



BASEL III, PILLAR 3 DISCLOSURES

Bermuda Commercial Bank Limited | September 30, 2019



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Introduction

Background

The disclosure and analysis provided in this document relate to Bermuda Commercial Bank Limited (“BCB” or “the Bank”) which is incorporated in the island of Bermuda as a limited liability company. It is intended to be read in conjunction with the relevant Annual Audited Financial Report which includes important details about the Bank’s capital adequacy, risk management, and other information. The disclosures are prepared on a consolidated group basis and are not based upon audited financial statements.

BCB’s accounting policies conform to International Financial Reporting Standards (“IFRS”).

The Bank has a banking licence under the Bank and Deposit Companies Act, 1999. These disclosures are solely in the context of the local regulatory requirements and guidelines provided by the Bermuda Monetary Authority (“BMA” or “Authority”) under Pillar 3 “Market Discipline of New Capital Adequacy Framework”. The Pillar 3 disclosures have been designed to complement the minimum capital requirements in Pillar 1 as well as the Supervisory Review and Evaluation Process in Pillar 2. The accepted aim of Pillar 3 is to promote market discipline by allowing market participants access to information of risk exposures and risk management policies and processes adopted by the Bank.

Frequency

The disclosures in this report are required to be updated on a semi-annual basis and more frequently if significant changes to policies are made. This report has been updated as at September 30, 2019 and policies disclosed within are effective at this time. All disclosures are published semi-annually in conjunction with BCB’s annual September 30 financial reporting processes.

Report Conventions

The disclosures in this report are not based upon audited financial statements and have not been audited by an external auditor and there is no requirement for this to be done. However, the disclosures have been prepared on a basis consistent with information submitted to the Authority and at the same level of internal review and internal control process as information provided in the Bank’s financial statement reporting.

Basel II & Basel III

Until the end-December 2015, Bermuda banks were required to follow the Basel II capital adequacy framework, and since January 1, 2016 the Bank has adopted the Basel III framework, of which this disclosure forms a part. This incorporates transitional arrangements until full implementation in 2019. These reforms strengthen capital and liquidity rules with the goal of promoting a more resilient banking sector that is able to absorb shocks arising from economic and financial stress.

BCB monitors its capital position against the Basel III framework and all businesses are operating cognisant of this. New transactions at BCB are also now evaluated on a fully implemented Basel III basis. Basel III seeks to raise the quality, consistency and transparency of the capital base, limit the build-up of excess leverage and increase capital requirements for the banking sector. Basel III adopts Common Equity Tier 1 (“CET1”) capital as the predominant form of regulatory capital as measured by the CET1 ratio. The BMA requires Bermuda banks to maintain a CET1 ratio of at least 7.0% of its Risk Weighted Assets (“RWA”), which is inclusive of a minimum CET1 ratio of 4.5% and a capital conservation buffer of 2.5%. Basel III also introduced the following additional requirements:

- Counter-cyclical buffer of up to 2.5% composed of CET1-eligible capital may be implemented by the BMA when macroeconomic indicators provide an assessment of excessive credit or other pressures building in the banking sector, potentially increasing the CET1, Tier 1 and total capital ratios by up to 2.5%;
- Net Stable Funding Ratio (“NSFR”) with a minimum requirement of 100%, with implementation effective for Bermuda banks from 1 January 2018.

The Basel III rules also address the areas of Leverage and Liquidity.

The Authority has adopted a minimum 5% Leverage Ratio calculated as the ratio of Tier 1 Capital to Total Exposure. The BMA requires Bermuda banks to maintain Tier 1 capital of at least 8.5% of RWA, inclusive of a minimum Tier 1 ratio of 6% and a capital conservation buffer of 2.5%. The BMA also requires Bermuda banks to maintain Total capital of at least 10.5% of RWA, inclusive of a minimum total capital ratio of 8% and a capital conservation buffer of 2.5%. The Bank is currently in excess of this requirement.

The Authority adopted the Liquidity Coverage Ratio (“LCR”) implementation timetable consistent with that published by the Basel Committee beginning on January 1, 2015, with a minimum requirement of 60% rising in equal annual steps to reach 100% on January 1, 2019 which is the present required minimum. The LCR is designed to ensure that banks have a sufficient stock of unencumbered High-Quality Liquid Assets (“HQLA”) to survive a significant liquidity stress scenario lasting 30 days. The LCR is calculated as HQLA divided by total net cash outflows over the period of the next 30 days. Total net cash outflows are calculated in accordance with rules prescribed by the BMA. The Bank is compliant with the LCR 100% ratio requirements.

BCB has adopted the Basic Indicator Approach as being most appropriate for the scale and scope of the Bank’s operations. Accordingly, the Bank agrees its Board of Directors (“Board”) approved Capital Adequacy and Risk Profile (“CARP”) documents with the BMA. BCB’s position at September 30, 2019 exceeds the Basel Committee’s 2019 fully implemented Basel III requirements, i.e. minimum ratios plus capital conservation buffer.

Overview of the Bank

The Bank began by an Act of Parliament in February 1969 and operated under the management of Barclays from its inception until May 1993. A decision was made by Barclays to sell its minority shareholdings worldwide in the early 1990’s and this set the stage for a new shareholder, who would bring a new focus and direction, to acquire the Bank.

In April 2010, the majority shareholding in the Bank was purchased by an investor group through Permanent Investments Limited (“Permanent”). In October 2011, BCB expanded its trust and corporate administration services business through the acquisition of two established Bermuda companies. This was consistent with the Bank’s strategic objectives and overall business goals of creating a full-service financial services institution in Bermuda.

In October 2012, as part of a strategic restructuring, BCB merged with BNL I Limited, a wholly owned subsidiary of Somers Limited (“Somers”, formally known as “Bermuda National Limited” or “BNL”), resulting in BCB becoming a wholly-owned subsidiary of Somers. Somers is a Bermuda exempted investment holding company with investments in the financial services sector and is listed on the Bermuda Stock Exchange (“BSX”). BCB itself delisted from the BSX subsequent to this restructuring.

In November 2015, BCB implemented a state-of-the-art core banking system, along with a suite of products, including internet banking. This allowed the Bank to grow its channel offerings and business lines, as well as providing better reporting and analysis. It also improved the Bank’s exceptional customer service. In June 2016, the BCB Group of Companies moved into a new location at 34 Bermudiana Road, Hamilton, Bermuda.

In 2019, BCB celebrates its 50-year anniversary of providing banking services to Bermuda and internationally.

On 5 February 2019, Somers Limited announced it had entered into an agreement to sell its 100% shareholding of BCB to Permanent Capital Limited. At the time of publication of this Pillar 3 report, this contemplated transaction is in the process of receiving regulatory and governmental approvals.

The management of risk is an important criterion to all users of financial services. The Bank has established a policy of managing its risk by following a conservative policy in balance sheet management. The Bank maintains a conservative leverage ratio, strong liquidity and follows other principles and policies on risk management which are aligned to BMA regulations.

Risk Culture

The risk culture of the Bank and its wholly-owned subsidiaries (“Group”) reinforces its core beliefs and represents the various Board’s and Senior Management’s values for effectively and efficiently managing risk. All of the Group’s Employees are empowered to, and responsible for, credibly challenging any decision-making processes that may conflict with the Group’s risk appetite and risk culture. A strong risk culture promotes an environment where Employees are encouraged to proactively identify, escalate, and mitigate current and emerging risks and issues, with clear understanding of the consequences associated with not doing so.

The Group is committed to acknowledging and responding to risk as the organisation continues to grow and considers offering new products and services, or entering new geographic markets and client relationships.

Scope of Application

The capital adequacy framework implemented in Bermuda apply to BCB and its subsidiaries.

BCB is incorporated in Bermuda with limited liability. The Bank has a number of wholly-owned and controlled subsidiaries. These subsidiaries are subject to consolidation requirements under IFRS and under the capital adequacy framework.

Directly-owned Subsidiary Undertakings

Name	Location
BCB Charter Corporate Services Limited	Bermuda
BCB Paragon Trust Limited	Bermuda
BCB Asset Management Limited	Bermuda
BCB Management Limited	Bermuda
BCB Management Services Limited	Bermuda
Bercom Nominees Limited	Bermuda
VT Strategies Holdings Limited	Bermuda

As at September 30, 2019, these subsidiaries were wholly-owned by BCB, and included in the Bank’s consolidated financial statements.

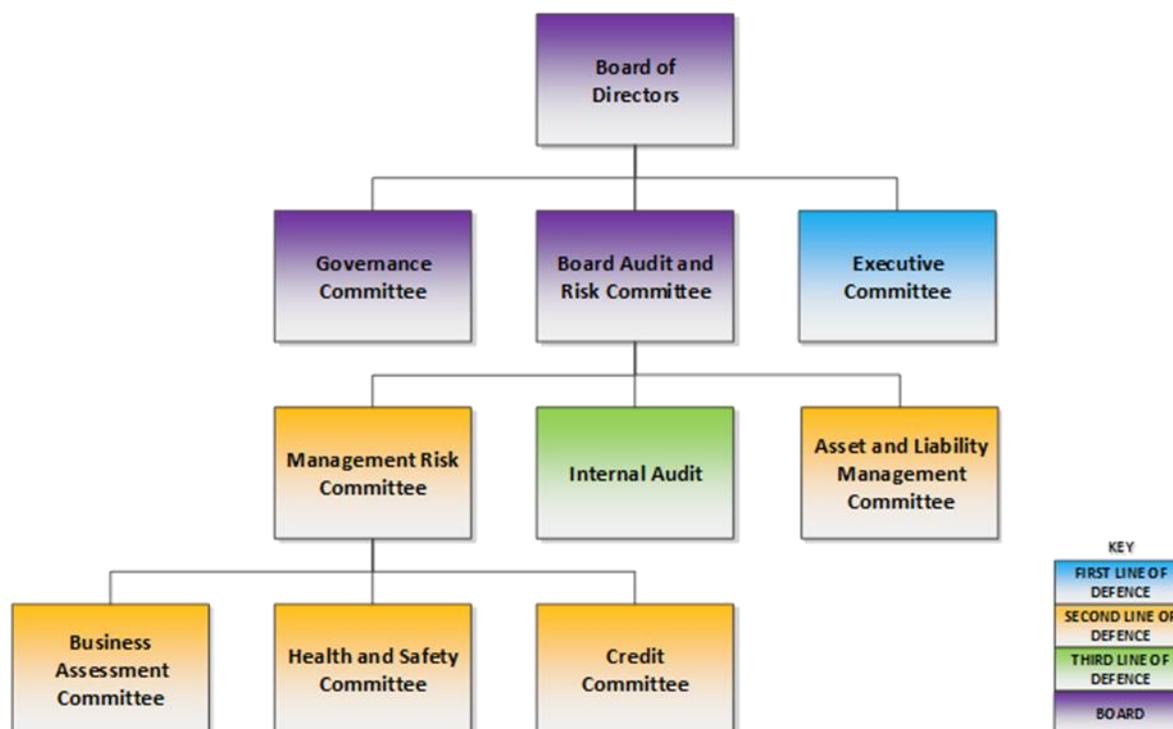
The Group is subject to annual audit, on a consolidated basis, by an external audit firm and the Annual Consolidated Financial Report is published in hard copy and is also available on the BCB website. Further, in respect to various statutory licenses the Bank and its subsidiaries are subject to supervisory oversight and onsite inspection by the BMA.

Risk Management Objectives and Policies

Governance

The management of risk is core to the Bank's activities and its governance structure ensures oversight on an enterprise-wide basis consistent with sound risk management practices. The Board has overall responsibility for maintaining internal controls to ensure that effective risk management and oversight processes operate across the Bank. The Bank's governance and reporting structures are subject to ongoing assessment to ensure they are current and relevant for the risk profile of the Bank.

