BANQUE DE PATRIMOINES PRIVES
Wealth Management

# Banque de Patrimoines Privés

## Pillar 3 Disclosure Report
## 2018

Crèdit Andorrà Financial Group

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# INDEX OF ABBREVIATIONS

| | |
|---|---|
| AML | Anti-Money Laundering |
| BIA | Basic Indicator Approach |
| CEBS | Committee of European Banking Supervisors |
| CET1 | Common Equity Tier 1 ratio |
| CRD IV | The Capital Requirements Directive IV |
| CRR | The Capital Requirements Regulation |
| CSSF | Commission de Surveillance du Secteur Financier |
| EBA | European Banking Authority |
| HQLA | High Quality Liquid Assets |
| IAS | International Accounting Standards |
| ICAAP | Internal Capital Adequacy Assessment Process |
| ILAAP | Internal Liquidity Adequacy Assessment Process |
| KYC | Know Your Customer |
| LCR | Liquidity Coverage Ratio |
| LTI | Long Term Incentive |
| NSFR | Net Stable Funding Ratio |
| RAS | Risk Appetite Statement |
| RCSA | Risk and Control Self-Assessment |
| SREP | Supervisory Review and Evaluation Process |
| VAR | Value-at-Risk |

# 1. OVERVIEW

## 1.1. Purpose

This document presents the Pillar 3 disclosure report of Banque de Patrimoines Privés ("BPP" or "the Bank").

The purpose of this report is to provide information on the implementation of the Basel III framework and risk assessment processes in accordance with the Pillar 3 requirements in accordance with part XIX "Disclosure by Credit Institutions" of the Commission de Surveillance du Secteur Financier ("CSSF") circular 06/273 as amended, and Circular CSSF 15/618 transposing EBA guidelines on "Pillar 3 disclosures". In particular, Circular 06/273 sets out the requirements related to the own funds adequacy in the financial sector by transposing into Luxembourg Law directives 2006/48/EC and 2006/49/EC of the European Parliament and the Council derived from the recommendations of the Basel Committee (Basel III).

The disclosures presented in this document are complimentary to other work undertaken by the Bank in its assessment of capital requirements under the Internal Capital Adequacy Assessment Process ("ICAAP") and to the 2018 Annual Report.

## 1.2. Regulatory framework

The Basel framework has established a more risk sensitive approach to capital management and this is comprised of three pillars. Doing so enables the market to have a greater scope of visibility to its constituents.

### 1.2.1. Pillar 1

This is the **Minimum Capital Requirement** related to credit, market and operational risks that the Bank incurs. This further extends beyond solvency requirements and covers the Bank's liquidity requirements.

### 1.2.2. Pillar 2

Pillar 2 lays out the requirements for **Supervisory Review and Evaluation Process** ("SREP") and the settling of individual capital requirements of the Bank, taking into consideration the Bank's own assessment of capital requirements. Doing so allows supervisors to evaluate the Bank's assessment of its own risks and determine whether the assessment seems reasonable.

### 1.2.3. Pillar 3

The aim of Pillar 3 is **Market Discipline** which aims to produce disclosure which allows market participants to assess the capital position, risk exposure and risk management processes. This includes all material risks thus enabling a comprehensive view of the Bank's risk profile. The purpose here is to have greater transparency in Bank's financial reporting thus enabling market place participants to better strengthen the risk management environment.

The Pillar 3 disclosure will comprise of both quantitative disclosures relating primarily to actual risk exposures and qualitative disclosures relating to risk management practices.

A further qualitative disclosure has been applied by presenting a summary of the Bank's Remuneration Policy.

## 1.3. Frequency and location of disclosure

This document is prepared and updated at least annually and more frequently if deemed necessary. Unless stated otherwise, all figures are as of December 31st, 2018.

The report will be published on the Bank's website (www.banquedepatrimoinesprives.com) and will not be subject to external audit, except to the extent that any disclosures are equivalent to those made under accounting requirements. The disclosures presented in this report do not constitute any form of audited financial statement.

These disclosures have been reviewed and verified by the Authorized Management of the Bank.

## 1.4. Materiality

CRR Article 432(1) provides that a firm may omit one or more of the required disclosures if the information provided by such disclosures is not regarded as material. Information is considered to be material if its omission or misstatement could change or influence the assessment or decision of a user relying on it for the purpose of making economic decisions.

## 1.5. Proprietary or confidential information

CRR Article 432(2) provides that an Institution may omit one or more items of information included in the disclosures listed in Titles II and III if those items include information which is regarded as proprietary or confidential in accordance with the second and third subparagraphs, except for the disclosures laid down in Articles 437 and 450.

Information shall be considered as proprietary to a firm if disclosing it publicly would undermine its competitive position and may include information on products or systems which, if shared with competitors, would render the firm's investments therein less valuable. Information is regarded as confidential if there are obligations to customers or other counterparty relationships binding the firm to confidentiality.

Where information has been omitted from these disclosures in accordance with either CRR Article 432(1) or Article 432(2), this has been stated in the relevant section.

# 2. COMPANY OVERVIEW AND ACTIVITIES

Banque de Patrimoines Privés was incorporated in Luxembourg on 1 July 2010 as a limited company under Luxembourg Law. Since 9 April 2011, the Bank is a wholly-owned subsidiary of Crèdit Andorrà Financial Group (hereinafter “the Parent Company” or “CAFG”).

The Bank has its registered office at 30 Boulevard Royal, Luxembourg and is authorized and regulated by the CSSF and as such is subject to minimum regulatory capital requirements.

The Bank established as its Core Strategy to strengthen and expand its market presence in the Private Banking and the Corporate & Funds Services, by positioning itself as a preferential service provider for a wide base of customers, covering different activities and geographical locations.

The Bank´s objective is to propose custom-made solutions for their customers avid to create any investment vehicle types or to settle down to the Grand Duchy via domiciled companies. The Bank’s services include the preparation and the constitution of companies and investment funds, their domiciliation, with possibility for administrative and accounting management, as well as the missions of the depositary bank which ensue from it. On the other hand, in the dynamics of the Group, the Bank also proposes private banking and wealth management services to customers.

