual value risk, taking into consideration asset type, length of lease and the secondary market for equipment.

## **8.2. Policies relating to risk mitigant assessments concerning counterparty risk**

The Credit Risk Policy sets out principles and functional responsibilities in relation to the management of credit risk incurred at the Bank of London and The Middle East plc (“BLME” or “the Bank”).

This policy, which is owned by the Head of Credit, applies to all BLME employees, temporary staff, contractors, and third parties as related to the authorised use of BLME information, customer/client information and information covered under Non-Disclosure Agreements (NDAs).

The policy is part of the Bank’s Risk Management Framework, which also includes the Bank’s Risk Appetite Statement and underlying departmental procedures. The Credit Risk Policy (“CRP”) is a key component that underpins the Bank’s Risk Management Framework.

The purpose of the CRP is to provide policy guidance as to how to manage identified Credit risks through the following:

- Ensuring effective governance, approval and management of credit risk at the Bank within the risk appetite delegated by the Board.
- Developing policies relating to credit risk management and risk control that are aligned with and supportive of the business strategy.
- Enforcing appropriate collateral and risk mitigation techniques in the assessment, approval and on-going management of credit risks.
- Promoting the objective and consistent identification, measurement, reporting and control of all material credit risks within the Bank’s businesses.
- Emphasising the imperative for compliance with all applicable laws and regulations within each of the countries where the Bank operates .
- Achieving maximum efficiency in the management and planning of both regulatory and economic capital in relation to credit risk ).
- Defining such roles and delegate such responsibilities as required in achieving these objectives.
- Highlighting potential Sharia’a Board requirements, through the Credit process.
- Reflecting the Risk Appetite and Strategy of the Board.

This policy is subject to all the laws, rules and regulations that BLME is governed by.

### 8.3. Policies relating to wrong way risk exposures

Wrong way risk is defined as the risk that occurs when the exposure to a counterparty increases at the same time as that counterparty's credit worthiness decreases. As BLME primarily enters into profit rate basis and foreign exchange contracts it has very little exposure to wrong way risk which is considered an immaterial risk to the entity.

#### 8.3.1. Table 15: PRS & FX contract exposure

	£m		
	Gross positive fair value	Net derivative credit exposure	Risk weighted exposure
Profit rate contracts			
Interbank	0	0	0
Other	0	0	0
Foreign exchange contracts			
Interbank	1	1	0
Other	0	0	0
<b>Total</b>	<b>1</b>	<b>1</b>	<b>0</b>

**Net** derivatives credit exposure is the credit exposure on derivatives transactions after considering both the benefits from legally enforceable netting agreements and collateral arrangements; BLME currently benefits from no such arrangements.

### 8.4. Downgrade of own credit rating

BLME has no External Credit Assessment Institution rating.

### 8.5. Past due and impaired transactions

The CCRC meets on a monthly basis to assess the performance of the credit portfolio. This assessment determines whether there is a need to reverse any accrued earnings; add any credit assets to the Credit Watch List; or establish specific impairment provisions. Any recommendations for credit provisions or write-offs are reported to CCRC and subsequently to the Audit Committee before being presented to the Board for final approval. In order to determine any requirement for a collective provision an industry standard modelling approach is used which utilises probability of defaults, loss given default and emergence periods.

- A credit asset is considered to be past due where repayment of either profit or principal is 90 days overdue and where Management is not aware of any specific event that might mitigate the impact of the non-payment
- A credit asset is deemed to be impaired when repayment is more than 90 days in arrears, where collateral rights have been exercised or where Management considers the full and eventual repayment to the Bank to be at risk



### 8.6. Specific, Collective and general credit risk adjustments

The Bank has an established Credit Impairment and Non-Accrual process to monitor impairment events that could lead to losses in its asset portfolio. This process covers specific loss events for individual exposures, as well as events that relate to collective losses on groups of homogenous assets with common credit characteristics that have yet to be identified and assessed individually for impairment. The Bank writes off a balance and any related provisions for impairment when the CCRC determines that the balance is uncollectable. This determination is reached after considering information such as the occurrence of significant changes in the counterparty's financial position such that the borrower's obligation can no longer be serviced, or that proceeds from collateral will not be sufficient to pay back the entire exposure. The provision is recommended to the CCRC by the relevant Business Unit/Department before being referred to the Audit Committee and the Board for ultimate approval. For the year ending 31 December 2017 BLME considered it prudent to take impairment charges totalling **£8.2m** which was offset by recoveries and releases of **£11.5m**.