BCB's Board Governance and Reporting Structure



Board of Directors and Board Committees

The Bank's Board is ultimately responsible for oversight of the Enterprise Risk Management Framework ("ERMF") for the Group, and its alignment with the organisation's objectives and strategies. The Board's oversight responsibilities include understanding the Group's risk exposures, defining its risk appetite, and establishing risk measurement parameters that reflect its risk appetite. The Bank Board oversees Senior Management's implementation of an effective risk management function and internal control system and compliance with the Group's risk management policies by reviewing reports and holding discussions with Senior Management, auditors and other assurance providers on an ongoing basis. On a minimum quarterly basis, the measured performance against the approved Risk Appetite metrics are reported to Management and Board Committees and ultimately to the Board, highlighting those risks that are in breach of agreed limits and status on action plans for any relevant remediation activity.

The Board is responsible for oversight of overall risk management and sets the level of risk tolerance through policy and approval of the Bank's Risk Appetite Statement. It delegates authority for implementing risk control activities to the following Board and Management Committees:

a. The Board Audit and Risk Committee ("BARC")

The BARC is a committee of the Board and is chaired by an independent director. The BARC comprises a majority of independent directors and acts on behalf of the Group Board in fulfilling oversight

responsibilities with respect to financial reporting, high level risk management and related matters of governance including setting the expectations and requirements in relation to Audit and to Risk Management. It has oversight of the external auditor, internal auditor and finance functions of the Bank and provides recommendations to the Group Board on relevant matters. In addition, it reviews the Bank's CARP document annually. The BARC also provides oversight on behalf of the Board on matters relating to the Group's risk exposure, including the definition, oversight, policy setting, measurement and risk mitigation strategies. The responsibilities of the BARC covers all relevant matters set down in its Terms of Reference and as instructed by the Group Board. The BARC quarterly meetings review a comprehensive pack containing detailed reporting received on capital, credit, risk, legal, internal audit and compliance activities throughout the Group. The BARC reviews quarterly status reporting on KPIs aligned with the Group's Risk Appetite Statement.

b. The Governance Committee ("GC")

The GC is a committee of the Board and is chaired by an independent director. The GC comprises a majority of independent directors and acts on behalf of the Group Board in providing oversight of the Group Board Governance Principles and Policy. The GC Terms of Reference define responsibilities for recruitment, retention decisions, remuneration and compensation decisions, *inter alia*. Its remit is to oversee all Human Resources matters, policies and procedures and any other matters concerning employees and Management, including the appointment and performance assessment of and succession planning for members of the Board.

Both the BARC and GC are comprised of a combination of independent and non-independent members representing respective skill sets and experience, and with independent members representing the majority of each committee. Each committee reports to the Board on a minimum quarterly basis. The Group Board approves and reviews regularly the Terms of Reference for each Committee.

Additionally, the Board of the Bank's licensed operating subsidiaries, which include BCB Paragon Trust Limited and BCB Charter Corporate Services Limited, report to the Bank's Board and respective Board committees at least quarterly on the activities of those subsidiaries.

In addition to these Board committees, there are five Management level risk committees: the Executive Committee, the Asset and Liability Management Committee, the Management Risk Committee, the Credit Committee and the Business Assessment Committee, each of which has their own approved Terms of Reference.

The **Executive Committee ("EXCO")** is responsible for the oversight and management, including day-to-day operations and administration, of the Group, within the framework of the Group's policies, its Terms of Reference and such other directives as the Board may determine from time to time in line with role profiles.

The **Asset and Liability Management Committee ("ALCO")** is a Management committee established to oversee the Asset and Liability Management of the Group which is defined in the Asset and Liability Management ("ALM") Policy. ALCO monitors asset deployment limits, including investment limits, in order to monitor and manage the exposure of the portfolio to liquidity, interest rate, foreign currency, counterparty and funding risks, and to ensure that the assets in the Group's balance sheet are consistent with its risk appetite. The ALCO also provides oversight of the Bank's portfolio of financial assets and monitors the Bank's regulatory capital position to ensure adequate capitalisation. ALCO reports into the BARC.

The **Management Risk Committee ("MRC")** is a Management committee established to discuss, identify, monitor, measure and manage risks across business units. The MRC is comprised of Executive and certain Senior Management of the Bank with Terms of Reference that outlines the membership, responsibilities of the committee, and its operating characteristics. The MRC's activities are documented through the preparation of meeting minutes and actions. The MRC has also been delegated responsibilities including, but is not limited to: the reviewing of risk management reports articulating the Group's risk profile, including the monitoring of metrics in the Board-approved Risk Appetite Statement; receiving and reviewing updates on High and Medium-rated incidents and actions which have been identified to close control gaps; actively tracking new emerging risks to ensure that the Group is well placed to address these as they may arise; and approving risk policies and material changes to those policies. The MRC meets on a minimum quarterly basis and reviews a pack containing detailed reporting received on capital, credit, risk, legal and compliance

activities throughout the Bank. MRC is provided a status reporting on Key Performance Indicators (“KPIs”) aligned with the Group’s Risk Appetite Statement.

The **Credit Committee (“CC”)** is a Management committee established to provide authorisations as permitted and oversight of the Bank’s credit portfolio. It also provides guidance in relation to the opening of new account relationships with the Bank and borrowing accounts. The CC ensures credits are underwritten, reviewed and approved in accordance with the Group’s Risk Appetite Statement and Credit policies at pricing commensurate with the level of risk. The CC also has responsibility for the review and approval of expected credit loss (ECL) allowances for loans and investment holdings and any other financial assets qualifying for credit assessment. The CC has approved Terms of Reference and draws its general authorities from the MRC into which it reports.

The **Business Assessment Committee (“BAC”)** is a Management committee established to provide authorisations as permitted, and oversight of BCB’s and its subsidiaries’ client business portfolios. The BAC has approved Terms of Reference and draws its general authority from the MRC into which it reports.

Enterprise Risk Management (“ERM”)

The Group has adopted the Three Lines of Defence Model which addresses how specific duties related to risk and control are assigned and coordinated. This ensures that responsibilities for managing risk are clearly articulated to all levels of the organisation. It also allows Senior Management a clear view to assess whether there are gaps in coverage or a duplication of effort in the management of risk.

The Bank has defined its approach in its Enterprise Risk Management Framework (“ERMF”) which has been reviewed and approved by the Board.

The ERMF defines the Group’s overarching risk framework that ensures an appropriate risk governance structure, disciplines and tolerances are in place to achieve its strategic and business objectives.

The key principles underlying the ERMF are:

- Promotion of a strong risk culture in which risks are identified, assessed and reported in a transparent, consistent, and objective manner. This is accomplished through the establishment and functioning of Group Board and Senior Management committees that have been tasked with overseeing the management of risk and establishing accountability and governance for managing risk within the Group;
- Alignment of the risks undertaken in pursuit of the Group’s strategic and business objectives, through the Risk Appetite Statement and established risk tolerances;
- Rigorous assessment and measurement of risk, ensuring activities remain within the Group’s approved risk appetite through an enterprise risk evaluation process;
- Effective communication and reporting of risk information, such as changes to the risk profile, culture and performance of the Group to demonstrate adequate governance; and
- Monitoring the risk profile of the Group, to ensure the components of an effective ERMF are functioning well over time.

This is based on the concept of Three Lines of Defence.

First Line of Defence (Risk Management by Business Functions)

The First Line of Defence encompasses the controls that the Group has in place to deal with day-to-day business and manages risks in the business, to pre-agreed tolerances or limits. It identifies, manages and monitors risk within each area of the business, reporting and escalating issues as necessary and evidences control.

Business lines (First Line) have primary responsibility for risk decisions, and establishing ownership for the identification, measurement, monitoring and control of risks within areas of accountability. They are required to establish effective governance, and control frameworks for their business areas which are compliant with

Group policy requirements, to maintain appropriate risk management skills and processes to act within the Group's risk appetite parameters set and approved by the Board.

Second Line of Defence (Independent Risk Control)

The Second Line of Defence encompasses the risk oversight function, which is independent of the business and other functions. The second line supports a structured approach to risk management by maintaining and implementing the ERMF and Group-wide risk policies and monitoring their proper execution by the First Line of Defence. It also provides independent advice and oversight on risks relevant to the Group's strategy and activities, maintains an aggregate view of risk, monitors performance in relation to the Group's risk appetite, monitors changes in and compliance with external regulation and promotes best practice.

The Second Line of Defence reports systematically and promptly to the Board and Senior Management about risk management, in particular about perceived new risks or failures of existing controls.

Third Line of Defence (Audit & Governance)

Internal Audit provides independent assurance to the Board through BARC that the First and Second Lines of Defence are both effective in discharging their respective responsibilities. It is responsible for:

- 1) providing an independent and objective assurance activity designed to assist the Group in achieving its objectives;
- 2) evaluating the quality of the Group's risk management processes by conducting reviews in accordance with its audit plan, which is approved by the BARC; and
- 3) examining and evaluating the adequacy and effectiveness of the ERMF and internal controls by performing a broad, comprehensive program of internal auditing.

Findings and conclusions of all internal audits are reported directly to the BARC, as well as to the appropriate levels of management.

Risk Identification, Measurement and Control

The process of identifying risk exposures is key to the success of the risk management process as all other elements of the process flow from this initial step. It is crucial, therefore, that a thorough process of risk identification is accomplished on a regular basis.

The process for risk identification, measurement and control is integrated into the overall framework for risk governance. Risk identification processes are forward-looking to ensure emerging risks are identified. Risks are captured in a comprehensive risk register and measured using robust and consistent quantification methodologies. The measurement of risks includes the application of sound stress testing and scenario analysis and considers whether relevant controls are in place before risks are incurred.

When risks have been identified and assessed, the relevant business areas determine an appropriate method for addressing the risks which have been identified.

The methods of assurance are summarised as follows:

- **Self-review:** Line Management periodically review processes, systems and activities to ensure that all risk management processes continue to be effective and appropriate;
- **Risk review and compliance monitoring:** the purpose is to confirm the continued effectiveness of the management of risk within the business. This includes identification of potential control failures;
- **Internal audit:** as part of an agreed audit programme, internal audit will provide the Group with risk based and timely assurance on important aspects of the group's risk management control frameworks and practices. It is the responsibility of all business heads to provide responses to audit findings that focus on addressing root causes within the agreed timescales; and
- **External audit:** external audit reviews provide stakeholders, the Board, the BARC, business heads, staff and the risk function with an independent assurance over financial reporting.

Enterprise-wide risks

Enterprise-wide risks are those presenting the risk of a financial loss as a result of business activities. These types of risks are calculated and are driven by the Bank's strategy and appetite which are clearly defined and monitored to ensure performance between parameters the business deems acceptable. The following represent a list of the Bank's Enterprise-wide risks:

Risk Name	Definition
Credit and Counterparty risk	The risk to current or anticipated earnings or capital arising from an obligor's failure to meet the terms of any contract with the Group or otherwise perform as agreed.
Market and Interest Rate Risk	Market Risk is the risk of loss in both on and off balance sheet positions arising from movements in market prices. Interest Rate Risk is the risk to earnings or capital arising from movements of interest rates.
Operational Risk	Operational Risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or external events, including legal risks. Operational Risks is an enterprise-wide risk, but has a subset taxonomy of its own.
Liquidity Risk	Liquidity risk is the risk that the Group is unable to meet short term financial demands. This usually occurs due to the inability to convert a security or hard asset to cash without a loss of capital and/or income in the process.
Funding Risk	The risk associated with the impact on a project's cash flow from higher funding costs or lack of availability of funds.
Regulatory Compliance	The risk to current or anticipated earnings or capital arising from violations of laws, rules, or regulations, or from nonconformance with prescribed practices, internal policies and procedures, or ethical standards.
Conduct Risk	The risk that the Group or its Employees conduct themselves in such a way that leads to fines or sanctions or attracts negative media attention to the Group, which leads to a reputational risk.
Capital Risk	Capital risk is the risk that the Bank breaches regulatory capital limits resulting in fines, sanctions or a restriction of its license by the BMA resulting in reputational risk to the Bank.
Strategic and Business risk	The risk that strategic business decisions prove to be ill founded or poorly executed; or that there is a failure to anticipate and react to changes in the general economic environment.
Reputational Risk	Reputational risk is the risk of loss resulting from damages to a firm's reputation, which may manifest in the inability to attract new business, lost revenue, increased operating, capital or regulatory costs, or the destruction of shareholder value.