# 3. GOVERNANCE

## 3.1. Board of Directors

The Board has the ultimate responsibility for limiting and monitoring the Bank’s risk exposure as well as for setting targets for the capital ratios and risk appetite.

- Responsible for creating and delivering value by governing the Bank’s business while meeting the interest of shareholders and other stakeholders
- Establish, document and communicate the internal capital planning, management and adequacy in relation to the Bank’s risk profile.
- Establish the framework to actively promote an internal risk culture among the various operational departments.
- Monitor and approve the implementation of the principles, strategies and objectives setup as the risk appetite of the Bank.
- Review key documentation such as the ICAAP / Individual Liquidity Adequacy Assessment Process (“ILAAP”) as well as key business activity, material risk taking and risk-related control processes.

## 3.2. Authorized Management

- Implement sound and effective processes in order to identify, manage, report and mitigate all material risks, in relation to the established risk-bearing capacity.
- Establish internal reporting tools which allow a proper oversight of the risks identified.

- Ensure the proper management of risks in case that they materialize in a way that might affect the operational effectiveness of the Bank.
- Ensure that proper internal control systems (electronic and non-electronic) are setup, ensuring the follow up of Risks.

## 3.3. Risk Management Department

- Analyse, monitor and control the risks arising during the business activity of the Bank.
- Develop and maintain the Bank's risk management procedures and policies in order to ensure a continuous monitoring over the proper regulatory compliance.
- Provide relevant independent information, analysis and expert judgement on risk exposures and risk decisions
- Assist the Authorized Management and the Board of Directors in order to take informed decisions regarding risk management.
- Assist in the embedding of risk management within all areas of the business

An elaboration of the previously mentioned objectives, processes and strategies of the Risk Management department is detailed in Section 4 of this document.

## 3.4. Compliance Department

- Ensure the Bank remains relevant to the current regulatory guidance and requirements.
- Assisting in the designing of appropriate risk identification, assessment and reporting processes to facilitate the adherence to regulatory requirements.

## 3.5. Internal Audit Department

- Assist the Board of Directors in their oversight responsibilities relating to financial matters, including corporate reporting, risk management and internal control.
- Responsible for the oversight of the quality and integrity of accounting and reporting practices and the performance of the internal audit function and independent external auditors
- Ensure, through independent audits, that the adequacy of the risk control and risk management function is monitored.

# 4. RISK MANAGEMENT FRAMEWORK

## 4.1. Risk Management objectives and policies

The Bank is exposed to a variety of risks as a result of its business activities. As such, active and effective risk management is fundamental to the Bank's core competence. In order to support this, the Bank has developed procedures and policies which help define a structured and formulated approach towards risk management. The key areas which the Risk Management department focuses on are:

- The identification and effective management of all types of risks the Bank is exposed to.
- Use of key risk metrics and business performance indicators to monitor risk levels quantitatively and qualitatively.
- Monitoring the implementation of significant changes in the Bank and their associated impact on the Bank's metrics
- Promoting a culture of ethical conduct, accountability, risk awareness and transparency that extends across the Bank in all its departments and activities carried out.
- Full compliance with applicable regulation, laws and procedures.

The reporting of risk controls, either scheduled or exceptional, is made to the Authorized Management of the Bank on a periodic basis. The risk reporting is produced by internal tools and databases which have been developed internally, whereby controls are in place to ensure accuracy, completeness and coherence of the different databases.

Risk Management reports are produced periodically (monthly, quarterly and annual basis) and sent to the Parent Company in Andorra, which provide backward and forward-looking empirical measures regarding all key risks faced by the Bank.

### 4.1.1. Three Lines of Defence

The primary goal of the Risk Management activities of the Bank is to ensure that the outcome of the risk-taking activities across the departments is consistent with the Bank´s risk appetite defined by the Board of Directors. The Bank ensures that there is always proper balance between risk and reward, looking to maximize the profits always in the boundaries of the risk limits defined.

In the everyday identification and management of the risks it faces, the Bank operates with a "Three Lines of Defence" model.

**1st Line of Defence** – Conformed by the business and operational departments who are the owners of the risk origination activities. They are required to maintain effective processes, systems and controls to manage risks inherent to their operations.

**2nd Line of Defence** – Conformed by the Risk Management department and the Compliance department. These functions have clear segregation of duties and independence and support the first line of defence risk management activities as per the control framework setup across all the activities of the Bank.

**3rd Line of Defence** – Performed by the Internal Audit Department, whom assures the effectiveness of the Bank´s controls.

The Internal Control functions (Risk Management, Compliance and Internal Audit) are independent of each other, report directly to the Authorised Management and have direct access to the Board of Directors. In despite of this independence, the internal control departments work together and are involved in common controls, each of them within a defined framework.

## 4.2. Framework

Since its establishment, the Bank has had a Risk Management function which has developed and maintained the risk management framework through the setting up of various specific procedures for each department of the Bank. The internal Risk Management framework of the Bank is established in the Risk Management Policy, which describes how the risks are identified, measured, mitigated and reported.

The risks are defined in various types and subcategories whose granularity reflects the size and complexity of the Bank's operations. The allocation of own funds is determined by using as reference the information already reported to the CSSF within the Circular 06/273 as amended, and complement by adding the risks and capital requirements that are not covered by these reports and materialized in the ICAAP/ILAAP report which is validated by the Board of Directors and sent to the CSSF, at least, once per year.

This report presents the various risks to which the Bank is facing, or may face, as well as the stress scenarios which allow the Bank's Management to allocate specific capital or liquidity resources to each activity to cover the risk related to such activities. It also serves to implement the necessary procedures to monitor, mitigate and manage the identified risks, and to locate unidentified risks.

