Pillar III Disclosures

31st December 2016

Pillar III Contents

1 Introduction

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.

2 Scope of Pillar III Application

2.1 Background

The European Union Capital Requirements Directive (the Directive) came into effect on 1 January 2007. It introduced consistent capital adequacy standards and an associated supervisory framework in the EU based on the Basel II framework. The Directive was updated by the CRD IV Basel III requirements which became effective from 1 January 2014.

Since its authorisation as a licensed financial institution in July 2007, BLME has adopted the Standardised Approach to credit and market risk under the Directive. For operational risk BLME operates under the Basic Indicator Approach.

The Directive's framework is structured around three pillars:

- Pillar I is the Bank's minimum capital requirements.
- Pillar II (supervisory review) requires the Bank to identify, via the Internal Capital Adequacy Assessment Process (ICAAP), any specific risks that may result in additional capital being held.
- Pillar III defines the disclosure rules that allow market participants to assess key pieces of information on the Bank's capital, risk exposures and risk assessment processes.

2.2 Policy Statement

Basis of Preparation

The European Union ('EU') implemented the Basel III proposals published in December 2010 through the Capital Requirements Regulation ('CRR') and Capital Requirements Directive (together referred to as 'CRD IV') which came into force on 1 January 2014 and is enforced in the UK, together with local implementing rules and guidance, by the Prudential Regulation Authority ('PRA'). The rules include disclosure requirements known as 'Pillar 3' which apply to banks and building societies. These are designed to promote market discipline through the disclosure of key information about risk exposures and risk management processes. No material disclosures have been omitted and nor have any disclosures been omitted from this document for confidentiality purposes.

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. 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.

This document, in conjunction with the 31 December 2016 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 2016.

Verification

BLME's Pillar III disclosures have been prepared in accordance with CRD IV requirements and reviewed and approved by the Board of Directors on 14 March 2017. 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.

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 2016, 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.

2.3 Consolidation Basis

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 34 within the Annual Report and Accounts:

