

Bank of China (UK) Limited

**Annual Report and Financial Statements
For the year ended 31 December 2016**

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Chairman's Statement

The UK economy showed considerable resilience in the period following the June Referendum decision to leave the EU. GDP was broadly around 2% higher in 2016 with the unemployment rate falling to 4.8%, an eleven year low. In this context, Bank of China (UK) Limited achieved stable growth last year.

The bank's financial performance in 2016 was satisfactory, as significant growth was achieved in the underlying business. Management in London is to be congratulated on this performance since it was achieved without the advantage of a number of exceptional and one-off items of income, that were received in 2015 and substantially inflated the net profit position for that year.

The developing relationship with China is a very positive factor for the UK economy in general. The increasing involvement of outgoing Chinese companies in major infrastructure projects in the UK is further evidence of increasing co-operation between China and the UK. These high profile projects will provide the bank with significant business opportunities, further reinforcing its role as the first choice bank in the UK for China related business. In our view, such business opportunities result from a wider context of three internationalisations: the internationalisation of the Chinese economy which is now led by large M&A deals and overseas direct investment, the internationalisation of Chinese banks who are matching Chinese corporates' overseas footprints, and the internationalisation of Bank of China which is currently transforming its business model to better serve its customers in China and overseas. As the global financial centre, London is set to become a leading hub for these efforts.

Looking forward, there are numerous external factors that may impact the bank's business either directly or indirectly. Among these, the UK's process of leaving the EU brings uncertainties to our business but we believe the effects of that on the UK economy remain to be seen. However, increasingly positive Sino-British relationships and the improved market perception of the growth potential of the UK economy, in both the short to medium term, point to a positive environment in which the Board is confident that the management team will deliver further development in the bank's business.

Yingxin Gao

Chairman of the Board of Directors

Chief Executive Officer's Statement

Business conditions in the UK in 2016 were impacted by the decision taken by voters to leave the EU – referred to as the “Brexit” event. This unexpected result caused significant volatilities in the financial markets. The UK economy however, reacted positively in the period following the referendum decision. Despite such an eventful year, Bank of China (UK) Limited achieved stable growth over the course of year.

During 2016, the bank's underlying retail business continued to grow throughout 2016, achieving total assets of £1.55 billion, an increase of 20% over the previous year. However, the bank's net profit after tax for 2016 was £35.7 million, a reduction of £9.8 million over 2015, which was still 4.9% in excess of the 2016 target set for management by the Board. This can be explained by reference to the bank's 2015 report and accounts which confirm that 2015's profitability was significantly enhanced by additional one-off items of income.

The strategic direction of the bank's retail business in the UK remains focused on three main areas: providing retail services to the UK Chinese community, developing our services to the UK SME sector and supporting those outgoing Chinese companies establishing operations in the UK. The bank successfully launched new products for all three target sectors in 2016 in support of its continuing policy of achieving prudent organic business growth in these target market sectors.

Looking forward, the short-term impact of Brexit is unlikely to adversely affect the bank's UK business, although political uncertainty in the EU, caused by imminent elections in France, Germany and Italy, may negatively impact EU economies in the short to medium term. On a positive note, the continuing improvement in Sino-British relations and in particular, the involvement of Chinese companies in the UK Government's key infrastructure projects, are expected to have a positive impact on the UK economy and will provide significant opportunities for the management team to further develop the bank's business.

Yu Sun
Chief Executive Officer
Board Director

Directors' report

Principal Activities

Bank of China (UK) Limited ("BOC UK" or the "bank") is a full service bank offering retail, corporate and trade finance services in the United Kingdom (the "UK"). The bank is a wholly owned subsidiary of Bank of China Limited, Beijing ("BOC"). The bank is regulated by the Prudential Regulation Authority and Financial Conduct Authority and authorised by the Prudential Regulation Authority.

BOC UK was incorporated in England and Wales as a private company with limited liability on 29 March 2007. The bank's registration number at Companies House is 6193060.

Our retail activities focus on branch banking. The bank offers standard high street retail banking services including current accounts, savings accounts, debit and credit cards, mortgage products and business loans. Our corporate and trade finance business encompasses funding for Chinese corporates seeking to expand in the UK and Europe. Syndication plays an important role for the bank in gaining access to European corporate clients.

Future Developments

The directors intend to maintain the strategy and policies that have generated growth and preserved value of the business in recent years by continuing to provide banking services to the Chinese community based in the UK.