## 4.3. Risk identification and notification

All operational units and individuals of the Bank have the duty to identify and quantify potential risks in their area of responsibility. As a result, the Bank's risk identification process is a firm wide initiative which involves a proactive process of constant monitoring and assessment.

The Bank's risk identification process is both forward and backward looking. Assessment is done by regular review of processes in order to identify key areas of risk, weak points and points of failure. Similarly, following an incident, the bank conducts a further assessment to push mitigation actions and employ principles of learning from the event.

Once a risk has been identified, logged or realised, the Bank has ensured a procedure of centrally recording these errors. All the operational units (first line of defence) including individual employees must notify the Risk Management Department (second line of defence), in a timely manner, of the risks that have been identified and quantified.

## 4.4. Risk appetite

The Risk Appetite clearly defines the Bank's attitude to the type and amount of risk taking in consideration the type of business, capital targets, shareholders expectations and macroeconomic conditions.

The general Risk Appetite is low/moderate risk in the development of its business strategies. In this sense the Risk Appetite incorporates all material risks facing the Bank and aligns to the strategy using the forward-looking business plan. In order to ensure alignment to the strategy the Bank uses the following processes:

- Risk Capacity (capital and liquidity) is evaluated and quantified
- Risks arising from the business strategy are identified (quantitative and qualitative) and assessed

The Risk Appetite is approved by the Board of Directors on an annual basis as part of the strategic planning process and is outlined through both quantitative and qualitative measures. This is underpinned by the following planning processes:

- **Capital adequacy:** Hold enough capital to maintain capital ratios above both regulatory and stressed capital requirements.
- **Earning stability:** Limit earning volatility to support the ability to achieve state financial objectives.
- **Funding liquidity risk:** Manage liquidity and funding liquidity risk by maintaining sufficient funds to meet all obligations on both a business-as-usual basis and in periods of liquidity stress.
- **Minimization of reputational risk:** Avoid any transactions or services that bring risk of an unacceptable level of damage to the Bank's reputation.
- **Control of operational risk:** Ensure robust management of operational risk in the Bank's day-to-day operations and its forward-looking business strategy.
- **Concentration risk:** Proactively control concentrations within position risk by maintaining a well-diversified funding base.
- **Control legal risk:** Conduct business practices that are in line with the Bank's code of conduct and proactively identify sources of risk and/or breaches that may lead to reputational risk or regulatory sanctions.

## 4.5. Risk limits and mitigation

The Bank has several techniques which it employs to mitigate each risk depending on its nature. This includes the use of controls, outsourcing, contingency planning, capital allocation and collateral.

Based on these techniques, the Bank has developed approved limits set out by key risk type. These limits are then used as a basis for defining a more granular risk framework. The Authorized Management and the Chief Risk Officer are responsible for setting specific limits deemed necessary to manage the risk within individual lines of business and across counterparties as followed:

- Market risk is excluded as the Bank does not have a trading book and thus does not employ any methodology regarding, sensitivity, portfolio or stress management. Nevertheless, the Bank does monitor its banking book foreign exposure risk on a daily basis.
- Credit risk limits are based on a variety of exposure and stress measures including, for example, counterparty exposure and portfolio loss stress metrics. The overall credit risk management is designed to control overall credit quality, collateral arrangements and mitigation of concentration risk (such as single name) within the portfolio.

- Operational risk thresholds are based on a series of metrics designed to assess control effectiveness across the activities. The Bank has internally designed an operational risk database tool which allows for calibration and monitoring of events. This tool is designed to identify key areas of potential control weakness and helps drive development programmes to reduce operational risk. These thresholds are set in both quantitative (considering historical losses and gains) and qualitative terms.

These limits define the Bank's maximum risk appetite given management resources, market environment, business strategy and available resources to absorb potential losses.

## 4.6. Pillar 2

The Pillar 2 assessment is largely comprised on the ICAAP/ILAAP, which is the Banks methodology for assessing the level of capital that adequately supports all the Banks current and future risks in its business. The ICAAP/ILAAP focuses on the principal risks to the consolidated financial position and examines all risk categories to identify exposure that could put the Bank's capital at risk. The assessment is developed to ensure that capital resources:

- Remain adequate to support the Bank's risk profile and outstanding commitments;
- Maintain capitalisation in events of severe economic downturn stress scenario;
- Meet current and future regulatory requirements;
- Remain consistent with the Bank's strategic and operational goals and our shareholder and investor expectations.

The ICAAP/ILAAP is supported by a scenario analysis which is used to support the determination of a level of capital required for severe but plausible events. It is updated and reviewed annually, with more frequent reviews in the event of a fundamental or anticipated change to the Bank's business. The ICAAP/ILAAP is formally approved by the Authorized Management and Board of Directors, which has the ultimate responsibility for the effective management of risk and approval of the Bank's risk appetite.

## 4.7. Stress testing

Stress testing is a key part of the Bank's planning and risk management processes helping to identify, analyse and manage risks within the business. Capital planning forms part of the ICAAP and a range of stress test and scenario analysis are used to estimate the impact of stress events on capital resources and regulatory capital requirements. In addition, stress testing is conducted for the ILAAP and supports the Recovery Plan and its associated scenario analysis.

Stress testing and scenario analyses are conducted on a regular basis and the results, trend information and supporting analysis are reported to the Authorized Management. In particular, the scenarios are defined and based upon historical events or on forward-looking, hypothetical plausible events that could impact the Bank's positions in terms of capital, liquidity or profitability. The scenarios are reviewed and updated as markets and business strategies of the Bank evolve.

# 5. CAPITAL MANAGEMENT AND OWN FUNDS

## 5.1. Solvency

Article 56 of the law of April 5, 1993 related to the Financial Sector gives the CSSF the ability to determine the coefficients to be applied according to the International conventions as well as the European Directives that needs to be respected by the credit institutions under their supervision.

The methods to calculate the solvency ratio are described in CSSF's Circular 06/273 as amended, concerning the definition of Capital and Solvency Ratios.