### 8.7. Table 16: Performing and non-performing exposure analysis

	£m											
	Gross carrying values of performing and non-performing exposures						Accumulated impairment and provisions and negative fair value adjustments due to credit risk				Collaterals and financial guarantees received	
		Of which performing but past due > 30 days and < = 90 days	Of which performing forborne	Of which non-performing			On performing exposures		On non-performing exposures		On non-performing exposures	Of which forborne exposures
				Of which defaulted	Of which impaired	Of which forborne		Of which forborne		Of which forborne		
Debt Securities	116											
Financing arrangements	937	35	36	18	18	18	18	4		7	7	
Off balance sheet exposures	119											
Derivatives & LST	2											

**8.8. Table 17: Total and average net amount of exposures**

The total amount of exposures after accounting offsets and without taking into account the effects of credit risk mitigation, and the average amount of the exposures over the period broken down by different types of exposure classes:

	£m	
	Net value of exposures at the end of the period	Average net exposures over the period
Central governments or central banks	41	38
Regional governments or local authorities		
Public sector entities		
Multilateral development banks	71	69
International organisations		
Institutions	10	12
Corporates	662	617
Retail		
Secured by mortgages on immovable property	7	3
Exposures in default	20	22
Items associated with particularly high risk	198	234
Covered bonds		
Claims on institutes and corporates with a short term credit assessment	112	136
Collective investments undertakings		
Equity exposures	11*	9
Other exposures	41	37
<b>Total</b>	<b>1,174</b>	<b>1,177</b>

\* Aspenway Limited Jersey (see table 4)

**8.9. Table 18: Breakdown of net exposure amounts by geographical classification and exposure class**

The geographic distribution of the exposures, broken down in significant areas by material exposure classes

	£m					<b>Total</b>
	UK	Other Europe	Middle East	USA	Other countries	
Central governments or central banks	21		20			<b>41</b>
Regional governments or local authorities						
Public sector entities						
Multilateral development banks					71*	<b>71</b>
International organisations						
Institutions	10					<b>10</b>
Corporates	532	1	128	2		<b>662</b>
Retail						
Secured by mortgages on immovable property	3		5			<b>8</b>
Exposures in default	4		10		6	<b>20</b>
Items associated with particularly high risk	198					<b>198</b>
Covered bonds						
Claims on institutes and corporates with a short term credit assessment	73		5	34		<b>112</b>
Collective investments undertakings						
Equity exposures		11				<b>11</b>
Other exposures	41					<b>41</b>
<b>Total</b>	<b>881</b>	<b>12</b>	<b>168</b>	<b>36</b>	<b>77</b>	<b>1,174</b>

\*Exposure to Islamic Development Bank a Multilateral development bank hosted in Saudi Arabia

**8.10. Table 19: Breakdown of net exposure amounts by industrial classification and exposure class**

The distribution of the exposures by industry type, broken down by exposure classes

	£m																				
	Agriculture, forestry and fishing	Mining and quarrying	Manufacturing	Electricity, gas, steam and air conditioning supply	Water supply	Construction	Wholesale and retail trade	Transport and storage	Accommodation and food service activities	Information and communication	Real estate activities	Professional, scientific and technical services	Administrative and support service activities	Public administration and defence, compulsory social	Education	Human health services and social work activities	Arts, entertainment and recreation	Other services	Financial and Insurance Activities	Internal & other exposures	Total
Central governments or central banks														35					5		<b>41</b>
Multilateral development banks														71							<b>71</b>
Institutions																			10		<b>10</b>
Corporates		7	36	6	15	58	118	10	3	32	146	2	68		0	6	1	3	150	1	<b>662</b>
Secured by mortgages on immovable property											2									5	<b>7</b>
Exposures in default						7		6				2	3						2		<b>20</b>
Items associated with particularly high risk			1			58					122		17								<b>198</b>
Claims on institutes and corporates with a short term credit assessment																			112		<b>112</b>
Equity exposures																			11		<b>11</b>
Other exposures			1				4	14					2							20	<b>41</b>
<b>Total</b>		<b>7</b>	<b>37</b>	<b>6</b>	<b>15</b>	<b>123</b>	<b>122</b>	<b>30</b>	<b>3</b>	<b>32</b>	<b>270</b>	<b>4</b>	<b>91</b>	<b>106</b>	<b>0</b>	<b>6</b>	<b>1</b>	<b>3</b>	<b>291</b>	<b>27</b>	<b>1,174</b>

**8.11. Table 20: Breakdown of net exposure amounts by residual maturity**

The residual maturity breakdown of all the exposures, broken down by exposure classes