Risk Management Measurement, Monitoring and Reporting

The process of measuring, monitoring and reporting certain risks is managed independently from business unit managers conducting risk taking activities as per the Three Lines of Defence Model outlined above. Monitoring and reporting on risk taking activities include the following:

- The CC reviews credit risk management reports and monitors compliance with applicable limits. In addition, the CC assists with the development of credit risk mitigation action plans and monitors their implementation, *inter alia*;
- The MRC monitors the Group's operational risk exposures based on reports provided by businesses and functions and consistent with sound risk management practices. The MRC is responsible for operational risk monitoring activities including compliance. The MRC activities include administration and facilitation of the annual risk assessments and operational risk exception analytics and reporting. The Group may also periodically use independent consultants to assess the risk management governance structure and management processes;
- The ALCO reviews market risk management reports and monitors compliance with applicable limits. In addition, ALCO assists with the development of market risk mitigation action plans and monitors their implementation;
- The BARC receives reports from the MRC which independently summarises and reports market, credit, operational and compliance risk results on a quarterly basis. The BARC also receives quarterly reports on the activities of the ALCO, CC, BAC and other topical matters;
- Senior Management reports to the relevant Management and/or Board committees, the Board, and to the BMA on various risk results including any non-compliance issues as and when identified;
- The Treasury Department is primarily responsible for day-to-day liquidity management, including liquidity risk measuring, monitoring and reporting; and
- Internal Audit performs independent audits of the risk management functions to ensure that risk management objectives are achieved. Any enterprise risk management deficiencies noted are reported to Senior Management and the BARC.

In addition to the above, individual risk functions will have specific reporting requirements that are submitted to their relevant oversight committees. These specific reporting requirements are represented in the respective policies.

As the central management risk committee of the Bank, the MRC receives on a minimum quarterly basis comprehensive reports on the Group's enterprise-wide risk management framework, including, where appropriate, information on processes and resources necessary to execute the enterprise-wide risk programme, such as those relating to data aggregation, model governance, and the acquisition, development, and retention of risk talent. The MRC subsequently reports to the BARC providing the output of its reviews, approvals and, as appropriate, recommendations for the BARC approval. The MRC also escalates 'significant' items to the BARC, where 'significant' is defined as breaches of risk appetite limits and/or parameters as set out in the Risk Appetite Framework.

The following presents the scope and main content of regular risk exposure reporting within the MRC remit:

- Management's assessment of the aggregate enterprise-wide risk profile and alignment of the Group-wide risk profile with the strategic plan, goals, objectives and risk appetite, as set by the Board.
- Recommends to the BARC the overall risk tolerance and risk appetite, and reviews amendments to the Bank's Risk Appetite Statement, prior to passing this to the Board for approval.
- Review reports from Management and other Management committees regarding the adherence to risk limits and agreed risk tolerance and risk appetite.

- Approves policies and procedures generated by Management (which, in some cases, may be subject to review and approval by the BARC) to identify, assess, measure, and manage the major risks facing the entities in the group. This addresses credit risk, operational risk, compliance risk, market risk, liquidity risk, strategic and business risk, and reputational risk, as appropriate to the entity, as well as Management's capital management, planning and assessment processes.
- Reviews recommendations on the credit risks associated with the Bank's activities and, where relevant, provides approval with respect to new business initiatives and individual proposals.
- Reviews reports from Management regarding emerging risks and other selected risk topics and/or enterprise-wide risk issues.
- Reviews reports from Management regarding management's assessment of the design effectiveness of the Risk and Control Self-Assessment programme, including corrective actions taken by Management to address issues identified, in order to address control deficiencies and the implementation of risk management enhancements.
- Overseeing the regulatory reporting required to be provided to all applicable regulatory authorities, including the BMA. For the Bank, this includes, but is not limited to, the CARP, Pillar 3 disclosures, stress testing and BASEL III.
- Assess any risk incidents which have occurred in order to ensure that the remaining risk has been suitably mitigated with the actions agreed.

Further details on the risk management framework can be found in the Risk Management section of the Group's September 30, 2018 Annual Report.

Group Code of Conduct and Ethics for Employees and Directors ("Code of Conduct")

The Group has an established Code of Conduct setting out the core culture and expectations of the Group and how these are governed. The Code of Conduct mandates adherence to the standards set by the Group and provides guidance as to disclosure and escalation to ensure transparency and integrity. The Risk Appetite Statement has also established specific tolerance thresholds for Board and Management reporting and oversight for ensuring conformance with approved standards.

Potential adverse risk events are also identified through the Group's annual risk assessment process. Group personnel are responsible for identifying these risk events and potential concerns inherent in the various business activities and processes in which they are involved. These risk events are assessed in the risk assessment.

As part of the Operational Risk Management Policy, the Group has put in place an Operational Risk Incident Management Procedure to identify and document events or situations that have negatively affected the Group's operations or have the potential to adversely impact operations. Group personnel are responsible for promptly reporting incidents and taking corrective action to reduce the likelihood of similar events occurring in the future.

Stress and Scenario Testing

The purpose of stress and scenario testing is to quantify exposure to extreme and unusual market risk occurrences and represent important elements of the Bank's ongoing risk management processes. The Bank's objectives in stress and scenario testing are to review probable outcomes of plausible scenarios. The results of the stress testing are embedded in the strategic planning process and risk appetite to ensure that sufficient capital and liquidity are available at all times to support the Bank's growth plans, as well as to cover its regulatory requirements at all times and under varying circumstances. The Bank's programme also assesses credit and market risks to understand specific weaknesses in the solvency of the Bank. Further, relevant stress scenarios are also factored into the group wide stress scenarios. The feedback and output aid the modelling of a comprehensive control framework that is transparent and responsive to rapidly changing market conditions.

Stress testing is reviewed on at least an annual basis and more often in the event of a material change in capital or liquidity. Ongoing stress testing and scenario analysis outputs are used to inform the formal assessments and determination of required buffers, the strategy and planning for capital and liquidity management and the setting of risk appetite limits.

The Board and Senior Management have engaged in a number of exercises which have considered and developed standard and ad-hoc stress-test scenarios. The output analysis enables Management to evaluate the Group's capital and funding resilience in the face of severe but plausible risk shocks. The stress tests have included a range of Group-wide, multi-risk category stress tests, generic and idiosyncratic financial shocks, and operational risk scenario analyses assessing the impact of these stresses on the Bank's short term liquidity in terms of LCR and long term funding needs as measured by NSFR. Some of these scenarios include, but are not limited to, negative rate shock changes, movements in retail and non-operational deposit balances, and movements in HQLA and investment portfolio. Stress testing is an integral part of the adequacy assessment processes for liquidity and capital, and the setting of tolerances under the annual review of Group risk appetite.

The Bank has implemented a stress testing programme, with stress testing mandated at least annually. The following provides a summary outline of the Bank's programme and represents minimum standard criteria addressing:

- Parallel basis point interest rate decline
- Tiered Credit rating downgrade
- Parallel basis point fixed income securities rate shock (Bonds)
- Pricing decline in equities and funds
- Investment Impairments increases
- Default of a Related Party Exposures
- Top Depositors withdraw
- Major Cyber attack
- Major Regulatory Fine/Sanction

These minimum criteria are subject to review annually as a part of the CARP exercise. Additionally there are a number of Stress Testing scenarios conducted to assess its potential impact to the Bank's regulatory capital, LCR and NSFR, and the results of the stress tests are reviewed by ALCO at each regular meeting.

Key Prudential Metrics

The table below provides an overview of the Bank's key prudential regulatory metrics for the last 5 quarters.

Table 1: Key Metrics (KM1)

		a	b	c	d	e
		30-Sep-19	30-Jun-19	31-Mar-19	31-Dec-18	30-Sep-18
Available capital (amounts)						
1	Common Equity Tier 1 (CET1)	96,148	94,557	96,258	99,341	102,984
1a	Fully loaded ECL accounting model	96,148	94,557	96,258	99,341	102,984
2	Tier 1	96,148	94,557	96,258	99,218	102,861
2a	Fully loaded accounting model Tier 1	96,148	94,557	96,258	99,218	102,861
3	Total capital	96,148	94,557	96,258	99,218	102,861
3a	Fully loaded ECL accounting model total capital	96,148	94,557	96,258	99,218	102,861
Risk-weighted assets (amounts)						
4	Total risk-weighted assets (RWA)	277,007	270,557	272,682	263,519	249,362
Risk-based capital ratios as a percentage of RWA						
5	Common Equity Tier 1 ratio (%)	34.7%	34.9%	35.3%	37.7%	41.3%
5a	Fully loaded ECL accounting model CET1 (%)	34.7%	34.9%	35.3%	37.7%	41.3%
6	Tier 1 ratio (%)	34.7%	34.9%	35.3%	37.7%	41.2%
6a	Fully loaded ECL accounting model Tier 1 ratio (%)	34.7%	34.9%	35.3%	37.7%	41.2%
7	Total capital ratio (%)	34.7%	34.9%	35.3%	37.7%	41.2%
7a	Fully loaded ECL accounting model total capital ratio (%)	34.7%	34.9%	35.3%	37.7%	41.2%
Additional CET1 buffer requirements as a percentage of RWA						
8	Capital conservation buffer requirement (2.5% from 2019) (%)	2.5%	2.5%	2.5%	1.9%	1.9%
9	Countercyclical buffer requirement (%)	0.0%	0.0%	0.0%	0.0%	0.0%
10	Bank D-SIB additional requirements (%)	0.0%	0.0%	0.0%	0.0%	0.0%
11	Total of bank CET1 specific buffer requirements (%)	2.5%	2.5%	2.5%	1.9%	1.9%
12	CET1 available after meeting the bank's minimum capital requirements (%)	27.7%	27.9%	28.3%	31.3%	34.9%
Basel III Leverage Ratio						
13	Total Basel III leverage ratio measure	464,267	493,565	483,262	492,533	485,064
14	Basel III leverage ratio (%)	20.7%	19.2%	19.9%	20.1%	21.2%
14a	Fully loaded ECL accounting model Basel III leverage ratio (%)	20.7%	19.2%	19.9%	20.1%	21.2%
Liquidity Coverage Ratio						
15	Total HQLA	177,529	198,970	172,373	190,155	232,180
16	Total net cash outflow	91,069	93,230	71,255	35,027	96,584
17	LCR ratio (%)	194.9%	213.4%	241.9%	542.9%	240.4%
Net Stable Funding Ratio						
18	Total available stable funding	292,455	295,816	299,636	306,450	305,173
19	Total required stable funding	213,111	211,370	227,772	215,991	204,197
20	NSFR ratio (%)	137.2%	140.0%	131.6%	141.9%	149.5%

All amounts in '000's

In accordance with the BMA Basel III for Bermuda Banks - Final Rule - November 2017, the Capital Conservation Buffer requirement increased to 2.50% on 1st January, 2019 which has been reflected in the metrics above. The Bank's Common Equity Tier 1 over the past reporting period has contracted due to a combination of increased risk weighted assets and as a consequence of the challenging global markets negatively impacting performance of the investment portfolio. The Bank's operational expenses have reported under budget throughout the reported fiscal year which partly offset the weaker investment results.