The bank is subject to a number of factors that could cause its future results to differ materially from current expectations. These factors are uncertainties concerning the current and future business/economic climate and risks which are naturally inherent in a banking environment. The current business climate is subject to uncertainties in 2017 and beyond, most notably:

- The rate and sustainability of growth in relevant economies, particularly the UK and Eurozone
- The potential impact of UK exit from the EU
- The potential impact of consumer price changes on economic growth and corporate profitability
- The rate and extent of anticipated interest rate changes
- Risk of potential decline in property values

Dividends

The directors recommend the payment of a dividend of £35,690,000 in 2017 (2016: £45,450,000).

Directors' Interest

The directors of the bank who were in office during the year and up to the date of signing the financial statements were:

Mr. Yingxin Gao	Chairman
Mr. Yu Sun	Chief Executive Officer
Mr. Stephen Hinds	Chief Operating Officer
Mrs. Wei Shi	Chief Risk Officer
Mr. Christopher Fitzgibbon	Non-Executive (resigned 1 January 2017)
Ms. Li Ren	Non-Executive
Mr. Jonathan Spence	Non-Executive
Mr. Charles Hardy	Non-Executive (appointed 20 October 2016)
Dr. Gerard Lyons	Non-Executive (appointed 20 October 2016)

None of the directors who held office at the end of the financial period had any disclosable interest in the shares of the bank at that date.

During the year, the board determined that Mr. Jonathan Spence, Mr. Charles Hardy, Dr. Gerard Lyons and Mr. Christopher Fitzgibbon performed their roles as independent non-executive directors.

Directors' report (continued)

Board and Committee Meetings

	Board	Remuneration Committee	Audit Committee	Risk Committee
Scheduled Meetings	4	4	4	4
Attended Meetings:				
Mr. Yingxin Gao	3	-	-	-
Mr. Yu Sun	4	4	-	4
Mr. Stephen Hinds	4	-	4	4
Mrs. Wei Shi	3	-	3	3
Mr. Christopher Fitzgibbon	4	-	4	-
Ms. Li Ren	4	-	-	-
Mr. Jonathan Spence	2	4	2	4
Mr. Charles Hardy	1	1	1	-
Dr. Gerard Lyons	1	1	-	1

Directors' Remuneration

Information on remuneration of the directors of BOC UK, in accordance with the Companies Act 2006, is disclosed in Note 14 to the financial statements.

Directors' Indemnities

The BOC UK Board believes that it is in the best interests of the bank to attract and retain the services of the most able and experienced directors by offering competitive terms of engagement, including the granting of indemnities on terms consistent with the applicable statutory provisions. Qualifying third party indemnity provisions (as defined by Section 234 of the Companies Act 2006) were accordingly in force during the course of the financial period ended 31 December 2016 for the benefit of the directors and, at the date of this report, are in force for the benefit of the directors in relation to certain losses and liabilities which they may incur (or have incurred) in connection with their duties, powers or office.

Going concern assessment

The Board has given its consideration to the going concern status of the bank as at the reporting date. After due consideration the Board is of the opinion that the bank will continue as a going concern for the foreseeable future, generating cash flows from its continuing operations, but taking additional comfort from a two year financial forecast to support this assumption.

Financial Instruments

The bank's principal financial risk management objectives and policies including its exposure to credit risk, liquidity risk and market risk are set out in Note 6, pages 30 to 40, to the financial statements.

Employees

- Diversity

The bank is committed to employment policies, which follow best practice, based on equal opportunities for all employees, irrespective of sex, race, colour, disabilities or marital status. The bank gives full and fair consideration to applications for employment from disabled persons, having regard to their particular aptitudes and abilities. Appropriate arrangements are made for the continued employment and training, career development and promotion of disabled persons employed by the bank. If members of staff become disabled the bank continues employment either in the same or an alternative position, with appropriate retraining being given if necessary.

- Employee involvement

The bank systematically provides employees with information on matters of concern to them, consulting them or their representatives regularly, so that their views can be taken into account when making decisions that are likely to affect their interests. Employee involvement in the bank is encouraged, as achieving a common awareness on the part of the employees of the financial and economic factors affecting the bank plays a major role in maintaining its performance. The bank encourages the involvement of the employees by means of an employee representative forum which is held on a quarterly basis and chaired by a member of the Executive Management Committee.

Directors' report (continued)

Disclosure of Information to the Auditors

The directors who held office at the date of approval of this Directors' Report confirm that:

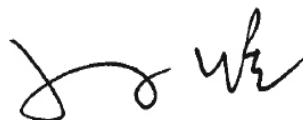
- So far as they are each aware, there is no relevant audit information of which the bank's auditors are unaware.
- Each director has taken all steps that he/she ought to take as a director to make himself/herself aware of any relevant audit information and to establish that the bank's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 (2) of the Companies Act 2006.