	£m						Total
	On demand	<= 1year	>1year <=5 years	>5 years	No stated maturity	Past due	
Central governments or central banks			35	5			<b>41</b>
Regional governments or local authorities							
Public sector entities							
Multilateral development banks		18	53				<b>71</b>
International organisations							
Institutions		10					<b>10</b>
Corporates		389	219	19		35	<b>662</b>
Retail							
Secured by mortgages on immovable property		7					<b>7</b>
Exposures in default		7	12			1	<b>20</b>
Items associated with particularly high risk		118	76			4	<b>198</b>
Covered bonds							
Claims on institutes and corporates with a short term credit assessment	95	16	1				<b>112</b>
Collective investments undertakings							
Equity exposures			11				<b>11</b>
Other exposures		33	5	3			<b>41</b>
<b>Total</b>	<b>95</b>	<b>599</b>	<b>412</b>	<b>28</b>		<b>40</b>	<b>1,174</b>

**8.12. Table 21: Credit quality of exposures by exposure class and instrument**

	£m						Net values
	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges for the period	
	Defaulted exposures	Non-defaulted exposures					
Central governments or central banks		41					<b>41</b>
Regional governments or local authorities							
Public sector entities							
Multilateral development banks		71					<b>71</b>
International organisations							
Institutions		10					<b>10</b>
Corporates		662					<b>662</b>
Retail							
Secured by mortgages on immovable property		7					<b>7</b>
Exposures in default	31		11				<b>20</b>
Items associated with particularly high risk		198					<b>198</b>
Covered bonds							
Claims on institutes and corporates with a short term credit assessment		112					<b>112</b>
Collective investments undertakings							
Equity exposures		11					<b>11</b>
Other exposures		41					<b>41</b>
<b>Total</b>	<b>31</b>	<b>1,154</b>	<b>11</b>				<b>1,174</b>

**8.13. Table 22: Credit quality of exposures by industry type**

	£m						Net values
	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges for the period	
	Defaulted exposures	Non-defaulted exposures					
Agriculture, forestry and fishing							
Mining and quarrying		7					7
Manufacturing		37					37
Electricity, gas, steam and air conditioning supply		6					6
Water supply		15					15
Construction	14	116	7				123
Wholesale and retail trade		122					122
Transport and storage	7	24					30
Accommodation and food service activities		3					3
Information and communication		32					32
Real estate activities		270					270
Professional, scientific and technical activities	4	2	2				4
Administrative and support service activities	3	88					91
Public administration and defence, compulsory social security		106					106
Education							
Human health services and social work activities		6					6
Arts, entertainment and recreation		1					1
Other services		3					3
Financial and Insurance Activities	3	289	2				291
Internal Assets		27					27
<b>Total</b>	<b>31</b>	<b>1,154</b>	<b>11</b>				<b>1,174</b>

8.14. Table 23: Credit quality of exposures by geography

	£m						Net values
	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges for the period	
	Defaulted exposures	Non-defaulted exposures					
United Kingdom	10	877	6				881
Switzerland		1					1
Jersey		11					11
Bahrain		8					8
Abu Dhabi		1					1
Dubai	7	13	2				18
Kuwait		98					98
OUAE		4					4
Jordan		1					1
Qatar		15					15
Saudi Arabia	8	17	3				22
United States		36					36
Cayman Islands	7						6
Other		71					71
<b>Total</b>	<b>31</b>	<b>1,154</b>	<b>11</b>				<b>1,174</b>



8.15. Table 24: Ageing of past due exposures

	£m					
	Gross carrying values					
	<=30 days	>30 days <=60 days	>60 days <=90 days	>90 days <=180 days	>180 days <=1 year	>1 year
Financing arrangements			35	4	5	
Debt Securities						
<b>Total</b>			<b>35</b>	<b>4</b>	<b>5</b>	

8.16. Table 25: Changes in the stock of general and specific credit risk adjustments held against financing arrangements and debt securities that are defaulted or impaired

	£m	
	Accumulated specific credit risk adjustment	Accumulated general credit risk adjustment
<b>Opening balance</b>	<b>17</b>	
Increases due to amounts set aside for estimated financing arrangements losses during the period	3	
Decreases due to amounts reversed for estimated financing arrangements losses during the period	-7	
Decreases due to amounts taken against accumulated credit risk adjustments	-3	
Transfers between credit risk adjustments		
Impact of exchange rate differences		
Business combinations, including acquisitions and disposals of subsidiaries		
Other adjustments	1	
<b>Closing balance</b>	<b>11</b>	
Recoveries on credit risk adjustments recorded directly to the statement of profit or loss		
Specific credit risk adjustments directly recorded to the statement of profit or loss		