Capital and Risk Weighted Assets

Capital Management

Sufficient capital must be in place to support business activities, according to both the Bank's internal assessment and the requirements of the Bermuda Monetary Authority.

BCB's goal is to maintain sound and optimal capital ratios at all times. The Bank constantly reviews the current position and projected developments in both its capital base and capital requirements. The main source of the Bank's supply of capital is shareholder investment and retained earnings.

The capital management process is based on the following steps:

- The monitoring of the regulatory capital and ensuring that the minimum regulatory requirements and the established internal targets are met.
- The estimation of the capital requirements based on ongoing forecasting and strategic planning.
- The reporting of the regulatory capital situation to the Board, Senior Management Team and the BMA.

Responsibility for overseeing these steps is vested with ALCO and MRC.

Regulatory Capital Framework

The regulatory capital framework for banks in Bermuda is based upon three 'pillars' which are summarised below:

- **Pillar 1 - Minimum capital requirements:** defines the minimum capital requirements that banks are required to hold for credit, market and operational risks.
- **Pillar 2 - Supervisory review process:** includes a requirement for firms to undertake an internal CARP process. The CARP represents the aggregated view of the material risks faced by the Group, and is used by the Board and Management to understand the levels of capital required to be held over the planning horizon to cover these risks and to withstand a range of adverse stress scenarios. The CARP is presented to BARC before presentation to the Board for challenge and approval and then submitted to the BMA. The BMA assesses the Bank's CARP to determine adequacy against capital standards under the Basel framework providing a final capital requirement and imposing any supervisory discretion in increasing regulatory capital requirements based on the risk factor assessments.
- **Pillar 3 - Market discipline:** aims to improve market discipline by requiring banks to publish information on their principal risks, capital structure and risk management in order to provide more transparency to market participants.

Capital Structure

The capital structure of the Bank comprises of Tier 1 capital which includes share capital, retained earnings, share premium, less goodwill and intangibles. The Bank does not carry any Tier 2 capital.

Capital ratios for Tier 1 and Total Capital of BCB as at September 30, 2019 are set out below.

Table 2: Composition of regulatory capital (CC1)

	a	b	
	Amounts	Source based on reference numbers/letters of the balance sheet under the regulatory scope of consolidation	
Common Equity Tier 1 capital: instruments and reserves			
1	Directly issued qualifying common share (and equivalent for non-joint stock companies) capital plus related stock surplus	38,939	(c)
2	Retained earnings	58,352	(d)
6	Common Equity Tier 1 capital before regulatory deductions	97,291	
Common Equity Tier 1 capital regulatory adjustments			
8	Goodwill (net of related tax liability)	1045	(a)
9	Other intangibles other than mortgage servicing rights (net of related tax liability)	97	(b)
28	Total regulatory adjustments to Common Equity Tier 1	1143	
29	Common Equity Tier 1 capital (CET1)	96,148	
Additional Tier 1 capital: regulatory adjustments			
45	Tier 1 capital (T1= CET1 + AT1)	96,148	
58	Tier 2 capital (T2)	-	
59	Total regulatory capital (TC = T1 + T2)	96,148	
60	Total risk-weighted assets	277,007	
Capital ratios and buffers			
61	Common Equity Tier 1 (as a percentage of risk-weighted assets)	34.7%	
62	Tier 1 (as a percentage of risk-weighted assets)	34.7%	
63	Total capital (as a percentage of risk-weighted assets)	34.7%	
64	Institution specific buffer requirement (capital conservation buffer plus countercyclical buffer requirements plus higher loss absorbency requirement, expressed as a percentage of risk-weighted assets)	2.5%	
65	Of which: capital conservation buffer requirement	2.5%	
68	Common Equity Tier 1 (as a percentage of risk-weighted assets) available after meeting the bank's minimum capital requirement.	27.7%	

All amounts in '000's. The references (a), (b), (c), (d) and (e) identify balance sheet components that are used in the calculation of regulatory capital – refer to Table 3

As at September 30, 2019, the CET1, Tier 1 and total capital ratios of the Bank all stood at 34.7%. The CET1 available after meeting the Bank's combined 4.5% minimum capital and 2.5% capital conservation buffer requirements stood at 27.7%.

BCB's capital ratios are above both the regulatory minimum capital ratios required by the BMA, and the Board imposed internal minimum capital requirement. There have been no material changes from the prior period.

Table 3: Reconciliation of regulatory capital to balance sheet (CC2)

	a	b	c
	Balance sheet as in published financial statements	Under regulatory scope of consolidation	Reference
	30-Sep-19	30-Sep-19	
Assets			
Cash and cash equivalents	147,852	71,892	
Receivable from related parties	166	166	
Interest receivable	3,150	3,150	
Other assets	2,156	2,156	
Loans and advances to customers	27,511	24,012	
Financial investments	261,360	340,819	
Derivative financial instruments	152	152	
Property, equipment and computer Software	16,973	16,973	
Goodwill and customer relationships (Intangible Assets)	1,143	1,143	
Of which: goodwill	1,045	1,045	(a)
Of which: intangibles (excluding MSR's)	97	97	(b)
Total assets	460,464	460,464	
Liabilities			
Deposits	352,472	352,472	
Customer drafts payable	50	50	
Other liabilities	7,429	7,429	
Interest payable	3,004	3,004	
Total liabilities	362,955	362,955	
Shareholders' equity			
Capital Stock	16,808	16,808	
Of which: amount eligible for CET1	16,808	16,808	(c)
Share Premium	22,131	22,131	
Of which: amount eligible for CET1	22,131	22,131	(c)
Retained Earnings	58,352	58,352	(d)
Accumulated OCI	218	218	
Total shareholders' equity	97,509	97,509	

All amounts in '000's. The references (a), (b), (c), (d) and (e) identify balance sheet components that are used in the calculation of regulatory capital – refer to Table 2

There have been no material changes from the prior period.

The Bank excludes Other Comprehensive Income (“OCI”) from the regulatory capital reporting however this is represented in Table 3 for the purpose of reconciliation.

Table 4: Differences between accounting and regulatory scopes of consolidation and mapping of financial statement categories with regulatory risk categories (LI1)

	a	b	Carrying values of items:			
			c	d	e	g
	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	Subject to credit risk framework	Subject to counterparty credit risk framework	Subject to the securitisation framework	Not subject to capital requirements or subject to deduction from capital
Assets						
Cash and cash equivalents	147,852	71,892	71,892	-	-	-
Receivable from related parties	166	166	166	-	-	-
Interest receivable	3,150	3,150	3,150	-	-	-
Other assets	2,156	2,156	2,156	-	-	-
Loans and advances to customers	27,511	24,012	24,012	-	-	-
Financial investments	261,360	340,819	340,819	-	1,923	-
Derivative financial instruments	152	152	-	433	-	-
Property, equipment and computer Software	16,973	16,973	16,973	-	-	-
Goodwill and customer relationships (Intangible Assets)	1,143	1,143	-	-	-	1,142
Total Assets	460,464	460,464	459,169	433	1,923	1,142
Liabilities						
Deposits	352,472	352,472	-	-	-	352,472
Customer drafts payable	50	50	-	-	-	50
Other liabilities	7,429	7,429	-	-	-	7,429
Interest payable	3,004	3,004	-	-	-	3,004
Total Liabilities	362,955	362,955	-	-	-	362,955

All amounts in '000's

The main differences between the carrying values under regulatory scope and as reported in the financial statement are due to:

- the reporting of HQLA maturing in next 90 days is included within Cash & Cash Equivalents rather than under Financial Investments in the financial statements;
- the loan portfolio is allocated differently between Loans & Advances versus Financial Investments; and
- securitisations are included under credit risk and securitisation risk.

Table 5: Main sources of differences between regulatory exposure amounts and carrying values in financial statements (LI2)

	a	b	c	d	e
	Total	Credit risk framework	Securitisati on framework	Counterpart y credit risk framework	Market risk framework
1 Asset carrying value amount under scope of regulatory consolidation (as per template LI1)	459,322	459,169	1,923	433	-
2 Liabilities carrying value amount under regulatory scope of consolidation (as per template LI1)	0	-	-	-	-
3 Total net amount under regulatory scope of consolidation	459,322	459,169	1,923	433	-
4 Off-balance sheet amounts	56,504	4,002			433
9 Exposure amounts considered for regulatory purposes	515,826	463,170	1,923	433	433

All amounts in '000's

The regulatory carrying amount excludes items subject to capital deductions and items not subject to capital requirements. Other differences are due to items being included in multiple risk framework categories and some items in the credit risk framework being excluded from the total as these are not included for regulatory purposes e.g. goodwill.

Risk Weighted Assets (“RWA”)

RWA are a risk based measure of exposures used in assessing overall capital usage of the Bank. When applied against eligible regulatory capital the Bank’s overall capital adequacy is determined. RWA are calculated in accordance with BMA Prudential Standards. The Bank’s total RWA as at September 30, 2019 is set out below.

Table 6: Overview of Risk Weighted Assets (OV1)

	a	b	c
	RWA		Minimum capital requirements
	30-Sep-19	30-Jun-19	30-Sep-19
1 Credit risk (excluding counterparty credit risk)	215,228	211,026	17,218
2 Of which: standardised approach (SA)	215,228	211,026	17,218
6 Counterparty credit risk (CCR)	943	862	75
7 Of which: standardised approach for counterparty credit risk	943	862	75
16 Securitisation exposures in the banking book	1,857	2,001	149
19 Of which: securitisation standardised approach (SEC-SA)	1,857	2,001	149
20 Market risk	2,575	263	206
21 Of which: standardised approach (SA)	2,575	263	206
24 Operational risk	56,404	56,404	4,512
27 Total	277,007	270,557	22,161

All amounts in '000's

The Minimum Capital Requirements column in Table 6 refers to only Pillar 1 capital which also includes a Capital Conservation Buffer of 2.5%.

The decrease in risk weighted assets over the prior period was driven primarily by lower interbank placements as a consequence of decreased deposit funding.

Leverage Ratio

The Basel III framework introduced the leverage ratio as a non-risk based measure to supplement the risk based capital requirements. As at September 30, 2019, the leverage ratio of the Bank was 20.7% representing an improvement from the prior quarter ratio of 19.2%, each of these well in excess of the BMA leverage ratio framework requirement of minimum 5.0%.

The below table provides a reconciliation of the accounting assets and the leverage denominator.

Table 7: Summary comparison of accounting assets vs. leverage ratio exposure (LR1)

	30-Sep-19
1 Total consolidated assets as per published financial statements	460,465
Adjustment for fiduciary assets recognised on the balance sheet pursuant to the operative accounting framework but excluded from the	
3 leverage ratio exposure measure	(1,143)
4 Adjustments for derivative financial instruments	943
Adjustments for off-balance sheet items (ie conversion to credit	
6 equivalent amounts of off-balance sheet exposures)	4,002
8 Leverage ratio exposure measure	464,267

All amounts in '000's

Table 8: Leverage ratio common disclosure template (LR2)

		a	b
		30-Sep-19	30-Jun-19
On-balance sheet exposures			
1	On-balance sheet exposures (excluding derivatives and securities financing transactions (SFTs), but including collateral)	460,465	489,899
2	(Asset amounts deducted in determining Basel III Tier 1 capital)	(1,143)	(1,197)
3	Total on-balance sheet exposures (excluding derivatives and SFTs)	459,322	488,702
Derivative exposures			
4	Replacement cost associated with <i>all</i> derivatives transactions (where applicable net of eligible cash variation margin and/or with bilateral netting)	433	412
5	Add-on amounts for PFE associated with <i>all</i> derivatives transactions	510	450
11	Total derivative exposures	943	862
Securities financing transactions			
12	Gross SFT assets (with no recognition of netting), after adjusting for sale accounting transactions	4,002	4,001
16	Total securities financing transaction exposures	4,002	4,001
Capital and total exposures			
20	Tier 1 capital	96,148	94,557
21	Total exposures	464,267	493,565
Leverage ratio			
22	Basel III leverage ratio	20.7%	19.2%

All amounts in '000's

Note: The basis for Leverage ratio disclosures is as at quarter end.