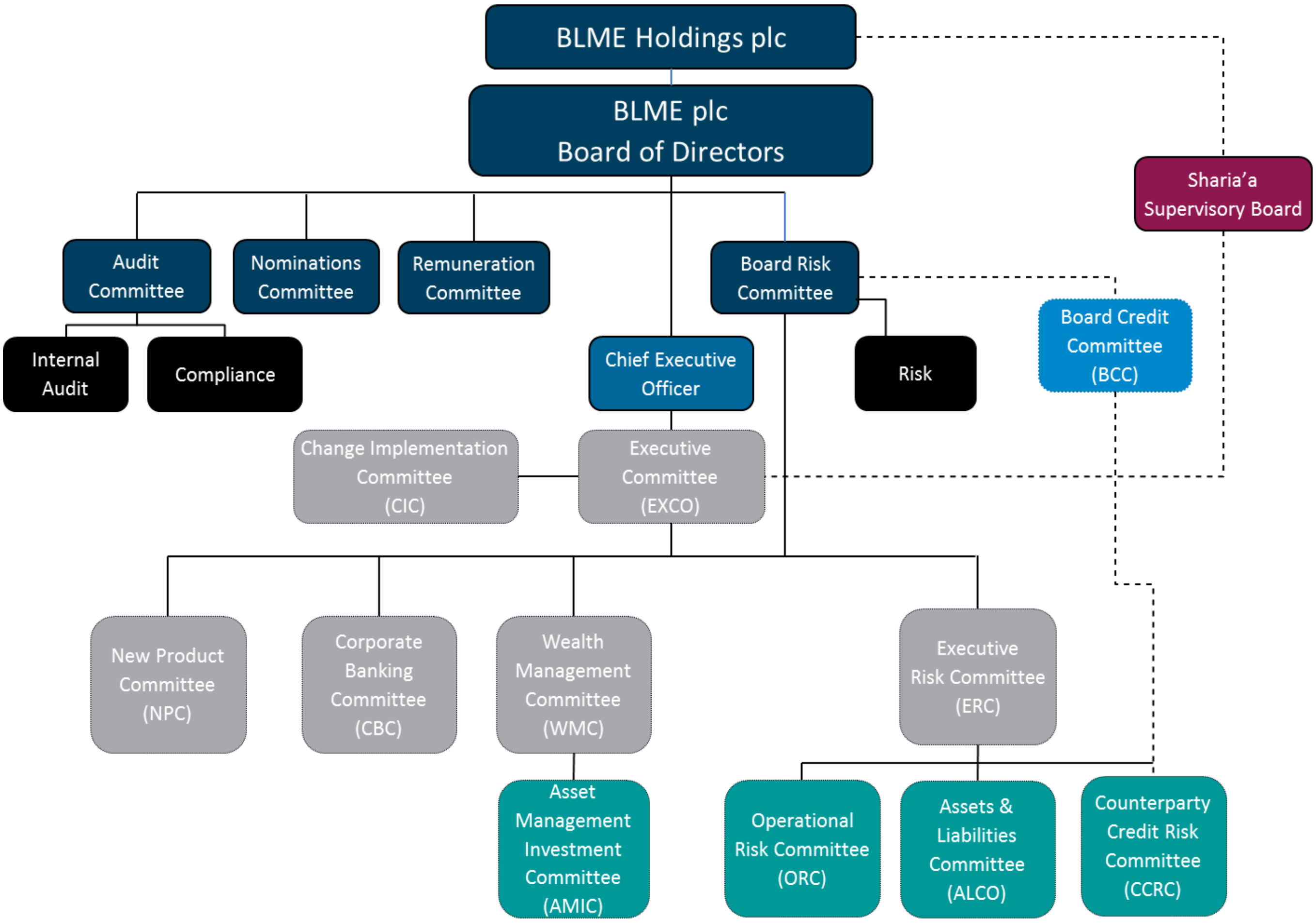
a) BLME's investment in the Luxembourg SICAV, which it established, is fully consolidated in the Annual Reports and Accounts but for regulatory supervision a qualifying portion is subject to credit risk weighting with the remainder deducted from regulatory capital if the appropriate threshold is breached.
b) There are two active structured entities ("SE") (2015: two) that do not qualify as subsidiaries under UK law but which are consolidated under IFRS 10 as the substance of the relationship is that the entities are deemed to be controlled by the Group, the regulatory basis recognises BLME's lending exposures to these entities on a risk weighted basis.
c) IFRS requires the consolidation of the assets of MKL Construction Equipment Finance Ltd (MKL) due to BLME's majority ownership; the regulatory basis recognises BLME's exposures to MKL on a risk weighted basis.

3 Risk Management Objectives and Policies

3.1 Risk Governance

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.

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").

In June 2016 the committee structure overseeing risk governance was amended as follows:

a) Executive Risk Committee took oversight responsibility for ALCO, CCRC and Operational Risk Committee
b) Created the Change Implementation (to replace the Strategic Development Committee), New Product, Operational Risk, Corporate Banking and Wealth Management Committees
c) Wealth Management Committee took oversight responsibility for the Asset Management Investment Committee

3.2 BLME Board of Directors

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 Guidelines that define credit risk appetite in terms of deal size, client rating, tenor, country risk and collateral considerations.

Directorships held by members of the Board

The number of external directorships and partnerships held by the Executive and Non-Executive Directors who served on the Board as at 31 December 2016 are detailed below.

Table 1: Board directorships

Name	Number of Directorships/partnerships [1]
Adel Abdul Wahab Al-Majed	1
Sheikh Abdullah Jaber Al-Ahmed Al-Sabah	2
Frank Vermeulen	3
Neil Holden	4
Michael Williams	2
Zeyad T. Al-Mukhaizeem	2
David Gareth Williams	1

Note 1: The number of directorships shown excludes the Company and its subsidiaries and also counts external directorships held within the same group of companies as a single directorship in line with CRD IV. Directorships of non-commercial organisations are not included.