8.17. Table 26: Changes in the stock of defaulted and impaired financing arrangements and debt securities

	£m
	<b>Gross carrying value defaulted exposures</b>
<b>Opening balance</b>	<b>51</b>
Financing arrangements and debt securities that have defaulted or impaired since the last reporting period	17
Returned to non-defaulted status	-5
Amounts written off	-3
Other changes	-29
<b>Closing balance</b>	<b>31</b>

### 8.18. Use of External Credit Assessment Institutions (ECAI Ratings)

Credit ratings are determined by either of Moody’s Credit Edge, Moody’s Risk Calc and BLME Internal Rating Methodology and a validation of major ECAI (External Credit Assessment Institution) ratings, such as Moody’s and Fitch, where such ratings exist. Where ECAI ratings are used and more than one such rating exists, the more conservative rating is adopted. This rating validation takes into account the transactional and collateral attributes of the credit proposal. Non-rated obligors are assessed using either Moody’s Credit Edge, Moody’s Risk Calc or BLME Internal Rating Methodology depending upon sector and approved at CCRC prior to commitment.

BLME follows the association of the external rating of each nominated ECAI with the credit quality steps prescribed in Part Three, Title II, Chapter 2 of the Capital Requirements Regulation [(EU) 575/2013].

**8.18.1. Table 27: The level and extent of the use of ECAI ratings as at 31st December 2017.**

Exposure class	Total	Of which rated
Central governments or central banks	41	41
Multilateral development banks	71	71
Institutions	106	35
Corporates	542	18
Secured by mortgages on immovable property	7	0
Exposures in default	20	0
Items associated with particularly high risk	171	3
Claims on institutes and corporates with a short term credit assessment	111	111
Equity exposures	11	0
Other exposures	41	0
	1,121	278

8.19. Table 28: Breakdown of regulatory exposure values by risk weight

	£m																Total	Of which unrated	RWA Total	
	0%	2%	4%	10%	20%	35%	50%	70%	75%	100%	150%	350%	370%	1,250%	Other	Deducted				
Central governments or central banks	21				15					5								41		8
Multilateral development banks	71																	71		
Institutions					10		96											106	71	50
Corporates							14			527	1							542	524	526
Secured by mortgages on immovable property						7												7	7	3
Exposures in default										9	10							20	20	25
Items associated with particularly high risk												171						171	168	256
Claims on institutes and corporates with a short term credit assessment					108		2											111		23
Equity										11								11	11	11
Others										41								41	41	41
<b>Total</b>	<b>92</b>				<b>133</b>	<b>7</b>	<b>112</b>			<b>595</b>	<b>182</b>							<b>1,121</b>	<b>843</b>	<b>943</b>

**8.20. Table 29: CCR exposure by approach**

The following table below details the Bank's exposure to Counterparty Credit Risk which occurs on derivative transactions undertaken. For BLME this exposure is derived from the small number of profit rate swap transactions that are undertaken to manage profit rate exposure and Foreign Exchange contracts which are transacted in accordance with business requirements or at the request of our customer base.

	£m						
	Notional	Replacement cost / current market value	Potential future credit exposure	EEPE	Multiplier	EAD post CRM	RWAs
Mark to market			1				
Original exposure	2					2	0
Standardised approach		-1			1.4		
IMM (for derivatives & SFTs)							
<i>Of which securities financing transactions</i>							
<i>Of which from derivatives and long settlement transactions</i>							
<i>Of which from contractual cross-product netting</i>							
Financial collateral simple method (for SFTs)							
Financial collateral comprehensive method							
VaR for SFTs							
<b>Total</b>	<b>2</b>	<b>-1</b>	<b>1</b>		<b>1.4</b>	<b>2</b>	<b>0</b>

8.21. Table 30: CCR exposure by regulatory portfolio and risk

	£m																Total	Of which unrated	
	0%	2%	4%	10%	20%	35%	50%	70%	75%	100%	150%	350%	370%	1,250%	Others	Deducted			
Central governments or central banks																			
Multilateral development banks																			
Institutions																			
Corporates																			
Secured by mortgages on immovable property																			
Exposures in default																			
Items associated with particularly high risk																			
Claims on institutes and corporates with a short term credit assessment					1													1	1
Other exposures																			
<b>Total</b>					<b>1</b>													<b>1</b>	<b>1</b>