Ernst & Young LLP have indicated their willingness to continue in office and a resolution that they be reappointed will be proposed at the 2017 AGM.

1 Lothbury
London
EC2R 7DB

On behalf of the Board,

A handwritten signature in black ink, appearing to be 'Yu Sun', written in a cursive style.

Yu Sun
Chief Executive Officer
Board Director

12 April 2017

Strategic report of the Directors

Business Review

As at 31 December 2016, Bank of China (UK) Limited ("BOC UK" or the "bank") had total assets of £1,549,898,000 (2015: £1,291,410,000).

The bank's assets are primarily financed by retail and intra-group deposits. The bank continues to focus its attention on developing the customer deposits base and this reflects our determination to develop our corporate banking services as well as to help in meeting the bank's funding requirements.

The bank generated a post-tax profit of £35,690,000 during 2016 (2015: £45,450,000).

The bank disposed of its investment in Bank of China (Suisse) S.A. during 2012 but continues to enjoy a share of income from the client base that existed on the signing of the sale and purchase agreement (SPA) dated 20 July 2012. Under the terms of the agreement, this arrangement will persist until 30 September 2017.

Retail Banking

In order to implement the group development strategy of "Serving Society, Delivering Excellence", maintaining our leading position against local Chinese peers and continuously enhancing the profit contribution of the bank, the personal banking business line has a clearly defined development plan for the next five years. This follows on from the products, services, channels, and the Head Office support perspective, drawing out the blue ocean strategic plan step by step in 2016.

With the strong support of the Head Office, the bank and domestic branches have established good relations to promote cross border business focusing on creating a robust financial services platform. The Interest only mortgage product has been launched, the Operational Working Group has been set up and long-term frozen dormant accounts have been cleared. This optimises the bank's personal customer structure and lays a solid foundation for future business development and customer service in 2017 and beyond.

Corporate Banking

Seizing on the opportunity of China's economic growth as well as fast growing China-UK bilateral trade and investment, the bank continues to develop its relationships with existing and target corporate clients by offering a comprehensive range of banking products and services including credit facilities, deposits, trade services, cash management, foreign exchange, debt capital market and RMB related products. As well as addressing the UK market, the bank is also focused on targeting new relationships in Europe, the Middle East and Africa.

A key objective for our corporate banking business is to be the first choice for China related business in the local market, which includes companies involved in trade and investment between the UK and China as well as China's "Going Out" enterprises in the UK, Europe and Africa regions.

Financial Markets

The Financial Markets and Financial Institutions department comprise three divisions: foreign exchange, money market and fixed income investments. During the year, these activities continued to focus upon efficient liquidity management, the funding requirements of the bank's activities and servicing client needs. There was no proprietary trading activity during the year under review.

Principal Risks and Uncertainties

The effect of one or a combination of factors, referred to on page 5 under future developments, could make the business environment a challenging one with regard to possible credit impairments being incurred and difficulty in identifying new assets/business opportunities that meet the bank's risk appetite.

Principal Risks: The bank is exposed to a number of financial and non-financial risks namely credit risk, market risk, liquidity risk and operational risk. Of these risks, credit risk and liquidity risk are deemed to be the principal risks which the bank is exposed to.

The Board, Board level Committees and other senior key staff carry out a continual assessment of the principal risks facing the bank and are certain that systems and controls are sufficiently robust to identify threats to its business model, future performance, solvency or liquidity.

Credit risk is the risk of financial loss to the bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations and is considered a principal risk due to the composition of the bank's balance sheet and lending being its primary business.

Strategic report of the Directors (continued)

The bank has established a set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that arises through the bank's normal business activities. These policies, procedures and limits are regularly reviewed in light of changes in markets and business strategies.

Further information on the management of credit risk is disclosed in Note 6 (a) of the notes to the financial statements.

Liquidity risk is the risk that the bank is unable to meet its obligations as they fall due resulting in an inability to support normal business activity and/or failing to meet liquidity regulatory requirements. The bank is exposed to the risk that it will be unable to meet its obligations as they fall due, arising from the differing maturity profiles of its assets and liabilities. To mitigate its exposure, the bank places limits on the mismatch of maturity dates and by holding a stock of liquid assets which could be sold at short notice if the need arose. The Board, as part of the going concern assessment, took additional comfort from a two year financial forecast which also provided comfort on the bank's assessment of its exposure to liquidity risk. A further mitigating factor is a committed short-term loan facility granted by the bank's parent company. Further information on the management of liquidity risk is disclosed in Note 6 (b) of the notes to the financial statements.