3.3 Board Committee Structures

The following sections set out the Bank's principal governance structures. The Board and its committees meet on at least a quarterly basis. Details of the actual number of meetings can be seen in the Annual Reports and Accounts.

3.3.1 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 are outside of stated risk appetite and/or meet other 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.

3.3.2 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.

It 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.

3.3.3 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 of prevailing market conditions, best market practice and regulatory compensation guidelines. RemCo has appointed Mercer as an independent professional advisor.

3.3.4 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, thorough a robust and prudent process, with the use of external consultants as necessary

3.4 Executive Committee Structures

3.4.1 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.

3.4.2 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.

3.4.3 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.

3.4.4 Counterparty Credit Risk Committee (CCRC)

CCRC is responsible for the approval of individual obligor risks using the Target Market Criteria, 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.

3.4.5 Asset Management Investment Committee (AMIC)

AMIC provides input and oversight of the investment activities within BLME's asset management business. These responsibilities, which take account of the Banks 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 WMC.

3.4.6 Change Implementation Committee (CIC)

CIC is responsible for overseeing new products and strategic projects (once approved by the New 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.

3.4.7 New Product Committee

Proposals for new products or material changes to existing products supported by EXCO are delegated to the NPC for processing. The purpose of NPC 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 it's regulatory responsibilities, risk management obligations, and obligations to its clients and the markets within which it operates.

3.4.8 Corporate Banking Committee

Using the delegated authority and discretions assigned by EXCO, the committee provides input, reporting and oversight on all matters related to the Corporate Banking business including: business performance, financial Performance, client management, controls and operational Risk, compliance, staffing, new product initiation, new business initiatives.

3.4.9 Wealth Management Committee

Using the delegated authority and discretions assigned by EXCO, the committee provides input, reporting and oversight on all matters related to the Wealth Management business including: business performance, financial performance, client management, controls and operational Risk, compliance, staffing, new product initiation, new business initiatives.

3.5 Sharia'a Supervisory Board

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.

3.6 Organisation of 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 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 credit 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.

3.7 Compliance

The Compliance Department is an independent function which is formed of two teams (Financial Crime and Compliance) that reports to the Chief Executive Officer. 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. New Product Committee.

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

3.8 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.

3.9 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.

3.9.1 Credit Risk (including Counterparty Risk)

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 its Corporate Banking 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 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. These 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

Table 2 - Group Credit Risk Capital Requirement as at 31 December 2016

Exposure Class	**£m**
Central governments or central banks	1
Institutions	2
Corporates	39
Retail Exposures	0
In default	3
Exposures associated with particularly high risk	27
Institutions and corporates with a short-term credit assessment	3
Equity exposures	0
Other items	2
Total Credit Risk Capital	77

Whilst not necessarily being Credit Risk related from a technical interpretation point of view, the following ancillary risks has been identified within the Credit Risk Capital component:-

Leasing

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.

3.9.2 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, currency rate movements in its FX activities, credit spread movements in its small Sukuk Trading book. The Bank has a small level of equity risk from its modest portfolio of private equity and venture capital investments.

FX activities are subject to relatively small position limits as dealing is mostly 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, and are checked by the Finance Department on a daily basis in conjunction with Risk Management. 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.

In BLME FX risk emanates mostly from spot deals (usually undertaken to fund and facilitate client business) and from hedging foreign currency profits and losses. In view of the limited risk appetite for FX risk, BLME has implemented small nominal based Net Open Position Limits within its Operating Risk Limits. The adherence to 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 2016 was £671k.

3.9.3 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. On a daily basis liquidity risk is managed by the Treasury desk who in conjunction with Finance Department and Risk Management ensure that BLME is compliant on an intra-day basis with its regulatory liquidity ratios. Daily reports are circulated to Senior Management showing BLME's actual and projected liquidity profile, and as 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.