In such Circular, the following concepts to be applied to Credit Institutions are defined:

- The levels of own funds to be respected;
- The terms of a notification system and the limits of large exposure;
- The capital requirements related to credit risk as well as dilution risk of all activities;
- Capital requirements to cover operational risks associated with the activities it develops;
- Capital requirements for currency risk hedging;
- Capital requirements to cover the risk of price changes in commodities;
- A simplified capital ratio relating to the risk weighting

The solvency ratio can give a clear outlook of the importance of own funds of the institution, as related to credit, currency and operational risks associated to the Bank's activities. In accordance to Circular 06/273, the Bank's own funds must be at least equal to the overall capital requirements.

### 5.1.1. Simplified ratio

Due to the absence of market activity, the Bank was exempted from calculating an integrated ratio in accordance with EU Regulation No 575/2013.

The Bank has obtained a waiver in order to calculate a simplified ratio during the reporting period in accordance to CSSF's Circular 06/273, Section V, Chapter 2, part 9 as amended, as the Bank has no trading portfolio.

| *In Euros* | 31.12.2018 | 31.12.2017 |
|---|---|---|
| **Tier 1 Capital** | 49,182,913 | 47,952,777 |
| *Where:* | | |
| *Tier 1 Common Equity* | *49,182,913* | *47,952,777* |
| *Additional Tier 1* | *-* | *-* |
| *Tier 2 Own Funds* | *-* | *-* |
| *Deductions* | *- 80,044* | *- 200,000* |
| **Own Funds** | **49,182,913** | **47,952,777** |
| **Risk Weighted Assets** | **123,115,912** | **131,090,661** |
| **Capital Adequacy Ratio** | **39.95%** | **36.58%** |

The calculation of the capital requirement is detailed below:

| *In Euros* | RWAs | | Minimum Capital Requirements | |
|---|---|---|---|---|
| | 31.12.2018 | 31.12.2017 | 31.12.2018 | 31.12.2017 |
| Credit risk (excluding CCR) | 93,807,832 | 104,017,058 | 7,504,627 | 8,321,365 |
| Of which the standardised approach | 93,807,832 | 104,017,058 | 7,504,627 | 8,321,365 |
| Of which the foundation IRB (FIRB) approach | | | | |
| Of which the advanced IRB (AIRB) approach | | | | |
| Of which equity IRB under the simple risk-weighted approach or the IMA | | | | |
| CCR | - | - | - | - |
| Of which mark to market | | | | |
| Of which original exposure | | | | |
| Of which the standardised approach | | | | |
| Of which internal model method (IMM) | | | | |
| Of which risk exposure amount for contributions to the default fund of a CCP | | | | |
| Of which CVA | | | | |
| Settlement risk | | | | |
| Securitisation exposures in the banking book (after the cap) | | | | |
| Of which IRB approach | | | | |
| Of which IRB supervisory formula approach (SFA) | | | | |
| Of which internal assessment approach (IAA) | | | | |
| Of which standardised approach | | | | |
| Market risk | - | - | - | - |
| Of which the standardised approach | | | | |
| Of which IMA | | | | |
| Large exposures | | | | |
| Operational risk | 29,308,080 | 27,073,603 | 2,344,646 | 2,165,888 |
| Of which basic indicator approach | 29,308,080 | 27,073,603 | 2,344,646 | 2,165,888 |
| Of which standardised approach | | | | |
| Of which advanced measurement approach | | | | |
| Amounts below the thresholds for deduction (subject to 250% risk weight) | | | | |
| Floor adjustment | | | | |
| **Total** | **123,115,912** | **131,090,661** | **9,849,273** | **10,487,253** |

## 5.1.2. Leverage Ratio

| *In Euros* | | 31.12.2018 | 31.12.2017 |
|---|---|---|---|
| **On-balance sheet exposures** | | | |
| 1 | On-balance sheet exposures (excluding derivatives and securities financing transactions (SFTs), but including collateral) | 536,550,513 | 418,860,441 |
| 2 | (Asset amounts deducted in determining Basel III Tier 1 capital) | -4,247,017 | -4,532,479 |
| 3 | **Total on-balance sheet exposures (excluding derivatives and SFTs) (sum of row 1 and 2)** | **532,303,496** | **414,327,962** |
| **Derivative exposures** | | | |
| 4 | Replacement cost associated with *all* derivatives transactions (where applicable net of eligible cash variation margin and/or with bilateral netting) | - | - |
| 5 | Add-on amounts for PFE associated with *all* derivatives transactions | - | - |
| EU-5a | Exposure determined under Original Exposure Method | 4,767,950 | 3,343,908 |
| 6 | Gross-up for derivatives collateral provide where deducted from the balance sheet assets pursuant to the operative accounting framework | - | - |
| 7 | (Deductions of receivable assets for cash variation margin provided in derivatives transactions) | - | - |
| 8 | (Exempted CCP leg of client-cleared trade exposures) | - | - |
| 9 | Adjusted effective notional amount of written credit derivatives | - | - |
| 10 | (Adjusted effective notional offsets and add-on deductions for written credit derivatives) | - | - |
| 11 | **Total derivative exposures (sum of rows 4 to 10)** | **4,767,950** | **3,343,908** |
| **Securities financing transactions** | | | |
| 12 | Gross SFT *assets* (with no recognition of netting), after adjusting for sale accounting transactions | - | - |
| 13 | (Netted amounts of cash payables and cash receivables of gross SFT assets) | - | - |
| 14 | CCR exposure for SFT assets | - | - |
| 15 | Agent transaction exposures | - | - |
| 16 | **Total securities financing transaction exposures (sum of rows 12 to 15)** | **-** | **-** |
| **Other off-balance sheet exposures** | | | |
| 17 | Off-balance sheet exposure at gross notional amount | 58,761,594 | 41,731,385 |
| 18 | (Adjustments for conversion to credit equivalent amounts) | | |
| 19 | **Off-balance sheet items (sum of rows 17 and 18)** | **58,761,594** | **41,731,385** |
| **Capital and total exposures** | | | |
| 20 | **Tier 1 capital** | **49,182,913** | **47,952,777** |
| 21 | **Total exposures (sum of rows 3, 11, 16 and 19)** | **595,833,041** | **459,403,255** |
| **Leverage ratio** | | | |
| 22 | **Basel III leverage ratio** | **8.25%** | **10.44%** |

# 6. PILLAR 1 RISK CATEGORIES

## 6.1. Credit and Counterparty risk

Credit and counterparty risk arise from the potential failure of the Bank's borrowers or counterparties to fulfil their obligations. This risk is the most significant risk faced by the Bank in terms of regulatory capital requirements that arise from its lending activities.