Key Performance Indicators

The bank's main Key Performance Indicator ("KPI") is monitoring its financial performance against financial targets set at the beginning of the financial year. The financial targets monitored include; the main income streams of the bank by income type and business department, operating expenses and net profit after tax.

1 Lothbury
London
EC2R 7DB

On behalf of the Board,



Yu Sun
Chief Executive Officer
Board Director

12 April 2017

Corporate Governance Statement

Bank of China (UK) Limited (“BOC UK” or the “bank”) is committed to the principles of corporate governance contained in the UK Corporate Governance Code (the “Governance Code”) issued by the Financial Reporting Council in April 2016. Although the bank is not required to comply with the Governance Code, it observes the provisions of the Code where practical and relevant, as a matter of good governance.

Corporate Governance Framework

The bank’s corporate governance framework centres on the Board of Directors (the “Board”), which provides guidance and effective oversight of the senior management of the bank and of its subsidiaries. In order to run the business effectively, the Board delegates responsibility for the day-to-day management of the bank to the Chief Executive Officer, who is supported by the Executive Management Committee, which he chairs.

Board and Committee meetings are arranged in advance to ensure, as far as possible, that directors can manage their time commitments. All directors are provided with supporting papers and relevant information for each meeting and are expected to attend, unless there are exceptional circumstances that prevent them from doing so.

In the event that a director is unable to attend a meeting, he/she will still receive the papers for the meeting and will normally discuss any matters they wish to raise with the chairman of the meeting, to ensure their views are taken into account. In addition, all directors are able to discuss any issues with the Chairman of the Board and/or the Chief Executive Officer at any time. During the year ended 31 December 2016, it is considered that all directors contributed the time necessary to discharge their responsibilities to the Board.

The Chairman of the Board works closely with the Company Secretary to ensure that accurate, timely and clear information flows to the Board. Supporting papers for scheduled meetings are distributed in advance of each meeting. All directors have access to the services of the Company Secretary.

Following the provisions in the Articles of Association the appointment or removal of a member of the Board requires the approval of the shareholders. Independent non-executive directors are appointed for three-year renewable terms which may, in accordance with the Articles of Association, be terminated without notice or payment of compensation.

Board Effectiveness

Under United Kingdom (the “UK”) Company Law, directors must act in a way they consider, in good faith, would be most likely to promote the success of the bank for the benefit of the shareholders as a whole. In doing so, the directors must have regard (amongst other matters) to the following:

- The likely consequences of any decision in the long-term
- The interests of the bank’s employees
- The need to foster the bank’s business relationships with suppliers, customers and others
- The impact of the bank’s operations on the community and the environment

The Board is responsible to shareholders for creating and delivering sustainable shareholder value through the management of the bank’s businesses. It therefore determines the goals and policies of the bank to deliver such long-term value and provides overall strategic direction within a framework of rewards, incentives and controls. The Board aims to ensure that management strikes an appropriate balance between promoting long-term growth and delivering short-term objectives.

Board Effectiveness (continued)

The Board delegates to the Audit Committee the responsibility for ensuring that management maintain systems of internal control that provide assurance of effective and efficient operations, internal financial controls and compliance with UK laws and regulations. It has fulfilled its obligation by assessing their effectiveness during the year. In carrying out this responsibility, the Board and the Audit Committee have had regard to what is appropriate for the bank's business and reputation, the materiality of the financial and other risks inherent in the business, and the relative costs and benefits of implementing specific controls.

The Board is also the decision-making body for all other matters of such importance as to be of significance to the bank as a whole because of their strategic, financial or reputational implications or consequences.

A typical Board meeting receives reports from the Chief Executive Officer and will also be presented with an update on the execution of strategy in the main businesses and functions. It will also receive reports from each of the principal Board Committees and may also receive a report from the Company Secretary on any relevant corporate governance matters.

Chairman and Chief Executive Officer

The roles of the Chairman and the Chief Executive Officer are separate. The Chairman's main responsibility is to lead and manage the work of the Board to ensure that it operates effectively and fully discharges its legal and regulatory responsibilities. The Board has delegated the responsibility for the day-to-day management of the bank to the Chief Executive Officer, who is responsible for recommending strategy to the Board, leading the executive directors and for making and implementing operational decisions.

Board Balance and Independence

The Board has collective responsibility for the success of the bank, however, executive directors have direct responsibility for business operations, whereas non-executive directors are responsible for bringing independent judgment and scrutiny to decisions taken by the Board, providing objective challenge to management. The Board can draw on the wide range of skills, knowledge and experience they have built up as directors of other companies and as business leaders.