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. 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.

3.9.4 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 the overall banner of 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.

3.9.5 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	Risk	ERC
Credit	Risk	BCC/ERC/CCRC
Operational	Risk	ERC/ORC
Financial Crime	Audit	EXCO
Conduct Risks		
Sharia'a compliance	Board	EXCO
Reputational risk	Board	EXCO
All other conduct risks	Audit	EXCO

4 Capital Resources

The amounts of regulatory capital shown below are based on the amounts reported to the PRA as at 31 December 2016 and differ from the balances shown in the Group's Annual Report and Accounts as the total below does not include adjustments arising from the annual audit process which were affected after regulatory submission deadlines.

The Group's capital resources are all components of Tier 1 and Tier 2 Capital. At December 31 2016 these were as follows:

Table 3: Regulatory capital composition

	31/12/2016	31/12/2015
Common equity tier 1 (CET1)	**£m**	**£m**
Share capital	49	49
Share premium	181	181
Indirect holdings of CET1 instruments	-4	-4
Retained earnings	-10	14
Accumuated other comprehensive income	0	0
Other reserves	2	1
Cash flow hedge reserve	0	-1
Significant investment in CET 1 instruments of financial sector entities	0	-35
Deferred tax assets	0	-2
Intangible assets	-2	-2
Total CET1	**216**	**201**
Additional tier 1		
Capital instruments eligible as AT1 capital	0	0
Total Tier 1 capital	**216**	**201**
Tier 2		
General credit risk adjustments*	4	3
Total Tier 2 capital	**4**	**3**
Total regulatory capital resources	**220**	**204**
Risk weighted assets - Pillar 1		
Credit risk**	960	1,220
Market risk***	7	3
Operational risk	87	81
Credit valuation adjustment***	1	1
Total	**1,055**	**1,305**
Capital ratios		
Common equity tier 1 (CET1)	20.42%	15.41%
Tier 1	20.42%	15.41%
Total capital	20.81%	15.65%

* this is the collective impairment provision, refer to the Annual Report and Accounts for full details
** including counterparty credit risk
*** the capital requirment associated with Market Risk and CVA Risk is not considered to be material and therefore no further disclosures of these items are made

Table 4 Capital Instruments - main features and terms

The table below details the key features of the regulatory capital instruments issued.

Issuer	Bank of London and The Middle East Plc	BLME Holdings Plc
ISIN	N/A not listed	GB00BB0RJ113
Governing law	English	English
CRR Rules	Tier 1	Tier 1
Instrument type	Share capital	Share capital
Regulatory capital value (£m)	48.9	48.9
Nominal value (£m)	48.9	48.9
Accounting classification	Equity	Equity
Date of issue	02 October 2013	02 October 2013
Perpetual or dated	Perpetual	Perpetual
Maturity date	n/a	n/a
Callable	No	No
Convertible	No	No
Coupon rate and any related index	n/a	n/a

The table below details the nature of amounts deducted due to the application of prudential filters or CRR instructions:

Table 5: Prudential filters and deductions; per CRD IV

	£m
Adjustments to CET1 due to prudential filters in accordance with CRR Articles 32 to 35	
Cash flow hedge reserve	0
	0
Adjustments to CET1 due to deductions in accordance with CRR Articles 36, 56 and 66	
Losses for the current financial year	21
Direct, indirect and synthetic holdings by an institution of own Common Equity Tier 1 instruments	4
Intangible assets	2
	27
Items not deducted in accordance with CRR Articles 47, 48, 56, 66 and 79	
None	0
	0

Table 6: Total minimum pillar 1 capital requirement

	31/12/2016		**31/12/2015**	
	Risk weighted assets	**Pillar 1 capital requirement**	**Risk weighted assets**	**Pillar 1 capital requirement**
	£m	**£m**	**£m**	**£m**
Credit risk*	960	77	1,220	98
Market risk**	7	1	3	0
Operational risk	87	6	81	6
Credit valuation adjustment**	1	0	1	0
Total	**1,055**	**84**	**1,305**	**104**
Capital resources		220		204
Capital resources surplus over Pillar 1 requirement		**136**		**100**

* including counterparty credit risk

** the capital requirment associated with Market Risk and CVA Risk is not considered to be material and therefore no further disclosures of these items are made

5 Capital Adequacy

5.1 Adhering to CRD IV Capital Requirements

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

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.