The increase in the leverage ratio over the past quarter has been the result of a decrease in the balance sheet driven by decreased depositor funding.

Credit Risk

Overview

Credit or Counterparty Risk refers to the risk that a counterparty or associated party with whom the Bank has contracted to meet its obligations might fail to discharge their contractual obligations as they fall due causing a loss of the Bank's assets through the consequent reduction in earnings and/or value. Credit risk across the group arises mainly through the lending and treasury activities of the Group. This risk exists where there is any transfer of value from the Bank to other parties, be it in the shape of a loan or a deposit. The Bank manages and controls credit risk by setting policy limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank offers some loan and other credit facilities to clients, but is primarily exposed to credit risk through:

- (i) the placement of funds with other banks. The size of these deposits is limited and controlled by both the Bank's internal risk policies and by the Large Exposure limits stipulated by the BMA. All counterparty banks must be approved by the Bank's ALCO. The maximum amount that may be deposited with any single bank or money market fund is governed by a number of controlling variables within the Bank's ALM Policy including, inter alia, the external credit ratings for that bank. Counterparty banks with a rating lower than single-A are not generally used to place deposits. These limits will be reviewed periodically and will be adjusted as the capital of the Bank changes or if the rating of a counterparty bank falls below the single-A level.
- (ii) its portfolio of financial investments.

The Bank's internal policies are designed to create a well-diversified and controlled balance sheet by limiting investments or placement by counterparty, currency, geography and industry. The Bank remains compliant with the Large Exposure limits required by the BMA and places no more than the equivalent of 25% of its capital in any single fund or instrument.

Credit Risk - Loans

Credit risk is managed through the Risk Management department, headed by the Chief Risk Officer ("CRO"), who holds overall responsibility for the management of the credit policy and processes as delegated. The Credit activities of the Bank are detailed within the Bank's comprehensive Credit Manual which presents the specific Credit related policies and procedures.

The Bank's Credit framework comprising policies, procedures and processes are based on sound lending practices and will be continuously updated and enhanced as the Bank credit appetite and relevant functions, local regulations and/or international banking and lending standards are introduced and approved by the Bank's governance structure. The Bank consistently conforms to all statutory, regulatory, policy and prudential requirements in maintaining an adequately controlled credit risk environment which includes:

- a well-documented strategy for assuming credit risk, with sound and prudent relevant policies and processes;
- well defined criteria for approving new exposures (and for renewing and refinancing existing exposures) and establishing appropriate levels of authority for approving exposures, reflective of their size and complexity;
- effective segregation between the front line Credit Underwriting and independent Second Line Credit Risk Management functions in dealing with all credit matters;
- effective administration policies and processes, including continuing analysis and assessment of borrowers' ability to meet their obligations, monitoring of documentation (including legal covenants, contractual requirements and collateral), and a credit classification system that takes into account off-balance-sheet transactions and is suited to the nature, size and complexity of the institution's activities;

- comprehensive policies and processes for ongoing reporting of credit exposures;
- prudent lending controls and limits, including policies and processes for monitoring exposures in relation to limits and for dealing with approvals against limits and exceptions to limits;
- policies and procedures that include potential future exposure (having regard to the nature of individual products or transactions and the size or complexity of the institution itself) in identifying, measuring, monitoring and controlling counterparty credit exposure;
- policies and procedures for aggregating, monitoring and reporting total indebtedness of counterparties;
- early identification of deteriorations in asset quality, for determining institutions' provisioning decisions, for ongoing monitoring of problem assets, for assessing the value of risk mitigants, including guarantees and collateral (reflecting net realisable value), for collecting on past due obligations, and for determining write-offs, having regard to realistic repayment and recovery expectations; and
- Policies designed to ensure that the Bank's credit decisions are free of conflicts of interest, commercially prudent, and that the terms and conditions attached to any lending, and in particular Related Party situations, are conducted at a fully arm's length basis.

Individual credit authority for loans are specified under the Bank's Delegation of Authority Policy and granted to certain Executive Management. Exposures in excess of the specified individual limits require the authorisation of the Bank's CC which also has oversight of the ongoing review of loan credit activity, establishing credit policies and procedures and approving credit structures. The Bank's Credit mandate is defined within the Board approved Risk Appetite Statement which comprises a core documentation of tolerances under the Bank's Enterprise Risk Management Framework. The CC also reviews related party and large credit exposures reported or escalated to the BARC as appropriate and in accordance with the Bank's credit policy requirements. The Bank's Treasury manages the counterparty bank relationships within the provisions of the ALM Policy. Counterparty risk is reviewed by ALCO and MRC in the regular meetings.

All credit exposures undertaken by the Bank are risk rated during the process of approval in accordance with an approved risk ratings schedule. In accordance with policy, all credit exposures shall be subject to periodic reviews, at minimum annually, and upon each review the risk ratings shall be considered for update. Periodic reviews require the consent of the CRO or the CC depending upon prescriptive parameters.

Consistent with the Bank's Three Lines of Defence Model, the Bank's Credit Function is subject to periodic review by the Group's Internal Auditor to test structural and control effectiveness. Issues identified in the course of internal audit reviews are presented initially for Management to address and, where required, provide action plans to remediate. The final report is presented to the BARC which provides oversight to ensure implementation of improvements agreed.

Credit Risk Concentrations

Concentration Risk is the risk posed to a financial institution by any single or group of exposures which have the potential to produce losses large enough to threaten the ability of the institution to continue operating as a going concern.

The management of concentration risk is addressed by the Bank's Related Party Transaction Policy and related credit guidelines, which require that credit facilities to entities that are linked or affiliated through common ownership or management to be aggregated for large exposure reporting purposes. The Risk Management Department monitors the large exposures and reporting on these to the CC, the MRC and the BARC.

The Bank also monitors concentrations with connected parties which arises where two or more individual counterparties are connected with each other in such a way that the financial soundness of any of them may affect the financial soundness of the other.

Further information on the credit risk concentrations and mitigation techniques may be found in the section on Related Parties Disclosures in the Group's September 30, 2018 Annual Report.

Sectoral Concentration

In the advancement and monitoring of credit facilities the Bank is considerate of the location of both the borrower and any underlying asset in the context of both sectoral concentration and accessibility to borrower and collateral.

Country Risk

In addition to monitoring and controlling individual counterparty concentrations, and in accordance with requirements set by the Bank's Risk Appetite Statement, the Bank may conduct periodic monitoring of the aggregate composition of its credit portfolio to ensure no excessive concentrations to individual (or linked) economic sectors, geographical areas or regions, or currencies. The Bank's credit portfolio is substantially directed to Bermuda based borrowers and element of which reflects underlying exposure to international publicly traded securities.

Credit Risk Exposures

The table below details the BCB consolidated regulatory credit risk exposures based upon the BMA Revised Framework for Regulatory Capital Assessment guidance as at September 30, 2019.

Table 9: Credit quality of assets (CR1)

		a		c	d		e	f	g
		Carrying values of			Allowances/ impairments	Of which ECL accounting provisions for credit losses on SA exposures			
		Defaulted exposures	Non-defaulted exposures			Allocated in regulatory category or Specific	Allocated in regulatory category or General		Of which ECL accounting provisions for credit losses on IRB exposures
1	Loans	132	27,477	(98)	(98)				27,511
2	Debt securities	442	304,580						305,022
3	Other investments	-	32,299	-					32,299
4	Off-balance sheet exposures	-	5,465	-					5,465
5	Total	574	369,821	(98)	(98)	0	0	0	370,296

All amounts in '000's

Impairment Allowances for Debt Securities are included within OCI as required in accordance with IFRS 9.

Table 10: Breakdown by Geographical Area

Asset classes	North & South America	Europe	Asia & Middle East	Other	Total
Cash and cash equivalents	132,987	13,951	-	915	147,852
Receivable from related parties	166	-	-	-	166
Interest receivable	1,120	1,857	132	41	3,150
Other assets	2,156	-	-	-	2,156
Loans and advances to customers	19,335	-	-	8,176	27,511
Financial investments	112,861	138,106	8,339	2,054	261,360
Derivative financial instruments	114	39	-	-	152
Property, equipment and computer Software	16,973	-	-	-	16,973
Goodwill and other intangible assets	1,143	-	-	-	1,143
Total	286,855	153,953	8,471	11,186	460,465

All amounts in '000's

Table 11: Breakdown by Industry

Asset classes	Consumer Staples	Energy	Financials	Health Care	Industrials	Information Technology	Materials	Other	Retail	Utilities	Total
Cash and cash equivalents	-	-	147,852	-	-	-	-	-	-	-	147,852
Receivable from related parties	-	-	166	-	-	-	-	-	-	-	166
Interest receivable	47	211	2,447	64	102	18	97	0	4	160	3,150
Other assets	-	-	-	-	-	-	-	2,156	-	-	2,156
Loans and advances to customers	-	-	23,887	-	1,879	-	-	167	1,578	-	27,511
Financial investments	4,175	16,879	183,120	2,868	8,587	5,086	7,486	24,523	-	8,637	261,360
Derivative financial instruments	-	39	114	-	-	-	-	-	-	-	152
Property and equipment	-	-	-	-	-	-	-	16,973	-	-	16,973
Goodwill and other intangible assets	-	-	-	-	-	-	-	1,143	-	-	1,143
Total	4,223	17,129	357,585	2,932	10,568	5,103	7,583	44,963	1,582	8,797	460,465

All amounts in '000's

A Breakdown of Residual Maturity table may be found in the Risk Management section of the Group's September 30, 2018 Annual Report.

Table 12: Credit impaired exposures by Geographic areas

	North & South America	Europe	Asia & Middle East	Other	Total
Gross Carrying amount	555	3	-	20	578
ECL allowances	32	66	-	20	117
Write-offs in year	-	-	-	-	-

All amounts in '000's

The ECL allowance of credit impaired assets could be higher than the gross carrying value as the gross carrying value represents the recoverable value as at September 30, 2019 while the ECL allowance represents the value reduction compared to the amortised cost of those assets.

Table 13: Credit impaired exposures by Industry

	Consumer Staples	Energy	Financials	Health Care	Industrials	Information Technology	Materials	Other	Retail	Utilities	Total
Gross Carrying amount	3	422	-	-	-	20	-	-	134	-	578
ECL allowances	66	29	-	-	-	20	-	-	3	-	117
Write-offs in year	-	-	-	-	-	-	-	-	-	-	-

All amounts in '000's

Table 14: Age analysis of Past due exposures

Past due age analysis:	0-30 days	30-60 days	60-90 days	>90 days	Total
Loans				132	132
Debt securities				422	422
Total	-	-	-	554	554

All amounts in '000's

There are some investments and loans which have been restructured however these balances are not material to the Bank.

The table below presents the mapping between the primary ECAI used by the Bank and the credit quality steps assigned to determine the risk-weightings to calculate the credit risk requirement for respective rated counterparties. Where no external rating is available the exposures are assigned risk weightings as prescribed in the BMA's regulatory guidance.