The Governance Code sets out circumstances that the Board may find relevant when determining the independence of a non-executive director. The Board considers that the following behavior is essential in order for the Board to conclude that an individual is independent:

- Provides objective challenge to management
- Is prepared to challenge others' assumptions, beliefs or viewpoints as necessary for the good of the bank
- Questions intelligently, debates constructively, challenges rigorously and makes decisions dispassionately
- Is willing to stand up and defend their beliefs and viewpoints in order to support the ultimate good of the bank
- Understands the bank's business and affairs to enable them to properly evaluate the information and responses provided by management

All directors must report any changes in their circumstances to the Board and the shareholders reserve the right to terminate the appointment of a director if there are any material changes in their circumstances that may conflict with their commitments as a director of the bank, or that may impact on their independence.

Information and Professional Development

A three-part training programme is in place for Directors. This comprises:

- Induction training, when they join the Board
- Training and awareness of the businesses of the bank
- Training and awareness of external technical matters

A presentation is given to all new Directors, which outlines their responsibilities as a Director of a UK limited company and provides an overview of the bank and its businesses. Each new Director then has a tailored induction program to further familiarise themselves with the bank and its businesses. This takes the form of sessions with each of the executive directors and the heads of the main bank functions and includes opportunities to visit operational sites to meet with senior management and employees. Once they have completed the first part of their induction, and have a good overview of the bank, they then have further sessions with the executive directors and senior managers from each of the principal business units to gain a detailed and in-depth understanding of their business, which includes the challenges, opportunities and risks that are faced by each.

During 2016, the Board was provided with regular updates on Corporate Governance and Regulatory Responsibilities.

Performance Review and Evaluation

As with the previous year, annual performance contracts were established for the executive Directors for 2016 to assess their performance across five key performance areas aligned to the bank's 'balanced scorecard' approach to performance management, being:

- Financial
- Business Processes and Technical Skills
- Customer Focus
- Leadership
- Team

The performance contracts provide an overall summary of their achievements throughout the year in their roles as Directors of the bank.

Furthermore, the effectiveness of the Board and the three Board level committees is assessed by participants of each of these groups each year with plans to engage external consultants to perform a further review.

The internal performance evaluation process takes the form of a detailed questionnaire for the Board collectively and for each of the Board level committees. Submitted results are reported to the Board and relevant Board Committees which are then discussed thoroughly, agreed by all parties involved with detailed action plans formulated for future implementation.

Internal Control

The Board is responsible for the bank's system of internal control. It is designed to facilitate effective and efficient operations and to ensure the quality of internal and external reporting and compliance with applicable laws and regulations. In devising internal controls, the Board considers the nature and extent of the risk, the likelihood of it crystallising and the cost of controls.

The Board receives regular reports and updates from the Executive Management and the Audit Committee on the effectiveness of the bank's internal control system. The system of internal control is also subject to regulatory oversight.

Remuneration Committee Report

The Chairmanship of the Remuneration Committee ("the Committee") has recently passed from Mr. Jonathan Spence to Dr. Gerard Lyons. We thank Mr. Spence for his fine contribution to the running of the Committee during his tenure.

The Remuneration Committee comprises three directors, Dr. Lyons the Committee Chairman, Mr. Charles Hardy (non executive director), Mr. Yu Sun (Chief Executive Officer and Executive Director). Ms. Tracey Rutherford, Head of Human Resources ("HR") is also a Committee member.

The Committee is responsible for supporting and overseeing the implementation of an effective remuneration programme within the bank and ensuring that the bank meets all applicable statutory and regulatory requirements within an effective human resource function. The committee is not involved in setting the remuneration of its members.

The Committee aims to meet on a quarterly basis and met on four occasions in 2016. Key activities undertaken were as follows:

- Review, approval and monitoring of the HR annual work plan (including corporate culture project, implementation of the succession planning framework, annual reward programmes, impact and implementation of the Senior Manager & Certification Regime, review of the Final Salary Pension Scheme, consideration of the implementation of a HR information system with integrated payroll system to ensure efficiencies can be considered in relation to HR processes whilst ensuring HR information and management information reporting requirements can be met in the future).
- Review of the headcount budget for 2016 and achievement of headcount increase in alignment with business strategy and staff turnover data throughout 2016 with appropriate actions being taken should anything adverse be noted. In conjunction with staff development strategies, the Committee approved the Training and Development plan for 2016 to primarily focus on various technical training programmes including:
 - SME Lending (Banking, Branches, Corporate Banking)
 - Country and Sovereign Risk (Risk Management, Corporate Finance Unit and Financial Markets)