5.2 Leverage Ratio

Table 7: Leverage ratio

	31/12/2016	31/12/2015
	£m	£m
Tier 1 capital for the leverage ratio		
Total CET1 capital	216	201
Additional Tier 1 capital	0	0
Total Tier 1 capital	**216**	**201**
Exposures for the leverage ratio		
Total statutory assets per the statement of financial position	1,031	1,241
Off balance sheet items (after CCF)	54	82
Exposures deducted from regulatory capital	0	-35
Intangible assets	-2	-2
Leverage ratio exposure	**1,083**	**1,286**
Leverage ratio	**19.94%**	**15.63%**

6 Credit Exposure

BLME's credit exposure arises principally through its lending activities to corporate entities and high net worth individuals, as well as to financial institutions through liquidity and investment activities. It should be noted that the large majority of BLME's lending to corporate entities and private clients is secured. These exposures are well distributed by economic sector and by geography. Geography is primarily determined by country of incorporation or by country of economic activity where this is more appropriate.

The following tables show these exposures net of any credit provisions.

Table 8 - Exposure by Economic Sector & Geographic Region as at 31 December 2016

	Total £m	UK	Other *	MENA	EUROPE	R.O.W.
Central governments or central banks	27	2%	0%	0%	0%	0%
Multilateral development banks	77	0%	7%	0%	0%	0%
International organisations	0	0%	0%	0%	0%	0%
Institutions	19	2%	0%	0%	0%	0%
Corporates (inc SME)	545	38%	0%	8%	0%	1%
Retail	3	0%	0%	0%	0%	0%
Exposures in default	35	2%	0%	1%	0%	0%
Items belonging to high risk categories	245	16%	0%	0%	5%	0%
Short term claims on institutions or corporates	156	5%	0%	5%	1%	4%
Equity exposures	0	0%	0%	0%	0%	0%
Other items	27	3%	0%	0%	0%	0%
Total	**1,134**	**68%**	**7%**	**14%**	**6%**	**5%**

* Supranational

Table 9 - Average Exposure over four quarters in 2016 by Economic Sector

	Average credit risk exposure £m
Central governments or central banks	29
Multilateral development banks	94
International organisations	0
Institutions	15
Corporates (inc SME)	669
Retail	2
Exposures in default	40
Items belonging to high risk categories	295
Short term claims on institutions or corporates	142
Equity exposures	14
Other items	27
Total	**1,327**

The credit exposure to financial institutions tends to be short term. Exposures to Corporate Banking and Private Banking clients are usually longer term, depending on the credit quality of the borrower and the quality of the collateral. A breakdown of residual maturity and economic sector is as follows:-

Table 10 - Exposure by Economic Sector and Maturity as at 31 December 2016

	Total Credit risk exposure £m	Within 1 year £m	More than 1 year but within 5 £m	More than 5 years £m	Undated £m
Central governments or central banks	27	0	21	6	0
Multilateral development banks	77	8	69	0	0
International organisations	0	0	0	0	0
Institutions	19	9	10	0	0
Corporates (inc SME)	545	294	228	18	5
Retail	3	3	0	0	0
Exposures in default	35	12	15	0	8
Items belonging to high risk categories	245	165	47	0	33
Short term claims on institutions or corporates	156	156	0	0	0
Equity exposures	0	0	0	0	0
Other items	27	14	13	0	0
Total	**1,134**	**661**	**403**	**24**	**46**

7 Quality of Credit Portfolio

All counterparties are assigned an annually reviewed credit rating by Credit Risk Management which must be approved by CCRC. Where available, the counterparty credit ratings of major External Credit Assessment Institutions (ECAI's), e.g. Fitch, Moody's etc. are used to supplement the Bank's Internal Rating Methodology.