**8.22. Table 31: CVA capital charge**

	£m	
	Exposure value	RWAs
Total portfolios subject to the advanced method		
(i) VaR component (including the 3× multiplier)		
(ii) SVaR component (including the 3× multiplier)		
All portfolios subject to the standardised method	1	
Based on the original exposure method		
<b>Total subject to the CVA capital charge</b>	<b>1</b>	

8.23. Table 32: Breakdown of exposures by qualifying and non-qualifying CCP

	£m	
	EAD post CRM	RWAs
<b>Exposures to QCCPs (total)</b>		
Exposures for trades at QCCPs (excluding initial margin and default fund contributions); of which		
(i) OTC derivatives		
(ii) Exchange-traded derivatives		
(iii) SFTs		
(iv) Netting sets where cross-product netting has been approved		
Segregated initial margin		
Non-segregated initial margin		
Prefunded default fund contributions		
Alternative calculation of own funds requirements for exposures		
<b>Exposures to non-QCCPs (total)</b>		
Exposures for trades at non-QCCPs (excluding initial margin and default fund contributions); of which		
(i) OTC derivatives		
(ii) Exchange-traded derivatives		
(iii) SFTs		
(iv) Netting sets where cross-product netting has been approved		
Segregated initial margin		
Non-segregated initial margin		
Prefunded default fund contributions		
Unfunded default fund contributions		



## 9. Credit risk mitigation

### 9.1. Policies and processes for, and an indication of the extent of, on- and off balance sheet netting

The Bank has two transactions that have associated guarantees that are utilised as credit mitigation for regulatory capital purposes, the effect of which, in the context of its total assets, is not considered to be material to BLME's capital requirement. BLME currently benefits from no legally enforceable netting agreements.

### 9.2. Policies and processes for collateral valuation and management

BLME has secondary credit exposure as the Commercial Finance and Private Banking financing transactions are secured on assets. The Bank monitors the composition of these portfolios, within which the collateral assets are subject to regular assessment and review by professional valuation agents.

### 9.3. Main types of collateral taken

This section describes the types of collateral BLME accepts. In general terms BLME has no restriction on the types of collateral that can be accepted within the confines of:

- UK Regulatory requirements (transposed from the CRR)
- UK and/or local legal jurisdictional requirements
- Sharia'a law

#### 9.3.1. Guarantees

Guarantees are legal relationships between the guarantor and lender (the Bank), through which the guarantor assumes the responsibility to fulfil the obligor's obligations. In order to be considered appropriate for credit risk mitigation purposes, the guarantees must satisfy the conditions under articles 194, 203 and 204 of the CRR.

##### i. Personal guarantee

When taking a personal guarantee, an individual agrees to be responsible, or responsible to a certain, pre-determined limit for the financial obligations of a debtor or obligor to a financier, in the event that the debtor or obligor fails to pay an amount owing under the finance agreement

##### ii. Corporate guarantee

When taking a corporate guarantee, a company agrees to be held responsible, or responsible to a certain, pre-determined limit, for completing the duties and obligations of a debtor to a lender, in the event that the debtor fails to fulfil the terms of the facility.

##### iii. Credit institution guarantee

When taking a credit institution guarantee, a credit institution agrees to be responsible, or responsible to a certain, pre-determined limit, for completing the duties and obligations of a debtor to a lender, in the event that the debtor fails to fulfil the terms of the facility. Such guarantees may take the form of a formal bank guarantee or a Standby Letter of Credit (SBLC).

### 9.3.2. Tangible collateral

In the case of tangible collateral, the Bank acquires rights over a tangible asset which belongs to the obligor or the guarantor. The main types of tangible collateral BLME accepts include, but are not limited to:

- Mortgages or fixed charges over land/buildings
- Chattel mortgages & Fixed Charges over Leased Assets (Plant/Machinery)
- Fixed charges or pledges over cash deposits
- Fixed charges or pledges on bonds, Sukuk or listed stocks/shares
- Share pledges over private company shares
- Fixed charges or pledges over intellectual property
- Floating charges over receivables or stock
- Debentures
- Other floating charges
- General letters of pledge, incorporating a pledge over goods

The value of tangible collateral may fluctuate due to legal reasons, emergencies (natural disasters, etc) and other reasons. The value of collateral must therefore be assessed frequently..

#### Mortgages / Fixed Charges over land/buildings

A fixed charge is a charge or mortgage secured on particular property, e.g. land and buildings, a ship, piece of machinery, a deposit account, shares or intellectual property such as copyrights, patents, trademarks, etc.

#### Chattel Mortgages & Fixed Charges over Leased Assets (Plant/Machinery)

A chattel mortgage is a mortgage over moveable property. Typically this would be taken over vehicles or plant/machinery that is not physically fixed in place.