Remuneration Committee Report (continued)

- Internal regulatory training including: Anti Money Laundering (“AML”), Anti Bribery & Corruption, Enhanced AML training
 - Essential Letter Writing Skills
 - Customer Service Skills
 - Management Development Training including: Coaching Workshops, Performance Management and Succession Planning
 - Internal Workshops including: Business Continuity and Introduction to Corporate Values
 - IT skills training
 - Cultural Awareness training
 - Reputational Risk/Conduct Risk
- Continued implementation of Professional Bankers SME qualification in alignment with Performance Management strategies, the Committee approved the implementation of the Key Performance Indicator framework at Executive Management, Departmental and individual employee level to clarify measurement/target application, weighting application and moderation of performance ratings aligned to meet the bank’s and employees objectives.
 - The Committee approved the year-end performance management process which was also aligned to the annual salary review and discretionary bonus allocations.
 - The Committee continued to review the implementation of the FCA Remuneration Code and the impact on the bank and employees and reviewed the Remuneration Policy and application and impact of Capital Requirements IV Directive. In addition, they considered the outcome of the European Banking Authority’s remuneration guidelines on UK remuneration strategies.
 - The Committee considered the implementation of a formalised Career Development Framework which will outline the departmental development framework to clarify employees future career opportunities.

Audit Committee Report

The Chairmanship of the Audit Committee (“the Committee”) has recently passed from Mr. Christopher Fitzgibbon to Mr. Charles Hardy. We thank Mr. Fitzgibbon for his sterling work leading the Committee over the last nine years.

During 2016, there were four meetings, on a quarterly basis, all chaired by Mr. Fitzgibbon, with Mr. Jonathan Spence (a voting member) in attendance for two of these, and Mr. Stephen Hinds, Chief Operating Officer (a non-voting member) attending them all. In addition, Mr. Hardy attended the December meeting. The Chief Financial Officer, the Chief Risk Officer, the Head of the Risk Management Department, the Head of the Legal & Compliance Department, the Head of the Internal Audit Department and the external auditors were all standing attendees.

During the course of the year, the Committee considered: the effectiveness of the bank’s internal control systems; risk management; and compliance with financial services legislation and regulations, via the following key activities:

- The Committee received and reviewed all internal audit reports issued during the year. Progress in resolving the issues arising from those reports was monitored.
- Quarterly reports were received from the Risk Management and Legal and Compliance Departments and these were reviewed and discussed.

In addition, the Committee:

- Considered and approved the annual Internal Audit Department Plan.
- Approved the scope of the external auditors’ work and separately assessed their effectiveness. Non-audit services were also undertaken by the external auditors as disclosed in Note 13 .
- Carried out an assessment of the effectiveness of both the Internal Audit Department and the Committee itself. Both were felt to be operating effectively. The adequacy of the resources available to the Department was also considered, and deemed to be satisfactory.
- Reviewed in detail the annual financial statements and the quality and acceptability of the related accounting policies, practices and financial reporting disclosures.

After each meeting, a report to the Board was presented on the principal matters discussed to ensure all Directors were informed of the Committee’s work.

Board Risk Committee Report

The Board Risk Committee (“the Committee”) comprises three directors: Mr. Jonathan Spence (non-executive director), Chairman and Mr. Yu Sun (Chief Executive Officer) are voting members; Mrs. Wei Shi (Chief Risk Officer) is a non-voting member.

The Committee is responsible for the oversight and implementation of risk strategy and risk appetite within the bank, oversight of risk management performance and the executive committees including Compliance Committee, Operational Risk Committee, Assets and Liabilities Management Committee, Credit Risk Policy Committee and Credit Committee. The Committee also approves all credit limits, provisions (and/or write-offs) above the delegated limits of the Chief Executive Officer.

The Committee has regular meetings on a quarterly basis. During the course of these meetings it has also reviewed, discussed and challenged the bank’s Risk Appetite Statement, Individual Capital Adequacy Assessment (“ICAAP”) and Individual Liquidity Adequacy Assessment (“ILAAP”) documents prior to them being presented to the Board for approval.

In addition, during 2016 a further nine committee meetings were held to consider specific credit proposals, or policy proposals

Country by Country Reporting

Further information regarding the bank’s approach to the requirements of increased financial and tax transparency of the Capital Requirements Directive (“CRD IV”), as enacted by the Financial Services and Markets Act 2000, will be published on the bank’s website shortly after the approval of these financial statements at www.bankofchina.com/uk.