Table 11 - Credit Exposure by Rating Band as at 31 December 2016

ECAI or BLME Equivalent	£m
AAA+ TO AA-	131
A+ TO A-	218
BBB+ TO BBB-	219
BB+ TO BB-	400
B+ TO B-	50
CCC+ AND BELOW	116
	1,134

Where more than one ECAI rating exists and the ratings differ (i.e. a split rating) BLME will assign the most conservative of the ratings. Where none of the two afore-mentioned ECAI ratings exist BLME assigns its own internal counterparty rating. Overall, 50% of BLME's credit exposure is investment grade or equivalent. Within this, 50% of the portfolio was directly rated by at least one of the ECAI, with the remaining 50% being mapped using internal ratings.

Risk weighted asset values under the Standardised Approach are calculated by reference to six credit quality steps. The table below shows the mapping from the ECAI ratings to the six credit quality steps:

Table 8 - Credit Quality Step

	1	2	3	4	5	6
Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to BB-	B+ to B-	CCC+ and below
Moody's	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to Ba3	B1 to B3	Caa1 and below

The credit quality steps are then mapped to their relevant risk weightings, as follows:

Table 9 - Credit Quality Step

	1	2	3	4	5	6
Corporate	20%	50%	100%	100%	150%	150%
Institution - Maturity 3 months or more	20%	50%	50%	100%	100%	150%
Institution - Maturity 3 months or less	20%	20%	20%	50%	50%	150%
Sovereign	0%	20%	50%	100%	100%	150%

In accordance with the Standardised Approach all credit exposures without an ECAI rating (i.e. credits assigned a BLME Internal Rating) are mapped with a minimum risk weighting of 100%.

8 Counterparty Pre-Settlement Risk

Counterparty pre-settlement risk is very limited. It arises through a small number of Profit Rate Swaps transacted to hedge the fixed rate exposures in Banking Book transactions and a similar number of FX contracts undertaken for either funding purposes or on behalf of clients. In these hedging and funding strategies, BLME uses ECAI investment grade rated banks, for which BLME allocates separate sub-limits. BLME's assessment of pre-settlement risk takes account of the daily mark-to-market of these positions plus a conservative volatility add-on. The latter manages the risk that adverse future changes in market rates could result in higher counterparty risks. The exposures from these transactions are deemed to be immaterial for the purposes of this disclosure.

9 Secondary Credit Exposure through Collateral

BLME has secondary credit exposure as the Corporate Banking 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.

10 Credit and Dilution Risk

10.1 Impairment of Credit Risks

For credit risk management purposes:

- 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.

Every month the CCRC meets 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.

10.2 Impairment Assessment and Provision at 31 December 2016

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 2016 BLME considered it prudent to take impairment charges totalling £18.2m which was partially offset by recoveries of £2.4m.

Table 12

As at 31 December 2016	£m
Exposures considered impaired	58
Impairment provision	23

Table 13 - Past Due Amount by Sector and Geographic Region

	Total £m	Europe	Middle East
Corporates	**1**	**100%**	**0%**
Manufacturing	1	100%	0%
	1	**100%**	**0%**

Table 14 - Charges for Specific and Collective Impairments by Sector

	Total £m	Specific £m	Collective £m
Financial Services	2	2	-
Manufacturing	5	5	-
Real Estate	5	5	-
Transportation and Storage	4	4	-
Others	7	3	4
	23	**19**	**4**

11 Analysis of Credit Exposures and Impairment

All credit exposures are considered for impairment on a specific basis.

12 Credit Risk Mitigation

The Bank has two transactions that have associated guarantees that are utilised as credit mitigation, the effect of which, in the context of its total assets, is not considered to be material to BLME's capital requirement.