Table 15: ECAI Mapping (CRD)

Credit quality step	S&P assessment	Moody's assessment	Fitch's assessment
Step 1	AAA to AA-	Aaa to Aa3	AAA to AA-
Step 2	A+ to A-	A1 to A3	A+ to A-
Step 3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-
Step 4	BB+ to BB-	Ba1 to Ba3	BB+ to BB-
Step 5	B+ to B-	B1 to B3	B+ to B-
Step 6	CCC+ and below	Caa1 and below	CCC+ and below
Step 7	NR	NR	NR

The following tables present the standardised portfolio exposure asset classes assigned to the respective credit quality steps:

Table 16: Sovereign Exposure Mapping (CRD)

Credit quality step	Risk weighting %	Exposure value
1	0%	147,739
2	20%	23,151
3	50%	-
4,5&7	100%	-
6	150%	-
Total		170,890

All amounts in '000's

Table17: Corporate Exposure Mapping (CRD)

Credit quality step	Risk weighting %	Exposure value
1	20%	5,083
2	50%	3,033
3,4&7	100%	101,132
5&6	150%	-
Total		109,248

All amounts in '000's

Table 18: Banks & Securities Firms Exposure Mapping (CRD)

Credit quality step	Risk weighting %	Exposure value
1	20%	4,437
2	20% - 50%	57,383
3&7	20% - 50%	38,000
4&5	50% - 100%	23,367
6	150%	-
Total		123,187

All amounts in '000's

Table 19: Securitisations Exposure Mapping (CRD)

Credit quality step	Risk weighting %	Exposure value
1	20%	-
2	50%	132
3&7	100%	1,791
4	350%	-
Total		1,923

All amounts in '000's

Impairment of Financial Assets

Effective October 1, 2018, the impairment of debt instruments is estimated in accordance with IFRS 9 – *Financial Instruments*. Under IFRS 9, the recognition of impairment no longer depends on a reporting entity first identifying a credit loss event but instead uses a more forward-looking approach to recognise expected credit losses (“ECL”) for all debt-type financial assets that are not measured at fair value through profit or loss (FVTPL). ECL allowances applicable to financial assets measured at amortised cost (“AC”) are deducted from the gross carrying value of the respective financial asset while the ECL allowances applicable to financial assets measured at fair value through other comprehensive income (“FVOCI”) are recognised in the Consolidated Statement of Other Comprehensive Income (“OCI”). The movements in ECL allowances are recognised in the Consolidated Statement of Income.

ECL allowances are a probability-weighted estimate of credit losses that are expected to arise over the life of the asset (the lifetime expected credit loss), unless there has been no ‘significant increase in credit risk’ since origination. Accordingly, for loans and advances and financial investments, an assessment is performed at the end of each reporting period to evaluate whether a financial instrument’s credit risk has increased significantly since its initial recognition.

Financial assets and loan commitments are categorised into the following groups based on the above assessment.

Stage 1 includes debt instruments where there has not been any significant increase in credit risk since initial recognition. For financial instruments under stage 1, an allowance is required for ECLs resulting from default events that are possible within the next 12 months from the reporting date (i.e. 12 Months ECL).

Stage 2 includes debt instruments where there has been a significant increase in credit risk since initial recognition on an individual or collective basis. For instruments under stage 2, an allowance is required for ECLs resulting from all possible default events over the expected life of the instrument (i.e. Lifetime ECL).

Stage 3 includes debt instruments that are credit-impaired due to objective evidence of impairment. For instruments under Stage 3, an allowance is required to reduce the carrying value of the asset to its recoverable value.

Originated credit impaired: Originated credit impaired assets (if any) are financial assets that are credit impaired on initial recognition. They are recorded at fair value at initial recognition and interest income is subsequently recognised based on a credit-adjusted effective interest rate (“EIR”). ECLs are only recognised or released to the extent that there is a subsequent change in the expected credit losses.

- ECL allowances for accounts receivable are estimated based on the simplified approach allowed in IFRS 9.
- The ECL allowance is an estimate and may vary from the actual losses. This is because, the provisioning under IFRS 9 is subject to various forward-looking assumptions such as the probability of default (PD), exposure at default (EAD) and loss given default (LGD). Due to the volatility, the inputs and the assumptions are continuously reviewed as new information is available, and the impact to the income statement and the retained earnings are quantified as required by IFRS.

Recognition of Interest Income from debt instruments

Interest income is recognised in the Consolidated Statement of Income for all interest bearing instruments measured at AC and FVOCI, on the accrual basis, using the effective interest rate method. Effective October 1, 2018, the interest income from financial assets that are classified as Stage 3 for ECL purpose, is calculated by applying the effective interest rate to the net carrying value of the asset, which is the gross carrying amount less the applicable provision for ECL.

Difference in accounting and regulatory treatment

For accounting purposes, a financial asset is treated as “past due” when a counterparty has failed to make a payment when contractually due. The past due period is one of the several parameters considered in assessing whether there is a significant increase in credit risk to warrant an ECL allowance under IFRS 9. Therefore, an accounting provision may be required even when the financial asset is not past due. In contrast, under regulatory rules, a financial asset is treated as past due when the payment is ninety days past the contractual due date.

The impairment provisions shown below are the accounting values as reported in the Bank’s management accounts at September 30, 2019.

Table 20: Changes in stock of defaulted loans and debt securities (CR2)

	30-Sep-19
1 Defaulted loans and debt securities at the end of the previous reporting period	1,155
2 Loans and debt securities that have defaulted since the last reporting period	20
3 Returned to non-default status	12
4 Amounts written off	0
5 Other changes	(590)
6 Defaulted loans and debt securities at the end of the reporting period	574

All amounts in '000's

The movement in defaulted loans and debt securities primarily relate to regular settlements of loans & advances, market price movements and disposals applicable to debt securities.

Troubled Debt Restructure

A Troubled Debt Restructure (“TDR”) occurs when the Bank grants a concession due to economic or legal reasons related to the financial position of a credit facility under the following conditions:

- The debtor must be experiencing financial difficulties;
- The creditor must grant a concession in consequence of the debtor’s financial difficulties.

A TDR may be either performing or non-performing at the time of restructure. TDR situations present the Bank with extraordinarily cumbersome obligations and costs, both expense and capital, and are instituted only as a final alternative and apply the basic tenets for Non-Performing Loans.

The Bank has not restructured any facilities during the period.

Credit Risk Mitigation

The following table reports the split between the Bank's secured and unsecured exposures as at September 30, 2019.

Table 21: Credit risk mitigation techniques - overview (CR3)

	a	b	c	d	e	f	g
	Exposures unsecured: carrying amount	Exposures secured by collateral	Exposures secured by collateral of which: secured amount	Exposures secured by financial guarantees	Exposures secured by financial guarantees, of which: secured amount	Exposures secured by credit derivatives	Exposures secured by credit derivatives, of which: secured amount
1	Loans	16,569	10,942	10,942	-	-	-
2	Debt securities	297,154	7,868	7,868	-	-	-
3	Total	313,723	18,810	18,810	-	-	-
4	Of which defaulted	5	1,133	1,133	-	-	-

All amounts in '000's

There has been no material change in loan exposures which have reflected net new financing advanced during the reporting period offset by scheduled term loan repayments and unscheduled prepayments. The increase in the debt securities was driven by the funding sourced through the Bank's customary business cycles and within exposure levels stipulated by the ALM Policy.

The effective management of credit risk in the Bank's loan book is addressed by relevant credit underwriting policies and guidelines and the key assessment of the ability of a borrower to service the obligation. In addition, the Bank operates a robust and effective oversight and past due management process. The majority of the Bank's lending is secured as a secondary source of repayment of the debt if the borrower defaults. For residential property loans, the Bank takes a first mortgage collateral position on the respective property supported by appropriate valuations using Bank approved independent firms of qualified valuers. Throughout the outstanding term of all exposures secured by real estate property, valuations on the properties are periodically updated by qualified valuers to ensure appropriate coverage is maintained. The Bank requires that suitable insurance coverage is maintained through third party insurers to cover property risks.

The Bank uses a range of cash or alternative forms of acceptable collateral to collateralise credit exposures. The type and extent of security to be taken is determined through the credit underwriting analysis in line with credit policies and prudent credit risk management guidance which imposes conservative coverage covenants to mitigate credit risks on exposures. In addition to residential and commercial real estate mortgages and cash, the types of collateral the Bank may also take as security are, inter alia, pledges of cash and investment securities portfolios, legal charges over operating and fixed assets, Assignments, debentures and Guarantees. Investment securities portfolios are monitored regularly to minimise potential market risk. The Bank does not take credit derivatives as security for exposures. The security taken does not result in any reduction in RWAs under the standardised approach to credit risk.

All credit documentation is subject to prior in-house legal review and agreement to ensure suitability for the Bank's legal enforcement if necessary. Approved independent legal counsel may be engaged to prepare documentation for more complex or substantial arrangements.

Collateral held as security for investment securities is determined by the nature of the instrument. Debt securities and treasuries are generally unsecured whereas asset-backed securities and similar instruments are secured by pools of financial assets.

The Bank does not make use of on-balance sheet netting.

The above criteria apply to all correspondent banks and MM/FX counterparty banks, except the domestic Bermuda banks where nostro/vostro account balance limits can be approved by ALCO outside of the above criteria to allow for a smooth flow of payments to and from BCB across the local payments clearing system. BCB policy also defines restrictions on Treasury Counterparty Limits.

The BCB policy on broker dealers requires that only credit settlement exposure will be incurred against broker dealers with all transactions conducted on a settlement against delivery basis.

The Bank may incur limited exposure periodically to derivative transactions through its currency hedging programme and has very insignificant counter party credit risk. The Bank has an exposure as a Trading Member of the BSX as a Central Counter Party (“CCP”). BSX is a direct member of a CCP for local equity securities. The exposure to the BSX is typically short dated and relatively minor. In the case where these transactions take place, liquidity is held for both additional collateral that would have to be posted in the event of a credit rating downgrade and adverse movements in market rates. Collateral requirements following downgrade are assessed on a contractual basis, whereas liquidity for changes in market rates is assessed using historic market rate volatility.

The Bank uses a reputable international securities custodian for the Bank’s own investment holdings as well as securities held by the Bank in a fiduciary capacity for clients. The Bank undertakes prudential reviews of the securities custodian relationship on a periodic basis in line with relevant Policies.

“Wrong-way risk” may occur when exposure to a counterparty is negatively correlated with the credit quality of that counterparty. Hence, there is a tendency for the exposure to increase as the creditworthiness decreases. This risk is managed through the Asset and Liability Management Policy, which governs the requirements for eligible collateral and Counterparty limits and which are monitored by the Bank’s ALCO.

Table 24: Analysis of counterparty credit risk (CCR) exposure by approach (CCR1)

	a	b	c	d	e	f
	Replacement cost	Potential future exposure	EEPE	Alpha used for computing regulatory EAD	EAD post-CRM	RWA
1 SA-CCR (for derivatives)	433	510		1	943	943
6 Total						943

Monetary amounts in '000's

Table 25: Standardised approach – CCR exposures by regulatory portfolio and risk weights (CCR3)

Risk Weight	a	b	c	d	e	f	g	h	i
	0%	10%	20%	50%	75%	100%	150%	Others	Total credit exposure
Asset classes									
Sovereigns									0
Non-central government public sector entities (PSEs)									0
Multilateral development banks (MDBs)									0
Banks and Securities firms			943						943
Corporates									0
Regulatory retail portfolios									0
Other assets									0
Total									0

Table 26: Composition of collateral for CCR exposure (CCR5)

	a	b	c	d	e	f
	Collateral used in derivative transactions				Collateral used in SFTs	
	Fair value of collateral received		Fair value of posted collateral		Fair value of collateral received	Fair value of posted collateral
	Segregated	Unsegregated	Segregated	Unsegregated		
Cash - domestic currency	-	-	-	-	-	-
Cash - other currencies	-	-	15,257	-	-	-
Corporate bonds	-	-	-	-	-	-
Equity securities	-	-	-	-	-	-
Other collateral	-	-	-	-	-	-
Total	-	-	15,257	-	-	-

All amounts in '000's

The \$5 million reduction in the composition of collateral for CCR exposure over the reporting period was due to the release of collateral formerly posted with a counterparty with which credit lines were discontinued.