Credit risk represents the Bank's largest regulatory capital requirement and is controlled through specific procedures that the Bank has in place. These procedures provide the Bank with qualitative and quantitative tools which allow diversification of counterparties, which are selected using a "credit rating" method developed by the Parent Company. Depending on the rating obtained, a specific limit will be granted to each counterpart. This procedure is mainly used for interbank activity.

Regarding credit risk, an internal procedure is in place consisting of a setting up of specific review and authorization steps for credit proposals. The procedure is formalized by the Credit Committee of the Bank.

Customer lending business is not a core activity of the Bank, and it is focused on private clients and well-recognized companies and fully collateralized by cash deposits or asset portfolios mainly in custody of the Bank. Specifically, any loan granted must be guaranteed by financial collateral, cash, life insurance policies or bank guarantee.

The collateral arrangements are periodically monitored by the "Professional Services & Credit Lending" department. The Bank has a very strict collateral policy related to lending and always requires a high level of collateralization when granting a loan. The credit risk is determined on by the standardized approach as defined by CSSF's Circular 06/273.

The tables below give details on the requirements of regulatory capital by type of exposure as of the end of 2018.

| *In Euros* | Exposures before CCF and CRM | | Exposures post CCF and CRM | | RWAs and RWA density | | Own Funds |
|---|---|---|---|---|---|---|---|
| **Exposure classes** | **On-balance sheet amount** | **Off-balance sheet amount** | **On-balance sheet amount** | **Off-balance sheet amount** | **RWAs** | **RWA density** | **TOTAL** |
| Central governments or central banks | 137,008,125 | - | 407,213,535 | 19,032,031 | - | 0% | - |
| Regional government or local authority | | | | | | | |
| Public sector entities | | | | | | | |
| Multilateral development banks | | | | | | | |
| International organisations | | | | | | | |
| Institutions | 315,783,262 | 8,471,616 | 75,773,660 | 8,471,616 | 32,473,802 | 39% | 2,597,904 |
| Corporates | 52,961,646 | 44,238,161 | 23,606,935 | 25,206,131 | 34,615,182 | 71% | 2,769,215 |
| Retail | 26,231,984 | 6,051,817 | 25,390,888 | 6,051,817 | 18,969,927 | 60% | 1,517,594 |
| Secured by mortgages on immovable property | | | | | | | |
| Exposures in default | | | | | | | |
| Exposures associated with particularly high risk | | | | | | | |
| Covered bonds | | | | | | | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Institutions and corporates with a short-term credit assessment | | | | | | | |
| Collective investment undertakings | | | | | | | |
| Equity | | | | | | | |
| Other items | 9,333,446 | - | 7,785,757 | - | 7,748,920 | 100% | 619,914 |
| **Total** | **541,318,463** | **58,761,594** | **539,770,774** | **58,761,594** | **93,807,832** | **16%** | **7,504,627** |

During 2018, the Bank did not transfer any credit or counterparty risk by using securitization vehicles.

### 6.1.1. Non-Performing and Forborne Exposures

Performing and non performing exposures as of December 31, 2018

| *In Euros* | Gross carrying value of performing and non-performing exposures | | | | | | |
|---|---|---|---|---|---|---|---|
| | | Of which performing but past due > 30 days and <= 90 days | Of which performing forborne | Of which non-performing | | | |
| | | | | | Of which defaulted | Of which impaired | Of which forborne |
| **Debt securities** | 86,208,713 | - | - | - | - | - | - |
| **Loans and advances** | 443,639,075 | 187,492 | - | 171,867 | 72,657 | 72,657 | - |
| **Off balance sheet exposures** | 57,795,700 | - | - | - | - | - | - |

The Bank held the following general impairment position:

| *In Euros* | 31.12.2018 | 31.12.2017 |
|---|---|---|
| Impairments to Financial Institutions | 8,893 | - |
| Impairments to loans and advances | 84,853 | 19,287 |
| **TOTAL** | **93,746** | **19,287** |

### 6.1.2. Reporting, measurement and mitigation

The Bank follows the alternative approach proposed by CSSF's Circular 06/273 as amended, to mitigate credit risk. The Bank has developed an internal system which allows the assessment on a day-to-day basis of the credit limit utilisation of counterparties in relation to their associated limit. Additionally, on a daily basis the Risk Management department develops a report to show the liquidity balance by counterparty and duration thus helping analyse overdrafts.

## 6.2. Market risk

Market risk is the risk of changes in market prices, interest rates, currencies or other economic factors that could cause a reduction in the value of assets or portfolio of assets. Market risk can arise from open market positions (either long or short) or imperfectly hedged positions. The Bank's exposure to market risk is mainly concentrated in foreign exchange rate and interest rate risk.

The Bank does not own a trading portfolio and as such is not subject to capital requirements to cover position risks. However, the bank is exposed to currency risk as it holds cash in different currencies.

The Bank's policy regarding the decisions to take foreign exchange positions is conservative and is to have enough cash to cover small operations from clients. However, an exchange risk on corporate credit lines as well as hedging spot/forward positions initiated by the clients, still exist. To control the market risk, the Risk Management department performs daily checks on the foreign exposure in the banking book.

The Bank does however face the potential of market risk in the form of interest rate risk (as a result of fluctuations in interest rates in connection with cash movements or borrowing or currency risk in operating business when recognising net revenues denominated in foreign currencies).