13 Non-Trading Book Exposures in Equities

The Bank has only a small number of Private Equity and Venture Capital exposures; these are included as risk weighted assets in the calculation of capital resources.

14 Profit Rate Risk in the Banking Book

These risks principally emanate from the following sources:

- asset and liability rate reset mismatches from Corporate Banking 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.

The 31 December 2016 sensitivity to a standard parallel 100 basis points increase/decrease in the yield curve across all currencies for the Bank's transactional risks is detailed below.

Currency	100bps increase £000's	100bps decrease £000's
GBP	1,217	(1,857)
USD	(1,815)	1,825
EUR	3	(8)
Other	28	(28)
TOTAL	**(567)**	**(68)**

For Pillar 3 purposes only, the transactional base is adjusted for non-profit rate cash balances and enhanced for behavioural assumptions associated with contingent items.

15 Remuneration

BLME is a proportionality level 3 firm under the regulator's Remuneration Code and is required to provide disclosures of both quantitative and qualitative information about decision-making policies for remuneration and links between pay and performance. The following sections of BLME's Pillar III disclosures reflect the requirements of Capital Requirements Regulation (CRR) Part 8 (Article 450).

The tables below show the remuneration awards made by BLME in respect of 2016 and 2015 for employees who have been designated as individuals whose professional activities have a material impact on the risk profile of the Bank.

Table 16: Analysis of Identified Staff – Business Area

	Wealth Management £'000s	Corporate Banking £'000s	Central Functions £'000s	Total £'000s
Total remuneration - 2016	418	790	2,571	3,779
Total remuneration - 2015	159	596	1,949	2,704

Table 17 - Analysis of Identified Staff – Senior Management and Other Staff

	2016 Senior Management £'000s	2016 Other Identified Staff £'000s	2016 Total £'000s	2015 Senior Management £'000s	2015 Other Identified Staff £'000s	2015 Total £'000s
Total remuneration	1,123	2,656	3,779	1,140	1,564	2,704
Number of Identified Staff	8	24	32	4	10	14

Total remuneration consists of base salary, car allowance, pension contributions, discretionary annual bonus and IFRS 2 share scheme costs (which are amortised over the investing period and therefore affect at least three accounting periods).

15.1 Decision Making Process for Remuneration Policy

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 2016 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.

i. Composition of the RemCo

The members of RemCo during 2016 were Neil Holden, Frank Vermeulen, Sheikh Abdullah Jaber Al-Ahmed Al-Sabah and Zeyad Al-Mukhaizeem. Neil Holden is the appointed chairman of RemCo.

ii. Role of the relevant stakeholders

RemCo received independent advice on executive remuneration issues from Mercer during 2016. Benchmarking to market of the Bank's salaries was conducted by independent remuneration advisors.

15.2 Identified Staff Criteria

These individuals can be classified as follows:

- Directors of BLME Holdings
- Non-executive directors of BLME Holdings
- Members of the Bank's Executive Committee
- Other employees deemed to have a material impact on the firm's risk profile through their professional activities (Material Risk Takers)
- Employees not falling into the categories above but remunerated at the same levels as senior management or Material Risk Takers.

15.3 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. 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 does not apply a formulaic approach on the grounds that this may encourage inappropriate risk taking. The annual bonus awarded to an individual is discretionary and dependent on the achievement of objectives. The pay-out levels depend on the performance of the Bank, of constituent business departments and of the individual.

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.

15.4 Long Term Incentives

BLME has an Approved Share Option Plan (ASOP) and an Unapproved Share Option Plan (USOP). Grants made under these schemes are made to eligible staff. In addition, BLME operates a Deferred Annual Bonus Scheme (DABS) under which any bonus in excess of a stipulated threshold is awarded in full or part as nil cost BLME share options. The ASOP, USOP and DABS schemes provide the main incentive tools to align the long term interests of Identified Staff with those of shareholders. Options granted under these schemes vest over a three year period and are subject to good/bad leaver provisions.