Table 27: Credit derivative exposures (CCR6)

	a	b
	Protection bought	Protection sold
Notionals		
Foreign Exchange Forward Contracts	61,048,402	(9,896,170)
Warrants	36,554	0
Total notionals	61,084,956	(9,896,170)
Fair values		
Positive fair value (asset)	471,248	0
Negative fair value (liability)	(244,164)	(74,661)

The table above shows the fair values of derivative financial instruments recorded as assets and liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying reference asset, index, or price and is the basis upon which changes in the value of derivatives are measured. The notional amounts of the derivatives are not recorded on the consolidated statement of financial position. The notional amounts indicate the volume of transactions outstanding at the year-end and are not indicative of the market risk or the credit risk. The movement in protection bought and sold due to maturing FX contracts and new ones purchased is in line with FX exposure policy.

Derivatives contracts are valued on a mark-to-market basis which substantially affects the movement in fair values over each quarterly period.

Securitisation

Table 28: Securitisation exposures in the banking book (SEC1)

	i	j	k
	Bank acts as investor		
	Traditional	Synthetic	Sub-total
1 Retail (total) - of which	1,923	-	1,923
2 residential mortgage	1,923	-	1,923

All amounts in '000's

Residential property in Bermuda comprises the main source of residential mortgage collateral and is a credit risk mitigant for the Bank's residential mortgages. All mortgage lending is supported by appropriate valuations using independent firms of qualified valuers. BCB has no securitisation exposure to the Bermuda residential property market. All residential property held by the Bank as mortgagee is to be insured through a third party insurer to cover property risks. There have been no significant changes over the reporting period.

The Bank does not run a trading book nor does the Bank act as originator or as sponsor of any securitisation.

Table 29: Securitisation exposures in the banking book and associated capital requirements - bank acting as investor (SEC4)

		a	b	c	h	l	p
		Exposure values (by RW bands)			Exposure values (by regulatory approach)	RWA (by regulatory approach)	Capital charge after cap
		≤20% RW	>20% to 50% RW	>50% to 100% RW	SA/SSFA	SA/SSFA	SA/SSFA
1	Total exposures	0	132	1,791	1,923	1,857	149
2	Traditional securitisation	0	132	1,791	1,923	1,857	149
3	Of which securitisation	0	132	1,791	1,923	1,857	149
4	Of which retail underlying	0	132	1,791	1,923	1,857	149

All amounts in '000's

The above table represents the aggregate amount of the Bank's securitisation holdings as at September 30, 2019 categorised by risk weighting.

Market Risk

Overview

Market risk is the risk that a change in the value of an underlying market variable (such as interest rates or foreign exchange rates) will give rise to a reduction in the Bank's income or an adverse movement in the value of the Bank's financial assets. BCB's main source of income is through the performance of its investment portfolio and interest income. The investment portfolio is managed conservatively to maximise return to the business, without excessive risk. Market risks are monitored closely by the Bank's Treasury Department and regularly reported to ALCO. The ALCO is responsible for balance sheet planning from a risk-return perspective, including the monitoring of primary financial risks, and the ongoing process of formulating, implementing, monitoring and revising strategies on assets and liabilities management to achieve the Bank's objectives, within approved policy risk tolerances.

Foreign Exchange Risk

Table 30: Market risk under the Standardised Approach (SA) (MR1)

		a
		Capital charge in SA
4	Foreign exchange risk	2,575
12	Total	2,575

All amounts in '000's

The Bank holds a portion of its investments in currencies other than US dollars and hence has some exposure to adverse changes in foreign exchange rates. The Bank manages its exposure to foreign exchange rate risk through the management of its net non-USD/BMD exposures to minimal levels via the utilisation of appropriate hedging instruments, master netting agreements, and other techniques as appropriate for maintaining a retained net risk position within the prescribed risk parameters.

It is the Bank's policy to hedge all major foreign exchange exposure with respect to BCB's functional currency. However, the ALCO may agree to allow certain positions to remain unhedged, where the cost of hedging outweighs the benefit. The Bank's monitoring tools for primary risks include, but are not limited to, maturity analysis, funding concentration, duration, Net Interest Income and Economic Value of Equity.

Further details on the risk management framework can be found in the Risk Management section of the Group's September 30, 2018 Annual Report.

Interest Rate Risk

In April 2016, the Basel Committee on Banking Supervision issued standards for Interest Rate Risk in the Banking Book ("IRRBB"). Those principles set out supervisory expectations for banks' identification, measurement, monitoring, and control of IRRBB, as well as supervision of this risk. The IRRBB was adopted by the Bank on January 2018 to manage its interest rate risk exposure.

Table 31: Quantitative information on IRRBB (IRRBB1)

In reporting currency	ΔEVE		ΔNII	
	30-Sep-19	30-Jun-19	30-Sep-19	30-Jun-19
Parallel up	(11,557)	(12,977)	(863)	(599)
Parallel Down	11,557	12,977	863	599
Steeper	(1,113)	(1,175)		
Flattener	1,910	2,621		
Short rate up	(455)	(826)		
Short rate down	455	826		
Maximum	(11,557)	(12,977)	(863)	(599)
Period	30-Sep-19		30-Jun-19	
Tier 1 capital	96,148		94,557	

All amounts in '000's

IRRBB is the exposure to movements in interest rates. Such risk occurs from a mismatch of interest rate exposures tied to the Bank's assets and liabilities and is a normal part of banking and an important contributor to earnings. The Bank developed an internal model to monitor the IRRBB and report the impact to the ALCO on a monthly basis. Adverse movements in interest rates can result in a reduction in the Bank's Economic Value of Equity ("EVE") and Net Interest Income ("NII"). Changes in interest rates affect earnings through NII variations and also changes to interest-sensitive income and expenses. Such changes also affect the underlying values of assets, liabilities and off-balance sheet instruments, and thereby the Bank's EVE, given that the present value of future cash flows changes as interest rates shift. The Bank discloses the impact of interest rate shocks on its Changes in Economic Value of Equity ("ΔEVE") and Net Interest Income ("ΔNII"), computed based on a set of **multiple** prescribed interest rate shock scenarios. Key assumptions and stress scenarios used to compute the IRRBB are approved by the ALCO.

The ALCO monitors asset deployment limits, including investment limits, in order to monitor and manage the exposure of the portfolio to liquidity, interest rate and currency risk and to ensure that the assets in the Bank's balance sheet are consistent with its risk appetite. ALCO ensures an appropriate ALM Policy is maintained for the Bank. The ALM Policy sets forth the Bank's asset and liability management general policy relating to liquidity risk management including contingency liquidity plan, interest rate risk management, capital management, foreign currency risk management including hedging and the use of derivatives, investment and other asset deployment limits.

Like many banks, BCB is exposed to IRRBB through its exposure to fixed income securities including HQLA, loans, other assets sensitive to interest rate movements, and customer deposits. A material impact of IRRBB comes through the Bank's exposure to a diversified portfolio of fixed income securities including HQLA. Duration is a measure of the price sensitivity of a fixed income security to changes in interest rate. The Bank manages the duration of its fixed income securities to mitigate the adverse impact of IRRBB.

For IRRBB, the Bank has applied the following assumptions:

- The loan portfolio comprises a small portion of the overall assets of the bank. As such, loan prepayment rates has not been utilised as the impact was deemed to be immaterial to the EVE.
- The majority of the Bank's currency exposure is in BMD and USD. Accordingly, all currencies have been aggregated and the US Treasury yield curve has been applied across all currencies.
- Commercial margins have not been included in the calculation of EVE
- The modified durations of the investment portfolio holdings is assumed to be the repricing impact for the parallel interest rate shock down.

With respect to investments, this risk only arises in the banking book, as the Bank does not run a trading book.

Funding & Liquidity Risk

Overview

Funding and Liquidity Risk is the risk that the Bank does not have sufficient financial resources to meet its financial obligations as they fall due, or can only do so at excessive cost. Funding and Liquidity risk exists where demand from clients to withdraw funds from their accounts exceeds the cash the Bank has available to fund those withdrawals because either there are no alternative sources of funds available to the Bank or it has failed to maintain sufficient liquid assets to be able to manage the outflow.

BCB deploys its assets in multiple currencies, funding this activity through the use of deposits (where available) and currency swaps. Currency swap facilities are established with BCB's banking counterparties by way of ISDA ("International Swaps and Derivatives Association") agreements, and supported by Credit Support Annex ("CSA") documents, which detail the collateral that BCB is required to post in support of its derivatives exposure to a counterparty. The ISDA agreements provide for the settlement netting of payment obligations arising under all of the derivative contracts covered by the agreement. Liquidity Risk arises mainly through maturity mismatches between the Bank's assets and its liabilities. To mitigate this risk, the Bank maintains a core liquidity position, which also provides the Bank with interest income.

The objectives of liquidity risk management are to ensure that the Bank can meet its cash flow requirements and capitalise on business opportunities on a timely and cost effective basis. The Bank manages its liquidity risk through cash and liquidity management techniques that maximise its liquidity, and through controls on the percentage of its balance sheet that can be converted to cash within specific short-term bands. The Bank maintains prudent levels of liquid assets in the form of cash and HQLA which are managed in parallel with the Bank's liability profile.

The Bank maintains significant liquidity thresholds in its balance sheet in the form of cash or near cash, other HQLA and assets within its investment portfolio. This high level of readily liquid assets factors into the Bank's contingency liquidity plan which is designed to provide alternative sources of liquidity to allow the Bank to meet its cash obligations without relying on external funding support during periods of stress. A variety of specific and systemic event scenarios that may present challenge to the Bank's liquidity are reviewed and updated at least annually through the Bank's customary stress testing analysis. In addition, the Bank's high level of capital relative to total deposits provides a meaningful contingency funding buffer. The Bank has a Liquidity Risk Management Policy approved by the BARC on the recommendation of MRC which defines the objectives for managing liquidity risk, sets conditions for the calculation of the minimum size of the liquidity buffer and the funding needed to support an adequate liquidity buffer. Ongoing monitoring and implementation of the liquidity policy is the responsibility of ALCO, under the approval of the BARC, and with responsibility for the daily monitoring and management assigned to the Treasury Department. The Treasury Department prepares liquidity reports and the results of stress testing performed and presented to ALCO on a monthly basis.

As part of its asset and liability management activities, the Bank produces a maturity analysis matrix to map all funding of relevant assets and liabilities into time buckets corresponding to their economic maturities. The matrix is compiled on an aggregated currency basis. Assets and liabilities from the deposit and mortgage book that show a history of being renewed or prolonged are assigned to time buckets reflecting their expected extension.

The maturity analysis matrix identifies the excess, or the shortfall, of assets over liabilities in each time bucket, facilitating the management of open liquidity exposures. The matrix analysis together with the liquidity planning process, which forecasts the funding supply and demand across business units, provides the key input parameters for the Bank's liquidity planning.