### 6.2.1. Interest rate risk

As specified in its dedicated policy, the Bank covers the treasury market risk in operations on behalf of its clients. The Bank's policy normally accepts on exceptional basis commitments which exceed 6 months and requests to cover most of its position when it is for more than 30 days (based on their expectations). However, due to the low sensitivity to movements in interest rates, no limits have been defined for this risk.

Stress tests are performed by the Bank, as per CSSF's Circular 08/338 as amended, which are done in a monthly basis. The methodology followed to perform the stress tests is by scenario simulation, taking in account those assets in the balance sheet that are sensitive to changes in interest rate. A calculation of the economic value and impact occurred when the interest rates changes are performed, allowing to calculate the financial margin and the impact on the income statement. The stress tests are designed to determine the impact in the Capital position of the Bank, from an upward or downward movement of 200 basis points in the interest rates curves.

As of December 31, 2018, the results of the stress test for a variation of 100 and 200 basis points on the interest rates were as followed:

| Sensitivity | Economic Sensitivity Value | Financial Sensitivity Margin |
|---|---|---|
| +100bp | 2.88% | 72.17% |
| -100bp | 4.09% | -11.4% |
| **+200bp** | **6.47%** | **146.44%** |
| **-200bp** | **0.99%** | **-40.08%** |

## 6.3. Operational risk

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people, and systems or from external events. The objective of the administration structure of the Bank is to ensure the business functions and to have available the necessary support for their operations.

The operational risk capital requirement has been based on the CSSF Circular 06/273 Part XV, as amended. The Bank has elected the Basic Indicator Approach ("BIA") for operational risk. The gross income indicator has been calculated based on accounting values for the last three years. The Bank has decided to adopt a prudent approach by using a 15% indicator for all its exposure.

The total capital requirement for operational risk amounted, at the end of December 2018, to EUR 2,344,646.

While the Bank currently employs the BIA approach, the firm is working towards developing the foundation of a sound risk control framework based on the Principles for a sound Management of Operational Risk from the Basel Committee in applying the Risk and Control Self-Assessment ("RCSA") practice to analyse its risk profile as well as the adequacy of its control to cover it.

The Bank also notes two sub-risks which fall under operational risk:

- **Compliance risk:** Defined as the risk generate by the macroeconomic and regulatory environment which the Bank operates in. This risk is mitigated by the Compliance function within the Bank identifying and evaluating compliance risk.

- **Reputational risk**: Defined as the risk from negative public perception which could cause a contraction in the customer base, costly litigations or shareholder value. This risk is mitigated by the robust application of Anti-Money Laundering ("AML") and Know Your Customer ("KYC") principles.

### 6.3.1. Reporting, measurement and mitigation

For monitoring purposes, the Bank has set up a database tool developed by the Parent Company whose methodology is known and accepted by the Bank. The purpose of the tool is centralising all reported operational risk incidents in order to ensure the collection of the entire incidents as well as to monitor the operational risk profile of the Bank.

Consequently, all operational incidents (with and without a financial impact) are assessed and logged, both on paper and electronically in the form of an incident report form, in order to control the deficiencies through all the processes, better adapt risk management processes and refine back testing work.

The monitoring of this database is ensured by the Risk Management Department of the Bank, who ensures the collection and registration of all operational incidents through the database, based on report incidents received by the responsible business lines.

## 6.4. Liquidity risk

Liquidity risk is defined as the possibility of incurring losses when there are not sufficient cash or liquid resources to comply with the obligations assumed. The Bank is exposed to liquidity risk as it may lack enough liquidity to meet its daily payment obligations or incur refinancing costs in the event of liquidity stress.

The management of liquidity risk is detailed by the Bank's liquidity risk procedure, which set out the full coverage of the Bank's liquidity standards as required by the regulator, stress tests and scenario analyses. The Bank utilises reverse liquidity stress tests to ensure that efficient liquidity during potential market disruptions and idiosyncratic scenarios.

As of December 31, 2018, the schedule of financial assets and liabilities is as follows:

**Maturities of financial assets and liabilities** *(book value, EUR)*

| | ≤ 3 months | > 3 m < 1 yr | > 1 yr < 5 yr | > 5 yr | Total |
|---|---|---|---|---|---|
| **Instrument Category (financial assets)** | | | | | |
| Treasury and balances with Central Banks | 50,836,249 | - | - | - | **50,836,249** |
| Financial Assets held for trading | 596,979 | 379,469 | - | - | **976,448** |
| Loans and advances to credit institutions | 311,452,201 | 4,473,799 | - | - | **315,926,000** |
| Loans and advances to customers | 44,191,578 | 15,348,811 | 1,908,054 | 15,380,366 | **76,828,809** |
| Investments held to maturity | 7,288,565 | - | 26,374,916 | 52,545,232 | **86,208,713** |
| **TOTAL** | **414,365,572** | **20,202,079** | **28,282,970** | **67,925,598** | **530,776,219** |
| **Instrument Category (financial liabilities)** | | | | | |
| Debts to central banks | - | - | - | - | - |
| Financial liabilities held for trading | 536,340 | 392,121 | - | - | **928,461** |
| Amounts owed to credit institutions | 18,654,616 | - | - | - | **18,654,616** |
| Customer Deposits | 454,941,978 | 6,756,511 | - | - | **461,698,489** |
| Other Liabilities | 8,471,616 | 1,177,249 | 1,083,804 | 157,130 | **10,889,799** |
| Engagements | 1,846,483 | 44,642,749 | 313,798 | 102,872 | **46,905,902** |
| **TOTAL** | **484,451,033** | **52,968,630** | **1,397,602** | **260,002** | **539,077,267** |

### 6.4.1. Reporting, measurement and mitigation

The Bank employs a range of liquidity risk assessments and stress tests to assess its ability to meet its obligations when they fall due.