#### Fixed charges or pledges over cash deposit

English law regards a cash deposit as a debt payable by the account bank to the account holder. It is common to grant security over that debt by charging or assigning the deposit in favour of the lender.

#### Fixed charges or pledges on bonds, Sukuk or listed stocks/shares

A charge or pledge over specific assets, generally taken as part of an overall security package or as primary security for Private Banking leveraged lending. The specific underlying assets may vary, but include (without limitation) the following:

- Sovereign, municipal, Corporate bonds or Sukuk.
- Shares, either in Corporates or in Funds or Unit Trusts.
- LME Warrants

#### Share Pledges over Private Company shares

These pledges are generally taken in circumstances when the Bank is providing sole banking facilities to a company, or is dealing with a single asset holding SPV. This is to ensure that the Bank is able to take full ownership of the company in the event of insolvency, thereby facilitating the potential sale of the company as an entity, rather than requiring repossession of the underlying asset.

#### Fixed charges or pledges over intellectual property

This is an asset class discouraged by BLME however Security can be taken over intellectual property by means of legal mortgage or fixed or floating charges. It is unusual for a legal mortgage to be taken over intellectual property ("IP") given that if this were taken, it would then have to give an exclusive licence back to the mortgagor

immediately in order for the IP to be used in the business. While a legal mortgage is viewed as the most robust form of security, a properly drafted, executed and perfected legal charge over IP provides the most important benefits.

IP includes, but is not limited to, brands, patents, design rights, copyrights and trademarks.

#### Floating Charges

A floating charge is a particular type of security, available only to companies. It is an equitable charge on (usually) all the company's assets, both present and future, occasionally the charge is over just a class of the company's assets, such as its stock or receivables. This particular type of charge should be considered as of a secondary nature.

#### Debentures

In the UK, a mortgage debenture is the most usual form for securing borrowing by a company. A debenture allows for a fixed charge over fixed assets such as land/buildings and a floating charge over stocks and receivables.

#### Other floating charges

It is possible to take specific floating charges, for instance over stock or receivables only, outside of a standard debenture.

#### General letters of pledge, incorporating a pledge over goods and Trust Receipts

A General Letter of Pledge (also known as a General Letter of Hypothecation and Pledge) is possessory security over goods. It is not a charge. The existence of a pledge is dependent on possession of the underlying goods through either physical or constructive means via documents of title.

### **9.4. Main types of guarantor and credit derivative counterparty and their creditworthiness**

The Bank has two transactions that have associated guarantees that are utilised as credit mitigation; the guarantees are provided by Financial Institutions with ECAI ratings of BBB or higher.

### **9.5. Market or credit risk concentrations within the credit mitigation taken**

There are no material market or credit concentrations within the credit risk mitigation taken.

9.6. Table 33: CRM techniques – Overview

	£m				
	Exposures unsecured - Carrying amount	Exposures secured - Carrying amount	Securitisation framework	Counterparty credit risk framework	Market risk framework
Debt Securities	127				
Financing arrangements	823	103			
<b>Total exposures</b>	<b>939</b>	<b>103</b>			
Of which defaulted	20				

9.7. Table 34: Credit risk exposure and CRM effects

	£m					
	Exposures before CCF and CRM		Exposures post CCF and CRM		RWAs and RWA Density	
	On balance sheet amount	Off balance sheet amount	On balance sheet amount	Off balance sheet amount	RWAs	RWA density
Central governments or central banks	41		41		8	1%
Multilateral development banks	71		71			
Institutions	10		106		50	5%
Corporates	596	66	501	41	526	56%
Secured by mortgages on immovable property	7		7		3	0%
Exposures in default	19	2	19	1	25	3%
Items associated with particularly high risk	146	52	146	25	256	27%
Claims on institutes and corporates with a short term credit assessment	111	1	111		23	2%
Equity	11		11		11	1%
Other exposures	41		41		41	4%
<b>Total</b>	<b>1,054</b>	<b>121</b>	<b>1,054</b>	<b>67</b>	<b>943</b>	<b>100%</b>

## 10. Unencumbered assets

BLME does not enter into collateralised or asset-backed contracts and none of its assets are encumbered.

### 10.1. Table 35: Assets

	£m			
	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
<b>Collateral received by the reporting institution</b>			<b>1,054</b>	
Equity instruments				
Debt securities			116	116
Other assets			938	938

## 11. Table 36: Exposure to equities not included in the trading book

Accounting portfolio	Objective	Status	£m	
			Balance sheet value	Fair value
A.F.S.	Capital gain	Unlisted	1	1

A small portfolio of unlisted equity investments is subject to third party valuations.