Pillar III Disclosures

Further information regarding the bank’s approach to risk management and its capital adequacy are contained in the unaudited disclosures made under the requirements of Basel II Pillar 3 (the Pillar 3 disclosures). These disclosures will be published on the bank’s website shortly after the approval of these financial statements at www.bankofchina.com/uk.

Statement of Directors' Responsibilities in Respect of the Directors' Report, Strategic Report and the Financial Statements

The following statement, which should be read in conjunction with the independent auditors report on page 16, is made by the directors to explain their responsibilities in relation to the preparation of the Director's Report, Strategic Report and Financial Statements.

The directors are responsible for preparing the Directors' Report, Strategic Report and the Financial Statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and applicable law.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the bank and of the profit of the bank for that period.

In preparing these financial statements, the directors are required to:

- select suitable accounting policies in accordance with IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements of IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the bank's financial position and financial performance; and
- state that the bank had complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping adequate accounting records that disclose with reasonable accuracy at any time, the financial position of the bank, and enable them to ensure that the financial statements comply with the Companies Act 2006.

They are also responsible for safeguarding the assets of the bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are satisfied that the bank has adequate resources to continue in business for the foreseeable future. For this reason, the financial statements are prepared on a going concern basis.



Yu Sun
Chief Executive Officer
Board Director
12 April 2017

Independent Auditors' Report to the Members of Bank of China (UK) Limited

We have audited the financial statements of Bank of China (UK) Limited for the year ended 31 December 2016 which comprise the Statement of Financial Position, the Statement of Comprehensive Income, the Statement of Cash Flow, the Statements of Changes in Equity and the related notes 1 to 34. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 15, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report and Financial Statements to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the bank's affairs as at 31 December 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

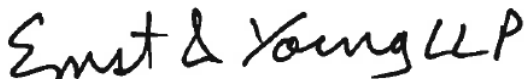
Independent Auditors' Report to the Members of Bank of China (UK) Limited (continued)

Matters on which we are required to report by exception

In light of the knowledge and understanding of the bank and its environment obtained in the course of the audit, we have identified no material misstatements in the Strategic Report or Directors' Report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



Kenneth Eglinton (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
12 April 2017

Bank of China (UK) Limited
Financial Statements for the year ended 31 December 2016

Income Statement

£000	Note	12 months to 31 December 2016	12 months to 31 December 2015
Interest income from financial investments		1,216	1,134
Other interest income		33,375	24,511
Interest expense		(4,629)	(3,095)
Net interest income	8	29,962	22,550
Fee and commission income		4,029	8,906
Fee and commission expense		(776)	(582)
Net fee and commission income	9	3,253	8,324
Net fair value gain on financial instruments	10	241	511
Foreign exchange gain		2,827	2,482
Other operating income	11	54,899	61,054
Non-interest income		57,967	64,047
Total income		91,182	94,921
Staff costs	12	(32,821)	(29,500)
Other expenses	13	(6,914)	(6,544)
Depreciation of plant and equipment	22	(918)	(965)
Amortisation of intangible assets	23	(144)	(146)
Impairment releases (charges)	20 (c)	(527)	155
Loss on disposal of subsidiary		-	(1,707)
Profit before income tax		49,858	56,214
Income tax expense	15	(14,168)	(10,764)
Profit for the year		35,690	45,450

Statement of Other Comprehensive Income

£000	Note	12 months to	12 months to
		31 December 2016	31 December 2015
Profit for the year		35,690	45,450
Other comprehensive income			
Amounts that will be reclassified to the income statement			
Net change in fair value of available for sale financial assets	20 (b)	(189)	(886)
Net change in fair value of available for sale financial assets transferred to profit or loss	20 (b)	-	-
Net (loss) on available for sale financial assets		(189)	(886)
Income and deferred tax credit relating to components of other comprehensive income	15	45	179
Other comprehensive expense for the year, net of income and deferred tax credit		(144)	(707)
Total comprehensive income for the year		35,546	44,743