The Bank performs daily assessment on the following regulatory ratios:

- Liquidity Coverage Ratio (“LCR”): The Liquidity Coverage Ratio requires financial institutions to hold a stock of liquid assets to cover the net cash outflow of the Bank over a period of 30 days. The net cash outflow is defined as the difference between the total cash outflows and the minimum between the total cash inflows and 75% of the total cash outflows

- The Net Stable Funding Ratio (“NSFR”): The purpose of the Net Stable Funding Ratio (“NSFR”) is to ensure that banks hold a minimum amount of stable funding based on the liquidity characteristics of their assets and activities over a one-year horizon. The objective is to reduce maturity mismatches between the asset and liability items on the balance sheet and thereby reduce funding risks.

Additionally, the Bank also analyses metrics regarding depositor concentrations, geographical location and currencies on top of quarterly stress tests to assess the Bank’s liquidity resilience.

Below is the calculation of the LCR disclosure template, as of December 31, 2018:

| | *In Euros* | Total unweighted value | Total weighted value |
|---|---|---|---|
| **High-quality liquid assets** | | | |
| 1 | Total HQLA | | 279,279,987 |
| **Cash outflows** | | | |
| 2 | **Retail deposits and deposits from small business customers, of which:** | **19,960,188** | **1,996,019** |
| 3 | Stable deposits | - | - |
| 4 | Less stable deposits | 19,960,188 | 1,996,019 |
| 5 | **Unsecured wholesale funding, of which:** | **450,283,342** | **431,115,673** |
| 6 | Operational deposits (all counterparties) and deposits in networks of cooperative banks | - | - |
| 7 | Non-operational deposits (all counterparties) | 450,283,342 | 431,115,673 |
| 8 | Unsecured debt | - | - |
| 9 | **Secured wholesale funding** | **-** | **-** |
| 10 | **Additional requirements, of which:** | **48,571,576** | **17,297,313** |
| 11 | Outflows related to derivative exposures and other collateral requirements | 699,780 | 699,780 |
| 12 | Outflows related to loss of funding of debt products | - | - |
| 13 | Credit and liquidity facilities | 47,871,796 | 16,597,534 |
| 14 | **Other contractual funding obligations** | **-** | **-** |
| 15 | **Other contingent funding obligations** | **2,418,182** | **-** |
| 16 | **TOTAL CASH OUTFLOWS** | | **450,409,006** |
| **Cash inflows** | | | |
| **17** | **Secure Lending (e.g. reverse repos)** | - | - |
| **18** | **Inflows from fully performing exposures** | 188,129,276 | 188,129,276 |
| **19** | **Other cash inflows** | 749,023 | 749,023 |
| **20** | **TOTAL CASH INFLOWS** | **188,878,299** | **188,878,299** |
| | | | **Total adjusted value** |
| **21** | **Total HQLA** | | **279,279,987** |
| **22** | **Total net cash outflows** | | **261,530,707** |
| **23** | **Liquidity coverage ratio (%)** | | **106.79%** |

Below is the NSFR disclosure:

| ***In Euros*** | **31.12.2018** | **31.12.2017** |
|---|---|---|
| **Available Stable Funding *(ASF)*** | 761,061,766 | 570,280,004 |
| **Required Stable Funding *(RSF)*** | 765,948,605 | 658,968,042 |

# 7. REMUNERATION DISCLOSURE

## 7.1. Introduction

The remuneration disclosure provides information related to the Bank´s remuneration policy and practices for the staff. The disclosure is based on the policies and procedures applicable. As a credit institution, the Bank is in conformity with the following regulatory requirements:

- Provisions of the Law of 23 July 2015 on the transposition of the Directive 2013/36/EU (CRD IV) and CSSF Circular 11/505.
- CSSF Circular 15/622 describing the procedure for higher ratio notification procedure applicable to remuneration policy according to Article 94(1)(g)(ii) of Directive 2013/36/EU ("CRD IV") following its transposition into Luxembourg law via Article 19,7°, Point g of the law of 23 July 2015.
- CSSF Circular 14/585 concerning the transposition of the European Securities Markets Authority's (ESMA) guidelines on remuneration policies and practices (MiFID) - Addition of Annexe V to CSSF Circular 07/307.
- Commission Delegated Regulation (EU) No 604/2014 of 4 March 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards with respect to qualitative and appropriate quantitative criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile.
- Article 450 of the European Regulation (EU) 575/2013 concerning the requirements for terms of disclosure of information related to compensation.
- Circular CSSF 17/658 related to the adoption of the EBA Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU (CRD IV) and disclosures under Article 450 of Regulation (EU) No 575/2013 (EBA/GL/2015/22).
- Directive 2014/65/EU (MiFID II).

## 7.2. Remuneration Policy

The Bank has established a Remuneration Policy ("the Policy") which is validated by the Board of Directors, at least, on a yearly basis[1]. The Policy aims to encourage prudent and sound risk management in order to not exceed the level of the Bank's tolerated risk. For such purpose, the Bank ensures having robust governance arrangements and effective processes to identify, manage, monitor and report the risks that is, or might be, exposed to. The activity is performed by the Risk Management Department, which is supervised directly by the Authorised Management of the Bank.

The Policy takes in consideration the Bank's conservative business strategy and the long-term interests and underlying values of wealth preservation and sustainable growth. This is highlighted by the reasonable percentage of variable remuneration paid, which is specifically designed to preserve a sound risk management culture avoiding conflict of interests with non-sustainable business profitability and excessive risk taking.

The Policy applies to all employees of the Bank and placing emphasis on takers of material risks as required by the Capital Requirements Directive. The implementation of the Policy is responsibility of the Authorized Management with the support of the Human Resources Department. The application of the Policy is reviewed yearly by the control functions and is also subject to a review by both the internal and external auditors of the Bank, before it's finally submitted for approval for the Board of Directors, at least, on an annual basis.