Liquidity Coverage Ratio

Table 32: Liquidity Coverage Ratio (LCR) (LIQ1)

	a	b
	Total unweighted value (average)	Total weighted value (average)
High-quality liquid assets		
1 Total HQLA		187,254
Cash outflows		
2 Retail deposits and deposits from small business customers, of which:	23,437	9,689
4 Less stable deposits	23,437	9,689
5 Unsecured wholesale funding, of which:	189,706	132,036
6 Operational deposits (all counterparties) and deposits in networks of cooperative banks	61,855	15,464
7 Non-operational deposits (all counterparties)	127,851	116,572
9 Secured wholesale funding		0
10 Additional requirements, of which:	14,961	14,389
11 Outflows related to derivative exposures and other collateral requirements	13,267	13,267
13 Credit and liquidity facilities	1,390	817
15 Other contingent funding obligations	305	305
16 TOTAL CASH OUTFLOWS		156,113
Cash inflows		
18 Inflows from fully performing exposures	88,970	67,442
19 Other cash inflows	769	769
20 TOTAL CASH INFLOWS	89,739	68,211
		Total adjusted value
21 Total HQLA		187,254
22 Total net cash outflows		87,903
23 Liquidity coverage ratio (%)		213.0%

All amounts in '000's

Note that average values were calculated using the simple average of the six month-end balances over the first half of fiscal year 2019.

The LCR metric is designed to promote the short-term resilience of a bank's liquidity profile ensuring the Bank has sufficient unencumbered HQLA that can be easily converted into cash to meet its liquidity needs in a 30-calendar day liquidity stress scenario. The BMA requires Bermuda banks to maintain a minimum LCR of 90% in 2018, increasing to 100% by January 1, 2019. The average month end BCB LCR has reflected 213.0% for the 6 month period ended September 30, 2019 which substantially exceeds current and future minimum requirements.

Net Stable Funding Ratio

Table 33: Net Stable Funding Ratio (“NSFR”) (LIQ2)

	Available stable funding (ASF) item	a	b	c	d	e
		Unweighted value by residual maturity				Weighted value
		No maturity*	<6 months	6 months to <1 year	≥1 year	
1	Capital:	96,148	-	-	-	96,148
2	Regulatory capital	96,148	-	-	-	96,148
4	Retail deposits and deposits from small business customers:	-	61,606	22,155	75,647	151,032
6	Less stable deposits	-	61,606	22,155	75,647	151,032
7	Wholesale funding:	-	189,961	2,027	1,076	43,429
8	Operational deposits	-	56,010	-	-	28,005
9	Other wholesale funding	-	133,951	2,027	1,076	15,424
13	All other liabilities and equity not included in the above categories	-	8,698	315	1,689	1,847
14	Total ASF					292,455
	Required stable funding (RSF) item					
15	Total NSFR high-quality liquid assets (HQLA)					13,749
16	Deposits held at other financial institutions for operational purposes	-	14,439	-	-	14,439
17	Performing loans and securities:	-	62,330	10,940	164,528	160,610
19	Performing loans to financial institutions secured by non-Level 1 HQLA and unsecured performing loans to financial institutions	-	53,232	0	19,837	27,822
20	Performing loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns, central banks and PSEs, of which:	-	205	17	2,729	2,431
22	Performing residential mortgages, of which:	-	-	-	1,092	710
23	With a risk weight of less than or equal to 35% under the Basel II standardised approach for credit risk	-	-	-	1,092	710
24	Securities that are not in default and do not qualify as HQLA, including exchange-traded equities	-	8,893	10,923	140,870	129,648
25	Assets with matching interdependent liabilities	-	-	-	-	-
26	Other assets:	-	5,284	235	18,794	24,313
29	NSFR derivative assets				152	152
31	All other assets not included in the above categories	-	5,132	235	18,794	24,161
32	Off-balance sheet items				5,465	0
33	Total RSF					213,111
34	Net Stable Funding Ratio (%)					137.2%

All amounts in '000's

* Items reported in the “no maturity” time bucket do not have a stated maturity. These may include, but are not limited to, items such as capital with perpetual maturity, short positions, open maturity positions, non-HQLA equities and physical traded commodities.

The NSFR requires banks to maintain a stable funding profile in relation to the composition of their assets and off balance sheet activities looking over a one year horizon. The BMA requires Bermuda banks to maintain a minimum NSFR of 100% from 1 January, 2018 onwards. The Bank NSFR stood at 137.2% as at September 30, 2019 which surpasses this requirement.

As at September 30, 2019:

- Customer deposits represent the main source of funding for the Bank;
- The Bank’s NSFR ratio of 137.2% is consistent with prior periods and there are no indications of significant movement; and
- The Bank’s balance sheet is comprised substantially of only deposits, loans and investments and without any notable amount of interdependent assets / liabilities.

Operational Risk

Overview

BCB has adopted the Basel Committee definition of operational risk, which is defined as ‘the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events’.

Operational risk is relevant to every aspect of the business processes, and cannot be entirely eliminated. However, it can be managed and mitigated to levels that are deemed acceptable by Management through the application of controls which have been designed appropriately and are operating effectively. Operational risk covers a range of risks such as fraud risk, system failure, people risk, and physical security risk. Risks relating to financial crime compliance are similarly included within the respective risk categories.

The Bank’s management of operational risk is the responsibility of the MRC, which reports to the BARC. The MRC meets on a minimum quarterly basis to review and discuss the material risks, and operation of controls. MRC also has oversight over the incident management process, ensuring that incidents which do occur are reported as appropriate, and managed to conclusion.

The Bank employs the ‘Three Lines of Defence’ Model to manage risk. The First Line of Defence refers to our risk and control owners, those that are accountable for managing risk in their day-to-day activities through the application of sound processes and controls. The Second Line of Defence refers to the Risk and Compliance function, who set policy, provide advice and challenge to the First Line. Our control environment includes a programme of Second Line reviews to provide assurance to Management that controls are operating as expected. The Third Line is Internal Audit, who provide independent review that our risk management, governance and internal controls are effective and fit for purpose.

Data on operational losses and any significant control failures are captured through the Bank’s Risk Incident Reporting process. All events are reported to MRC with High Risk incidents reported to BARC, each of which assess the adequacy of corrective actions taken by Management and mitigants deployed to prevent recurrence. Both the MRC and the BARC, and the Board also, receive regular reporting on the actual performance against approved risk appetite metrics.

On an annual basis, key risks are assessed on an inherent and residual basis. Controls are identified and rated as to their effectiveness, and form the basis for the assessment of the risk they address on a residual basis. Where controls are rated as less than effective, actions are identified to remediate the control or address any concern in the operational risk.

Risks which remain residually high-rated are identified and are the subject of further and additional mitigation, or risk acceptance, if required.

The Bank utilises automated systems to mitigate risk associated with criminal activity through the Bank’s products and services. These systems include application risk scoring systems for new business uptake and real-time wire activity screening against official watch-lists.

The Bank has implemented a suite of IT security tools to protect both systems and data. These include, but are not limited to, email security scanning/auto-blocking solutions, anti-virus products, intrusion detection real-time monitoring, vulnerability scanning and penetration testing tools and network traffic monitoring and alerting. We continually keep up to date with the cyber security landscape and consider improvements to our defences as that landscape changes. Logical access control is in place at the individual application level as well as at the network level. Password complexity and mandatory changes are enforced programmatically. User profiles limit what a user can access, see or change. Application database systems are also locked down and strictly controlled.

The Bank has adopted the Standardised Approach (“SA”) as set out in the Basel Capital Accord for the purposes of calculating its risk capital requirements. Under this approach gross income serves as a proxy for the scale of business operations and thus the likely scale of operational risk exposure within each of these business lines and the capital charge for operational risk is calculated based upon gross losses over the preceding three year period.

Other Information

Abbreviations:

The following abbreviated terms are used throughout the document:

ALCO	Asset and Liability Committee
ALM	Asset and Liability Management
ASF	Available Stable Funding
AT1	Additional Tier 1 Capital
BARC	Board Audit and Risk Committee
BCB or the Bank	Bermuda Commercial Bank Limited
BMA or Authority	Bermuda Monetary Authority
BSX	Bermuda Stock Exchange
CARP	Capital Adequacy and Risk Profile
CC	Credit Committee
CCF	Credit Conversion Factor
CCP	Central Counter Party
CCR	Counterparty Credit Risk
CET1	Common Equity Tier 1
Code of Conduct	Group Code of Conduct and Ethics for Employees and Directors
CRM	Credit Risk Mitigation
EAD	Exposure at Default
ECL	Expected Credit Loss
ERM	Enterprise Risk Management
ERMF	Enterprise Risk Management Framework
EVE	Economic Value of Equity
EXCO	Executive Committee
GC	Governance Committee
Group	Bank and its subsidiaries
HQLA	High Quality Liquid Assets
IFRS	International Financial Reporting Standards
IRRBB	Interest Rate Risk in the Banking Book
ISDA	International Swaps and Derivatives Association
KPIs	Key Performance Indicators
LCR	Liquidity Coverage Ratio
MDB	Multilateral Development Bank
MRC	Management Risk Committee
MSR	Mortgage Servicing Rights
NII	Net Interest Income
NSFR	Net Stable Funding Ratio
RSF	Required Stable Funding
RWA	Risk Weighted Assets
SA	Standardised Approach
SFT	Securities Financing Transaction
SSFA	Simplified Supervisory Formula Approach
T1	Tier 1 Capital
T2	Tier 2 Capital
Somers	Somers Limited
TC	Total Capital

Cautionary statements regarding forward-looking statements

These Capital and Risk Management Pillar 3 Disclosures as at 30 September 2019 contain certain forward-looking statements with respect to Bermuda Commercial Bank Limited (“the Bank”). Forward-looking statements are neither historical facts nor assurances of future performance. Instead, they are based on our current beliefs, expectations or assumptions regarding the future of our business, future plans and strategies, our operational results and other future conditions. Forward-looking statements may be identified by words such as ‘will’, ‘believe’, ‘expect’, ‘anticipate’, ‘project’, ‘estimate’, ‘predict’ and similar expressions, although not all forward-looking statements contain these identifying words and these are only intended to identify forward-looking statements.

These forward-looking statements may appear in the disclosures and may include, among others, statements with respect to our liquidity and capital requirements; business strategy; financial and operating targets or plans; projections of revenues, income, market share or other financial forecasts; expansion and growth of our business and operations; and future capital expenditures. These statements are based on certain assumptions and analyses we have made in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors believed to be appropriate in the circumstances. However, whether actual results and developments will conform to expectations and predictions is subject to a number of risks and uncertainties that could cause actual results to differ materially from expectations, including, among others, the risks discussed in this disclosure document.

We believe that these risks and uncertainties include, but are not limited to, those described in the Notes of Bank’s Audited Annual Report and Financial Statements, which include, but are not limited to: changes in economic and market conditions; changes in market interest rates; our access to sources of liquidity and capital to address our liquidity needs; our ability to attract and retain customer deposits; our ability to effectively compete with other financial services companies and the effects of competition in the financial services industry on our business; our ability to successfully execute our business plan and implement our strategy; our ability to successfully manage our credit risk and the sufficiency of our allowance for credit loss; our ability to successfully develop and commercialize new or enhanced products and services; damage to our reputation from any of the factors described in this section,

Consequently, all of the forward-looking statements made in this document are qualified by these cautionary statements and the results or developments that we anticipate may not be realized or, even if substantially realized, they may not have the expected consequences to, or effects on, us or our business or operations. The Bank assumes no obligation to update publicly any such forward-looking statements, whether as a result of new information, future events or otherwise.



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The Pillar 3 disclosures for September 30, 2019 are available on the Bank's website www.bcb.bm

Bermuda Commercial Bank Limited and its wholly owned subsidiary companies are licensed to conduct bank, investment, trust and corporate service provider business by the Bermuda Monetary Authority.