The amounts of total unrealised gains or losses and latent revaluation gains or losses are considered to be immaterial to regulatory capital levels.

There were no material cumulative realised gains or losses arising from sales and liquidations during the period

## 12. Exposure to market risk

### 12.1. Market Risk

Market risk is the potential for loss caused by adverse changes in market prices. In the case of BLME this applies to rate re-price risk in its Asset and Liability book and currency rate movements in FX activities. The Bank has a very small level of equity risk from its portfolio of private equity and venture capital investments.

FX activities are subject to relatively small position limits as dealing is primarily focused on facilitating client transactions. As a consequence, the most significant form of market risk is rate re-price risk. This arises from the cumulative mismatch between the re-pricing dates of a) the Bank's profit rate bearing assets and liabilities b) the investment of the Bank's capital and reserves and c) the Profit Rate Swaps transacted to mitigate the re-pricing risk. The Treasury desk is responsible for managing these risks under the guidance of ALCO. This is accomplished by providing the Treasury desk with "Operating Risk Limits" that define the maximum risk positions by currency and by tenor. These limits are expressed in basis point sensitivity (PV01) terms. Compliance with dealing limits is reported to management on a daily basis and reviewed at the monthly ALCO meetings. On a quarterly basis Risk Management provides BRC with a report on the development and use of all market risk limits.

The Bank's Stress Testing and Scenario Analysis Policy requires periodic stress testing of all market risks to be undertaken. Stress Test Guidance Parameters are set to measure the ability of BLME's capital resources to withstand extreme adverse changes in market rates. These are presented to ALCO and ERC monthly and BRC quarterly.

FX risk at BLME emanates mostly from any mismatch in unhedged customer forward business. These transactions on their own are usually of a very small size and as such, may not always reasonably be matched. Nevertheless, grouping such transactions does allow a large degree of matching leaving just a small residual FX risk. In regard to Spot FX risks BLME has limited risk appetite for (all) FX risk and has consequently implemented small nominal countervalue-based Net Open Position Limits within its Operating Risk Limits. The adherence to these limits is checked by the Finance Department, in parallel with Risk Management. Exceptions are reported to management on a daily basis and reviewed at the monthly ALCO meetings and quarterly BRC meetings.

The Capital Requirement for Position, FX and Commodities Risks as at 31 December 2017 was £671k

**12.2. Table 37: Market risk under the standardised approach**

	£m	
	RWAs	Capital requirements
Outright products		
Interest rate risk (general and specific)		
Equity risk (general and specific)		
Foreign exchange risk	1	
Commodity risk		
Options		
Simplified approach		
Delta-plus method		
Scenario approach		
Securitisation (specific risk)		
<b>Total</b>	<b>1</b>	

### 13. Exposure to Operational risk

Operational risk is the potential for financial loss or damage to reputation resulting from failed or inadequate internal processes and systems, the actions of individuals or the impact of external events. The Bank includes conduct, reputational and cyber-crime risk within operational risk. To mitigate Operational Risk BLME has the following safeguards:-

- A detailed Business Continuity Plan.
- Conducts full and partial tests of the Disaster Recovery site.
- Utilises the secure SWIFT system for payment messages.
- Maintains comprehensive insurance policies.
- A legal review is conducted on all new documentation (core agreements, contracts and legal documentation) and existing documentation is reviewed on a rotational basis. These reviews utilise specialist external support when appropriate.

- Operates a New Product Approval process that ensures that all new products are reviewed and authorised by relevant business and support areas.
- Ensures that all departments have their own operating procedures and policies, which provides an overview of BLME's operations.
- Operates a committee structure to facilitate the support of business areas and development of the new business initiatives within a robust and integrated operational framework.
- Operates with clearly defined and authorised delegated authorities.

BLME's Operational Risk Policy is founded on the Basel "Principle for the Sound Management of Operational Risk" guidelines that were issued in June 2011. The Bank operates and reports to the PRA using the Basic Indicator Approach, under which a prescribed percentage of the Bank's historic revenues form the basis of BLME's Operational Risk Capital Adequacy reporting.

In parallel with issuing its Operational Risk Policy, Risk Management has implemented an internal Operational Risk Database to record, follow-up and report risk events and losses. Risk Management has also undertaken operational risk awareness training for all relevant staff.