[1] In the review and update of the 2018 Remuneration Policy, the Bank used the services of external consultant Talantlers. The activity was closely supervised by the Human Resources department. It is noted also that no material changes were made to the Remuneration Policy when compared to the 2017 document.

## 7.3. Performance Management

In order to encourage its employees to participate as actively as possible in the achievement of the strategic objectives, controls and business goals, while respecting the work contracts in effect over time, the Bank applies, in a general manner and whenever possible, compensation polices which provides a fixed and a variable component based on the results achieved when pursuing the assigned objectives. The adoption of an adequate compensation mechanism allows to:

- Guide and encourage positive desired behaviours
- Influence motivation / personal expectations
- Support the achievement of strategic objectives in the long and short term.
- Recognize and reward individual / collective contributions
- Contribute to the competitiveness and the attractiveness of the Group in respect to other competitors in the labour market
- Retain the employees

The Bank has defined the remuneration structure for its employees based on the following two elements:

- **Salary**: The fixed part of the remuneration (including any benefits provided for in the collective agreement and / or the contract of employment). Fixed remuneration has the objective to reflect the relevant professional experience and organisational responsibilities required on the job description.

- **Bonus**: The variable part of the remuneration paid, which is linked to financial and non-financial performance. Its determined by an evaluation which combines the individual, business line and overall Bank´s performance.

The Remuneration Policy of the Bank is, as far as possible, adapted to the actual duties and responsibilities as set out in the job descriptions. It is also adapted to the commitment demonstrated, according to the position held, to the seniority and experience acquired by the employee. The assignment of an adequate remuneration makes it possible to positively influence employees towards professional and ethical behaviour. Equitable remuneration further enables the value of merit to be put into practice.

## 7.4. Limits to variable compensation

The Bank has set a maximum ceiling for the variable component. Pursuant to Article 38.6 (g) of the Act of 23 July 2015 transposing CRD IV, the variable component may not exceed 100% of the fixed component for material risk takers. Any approval of a higher ratio shall be made in agreement with the Board of Directors and following a specific procedure.

No employee of the Bank shall be entitled to a total remuneration of no more than EUR 1,000,000 during a working year.

Furthermore, as of today, the Bank does not remunerate its employees on the "Market Desk & Key Clients" activities based on their performance or established objectives in relation to the "trading" activity. In addition, the remuneration of employees of the Bank does not plan for the past year a component that would depend on financial or budgetary objective.

The Board of Directors is also entitled to require any employee, including its own members (the Management Body) to reimburse all or part of the variable compensation, granted or already paid, on the basis of data or elements, which subsequently prove to be fraudulent[2].

## 7.5. Identification and Remuneration of Material Risk Takers

The Remuneration Policy of the Bank applies to different categories of employees. In general terms, the Bank differentiates between Material Risk Takers from Other Employees.

Material Risk Takers are identified by a review procedure taking in several pre-established criteria, such as (but not limited to): size, nature and/or complexity of its activities, as well as its place in the organization or the type of information handled.

The analysis is leaded by the Authorized Management, with the assistance of the Human Resources department and the support of the Control Functions, in accordance to the applicable laws and regulations. Finally, the analysis is approved by the Nomination and Remuneration Committee of the Bank, on an annual basis.

For each of the categories, the risks associated with these categories are detailed, as is the number of persons involved (as of 31 December 2018):

| Category | Eligibility for variable remuneration | Risk taker | Number of persons concerned |
|---|---|---|---|
| Members of the Board of Directors (*) | No | Material | 5 |
| Members of the Direction<br>- *Managing Director*<br>- *Chief Operating Officer* | Yes | Material | 2 |
| Control Functions<br>- *Chief Internal Auditor*<br>- *Chief Risk Officer*<br>- *Chief Compliance Officer and Deputy Chief Compliance Officer* | Yes | Material | 4 |
| Commercial, Operational and support activities<br>- *Head of Accounting & Mgt Secretary (including HR).*<br>- *Head of IT Dept.*<br>- *Head of Corporate and Fund Services Dept.* | Yes | Material | 3 |
| Others (Employees not included in the previous categories) | Yes | N/A | 71 |

*(*) Including the Managing Director*

[2] Application of this provision is according to the definitions setup in the Remuneration Policy

## 7.6. Breakdown of total remuneration by type of Risk Taker

Remuneration of the staff identified as Risk Takers in relation to performance at the end of 2018:

| | |
|---|---|
| Number of Identified Risk Takers | 13 |
| Annual fixed Remuneration granted | 1,723,089 Eur |
| Variable remuneration granted | 296,500 Eur |
| Number of identified Risk Takers with total 2018 remuneration above 1m Euros | 0 |
| Reduced amount through performance adjustments (holdback/clawback) | 0 |

No employee identified as Risk Taker received a variable compensation which would depend on financial or sales related objectives.

As of December 31, 2018, the following two summary tables show the share of variable remuneration on the total remuneration paid:

| **Risk takers:** | **Number of people** | **Variable portion of total compensation** [3] | **Pension contribution** | **Long-term indemnities** |
|---|---|---|---|---|
| Members of the Board of Directors (*) | 5 | n/a | *None* | *None* |
| Members of the Direction<br>*- Managing Director*<br>*- Chief Operating Officer* | 2 | 15 % | *None* | *None* |
| Control Functions<br>*- Chief Internal Auditor*<br>*- Chief Risk Officer*<br>*- Chief Compliance Officer and Deputy Chief Compliance Officer* | 4 | 4 % | *None* | *None* |
| Commercial, Operational and support activities<br>*- Head of Accounting & Mgt Secretary (including HR).*<br>*- Head of IT Dept.*<br>*- Head of Corporate and Fund Services Dept* | 3 | 8 % | *None* | *None* |

*(*) Including the Managing Director*

| **Employees of the Bank** | **Number of people** | **Variable portion of total compensation** |
|---|---|---|
| Non-Risk Takers (other employees) | 71 | 73% |

[3] Given that variable compensation, consisting exclusively of a bonus / bonus for the relevant period, is only paid at the beginning of the following year.