As part of its PRA Pillar III ICAAP process, BLME's policy is to undertake an annual Risk and Control Self-Assessment (RCSA) across all Front and Back Office functions. This process takes account of the seriousness of the loss potential, the probability of occurrence and the effect of any risk mitigation factors. By asking respondents to identify any further risk mitigating initiatives, BLME has a means of tracking key risks to ensure that these are optimally addressed. The results from this assessment are reported to ERC (via ORC) and to EXCO, and are included within Risk Management's reporting to BRC.

#### 14. Exposure to interest rate risk on positions not included in the trading book

These risks principally emanate from the following sources:

- asset and liability rate reset mismatches from Commercial Finance and Private Banking lending.
- asset and liability rate reset mismatches from money market and liquidity management activities.
- strategies used to hedge the Bank's capital and reserves.

A table disclosing the impact of an increase/decrease of 100 basis points in profit rates at 31<sup>st</sup> December 2017 is shown within note 36.a.ix.c.i. of the financial statements

#### 15. Remuneration Policy

The following disclosures are those applicable to BLME as a proportionality level 3 firm (i.e. total assets < £15bn)

##### 15.1. Decision making process/body

BLME has an established Remuneration Committee (RemCo) which meets regularly to consider the overall reward framework across the Bank. Within the authority delegated by the Board, RemCo is responsible for approving remuneration policy and in doing so takes into account the pay and conditions across the Bank. This includes the terms of bonus plans, share plans, other long-term incentive plans and the individual remuneration packages of

executive directors and other senior Bank employees, including all employees in positions of significant influence and those having an impact on our risk profile (Material Risk Takers).

During 2017 the RemCo has striven to ensure that BLME's Remuneration and Benefits Policy is fair and transparent and that the Bank's remuneration framework supports our business strategy whilst discouraging inappropriate risk taking and appropriately rewarding staff. RemCo does not plan to materially amend the Remuneration and Benefits Policy or the framework that is currently in place. No directors are involved in deciding their own remuneration.

The members of RemCo during 2017 were Neil Holden, Sheikh Abdullah Jaber Al-Ahmed Al-Sabah, , Michael Williams and David Williams. Neil Holden is the appointed chairman of RemCo.

RemCo received independent advice on executive remuneration issues from Mercer during 2017. Benchmarking to market of the Bank's salaries was conducted by independent remuneration advisors.

### 15.2. Link between Pay and Performance

Total remuneration at BLME comprises salary, car allowance, annual bonus, pension contributions and long-term incentives designed to reward performance and delivery of key strategic objectives. In determining the level of award of any component of variable pay (annual bonus and long-term incentives), the Bank has a policy to assess the extent to which performance has been achieved.

BLME's remuneration policy is designed to reflect the extent to which the Bank's annual objectives have been met against the annual budget, the risk appetite framework and competitive market practice. The purpose of the existing Long Term Incentives has been to reward the creation of sustained growth in shareholder value and to encourage alignment with the interests of shareholders.

### 15.3. Table 38: Remuneration of senior management and members of staff whose actions have a material impact on the risk profile of the institution

	Total	Management body	Senior management	Other
Number of MRTs	30	10	9	11
Fixed:	£m	£m	£m	£m
Cash based	3.6	1.0	1.3	1.3
Share based	0	0	0	0
Total fixed pay	3.6	1.0	1.3	1.3
Variable				
Cash	1.0	0.3	0.4	0.3
Deferred cash*	0.5	0.3	0.2	0.0
Share based payment charges**	0.4	0.1	0.2	0.1
Total variable pay	1.9	0.7	0.8	0.4
Grand Total	5.6	1.7	2.1	1.7

- Accounted for in 2017 but deferred over 3 years

\*\* Reflects accounting charges relating to share based awards in 2017 and prior years



#### 15.4. Table 39: Analysis of remuneration by business area

		£m			
		Wealth Management	Commercial Finance	Central Functions	Total
Aggregate remuneration expenditure	2016	0.4	0.8	2.6	3.8
	2017	1.0	1.0	3.6	5.6

#### 16. Table 40: Leverage

The following leverage ratio calculations are disclosed in accordance with EBA and PRA guidance and on a fully phased in basis.

BLME has no fiduciary assets and accordingly does not report any fiduciary items as derecognised from the calculation of the leverage ratio.

The ratio has remained consistent throughout 2017 and in accordance with Bank risk appetite; there has been no requirement to manage excessive levels of leverage.

	Basel Leverage ratio	UK Leverage Ratio
31 <sup>st</sup> December 2017	19.28%	19.28%

UK Leverage metric: BLME has no claims against central bank entities that would be excluded in the calculation of a UK Leverage ratio.