Statement of Financial Position

£000	Note	31 December 2016	31 December 2015
Assets			
Cash and cash equivalents	16	311,917	344,019
Loans and advances to banks	18	24,270	62,633
Loans and advances to customers	19	1,159,696	810,776
Derivative financial instruments	17	4,577	8,173
Prepayments, accrued income and other assets	25	4,762	25,831
Available for sale financial investments	21	40,716	35,859
Deferred tax assets	24	562	425
Property, plant and equipment	22	3,276	3,514
Intangible assets	23	122	180
Investment in subsidiary companies	32	-	-
Total assets		1,549,898	1,291,410
Liabilities			
Deposits from banks	26	164,849	136,736
Deposits from customers	27	982,361	737,724
Derivative financial instruments	17	4,150	11,505
Other liabilities	29	13,620	17,145
Accruals and deferred income	30	5,874	4,512
Current tax liabilities		8,680	3,520
Deferred tax liabilities	24	-	-
Subordinated liabilities	28	60,000	60,000
Total liabilities		1,239,534	971,142
Equity			
	31		
Authorised and called up share capital		250,000	250,000
Retained earnings		60,648	70,408
Available for sale reserve		(284)	(140)
Total shareholders' equity		310,364	320,268
Total shareholders' equity and liabilities		1,549,898	1,291,410

The financial statements on pages 18 to 58 were approved by the Board of Directors of Bank of China (UK) Limited and authorised for issue on 12 April 2017. They were signed on its behalf by:



Yu Sun
Chief Executive Officer
Board Director

Statement of Changes in Equity

£000	Issued share capital	Retained earnings	Available for sale reserve	Total
As of 1 January 2016	250,000	70,408	(140)	320,268
Unrealised loss on available for sale investments net of income tax	-	-	(144)	(144)
Profit for the financial year	-	35,690	-	35,690
Total comprehensive income (expense)	-	35,690	(144)	35,546
Dividend paid	-	(45,450)	-	(45,450)
As at 31 December 2016	250,000	60,648	(284)	310,364
As of 1 January 2015	250,000	50,913	567	301,480
Unrealised loss on available for sale investments net of income tax	-	-	(707)	(707)
Profit for the financial year	-	45,450	-	45,450
Total comprehensive income (expense)	-	45,450	(707)	44,743
Dividend paid	-	(25,955)	-	(25,955)
As at 31 December 2015	250,000	70,408	(140)	320,268

Statement of Cash Flows

£000	Note	12 months to 31 December 2016	12 months to 31 December 2015
Cash flows from operating activities			
Profit on ordinary activities before taxation		49,858	56,214
Adjustments for non cash items			
Depreciation and amortisation of plant and equipment and intangible assets		1,062	1,111
Net impairment (gain) loss on loans and advances		527	(155)
Interest receivable from financial investments		(1,216)	(1,134)
Other interest receivable		(33,375)	(24,511)
Interest payable		4,629	3,095
Exchange-rate movements on available for sale investments		(4,958)	704
Changes in operating assets and liabilities			
Change in derivative financial instruments assets held for risk management		3,596	8,000
Change in loans and advances to banks		37,836	144,643
Change in loans and advances to customers		(348,920)	(88,564)
Change in other assets		20,998	1,918
Change in derivative financial instruments liabilities held for risk management		(7,355)	(9,984)
Change in deposits from banks		28,113	96,466
Change in deposits from customers		244,637	(28,175)
Change in other liabilities and provisions		(3,584)	(466)
Adjustment for cash items			
Interest and coupon received		34,582	25,736
Dividend paid		(45,450)	(25,955)
Interest paid		(4,527)	(2,994)
Income tax paid		(7,780)	(10,695)
Net cash (absorbed by) generated from operating activities		(31,327)	145,254
Cash flows from investing activities			
Acquisition of investment securities		(8)	-
Acquisition of property and equipment		(681)	(1,089)
Acquisition of intangible assets		(86)	-
Net cash from investing activities		(775)	(1,089)
Net cash from financing activities			
		-	-
Net (decrease) increase in cash and cash equivalents		(32,102)	144,165
Cash and cash equivalents at beginning of period		344,019	199,854
Cash and cash equivalents at year end	16	311,917	344,019

The statement of cash flows has been prepared under the indirect method.

Notes to the Financial Statements

Note	Note
1. Reporting entity	25. Prepayments, accrued income and other assets
2. Basis of preparation	26. Deposits from banks
3. Significant accounting policies	27. Deposits from customers
4. Critical estimates and judgements	28. Subordinated liabilities
5. New pronouncements	29. Other liabilities
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(d) Capital management	34. Going concern assessment
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Notes to the Financial Statements (continued)

1. Reporting entity

Bank of China (UK) Limited (the “bank”) is a company domiciled and incorporated in the United Kingdom (the “UK”) with its registered office at 1 Lothbury, London EC2R 7DB. The bank is primarily involved in retail and corporate banking. These financial statements present information for the company and not its subsidiaries.

Accounting policies for the year ended 31 December 2016

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to the years presented, unless otherwise stated.

2. Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (the “IFRSs”) as adopted by the European Union (the “EU”), IFRIC interpretations and the Companies Act 2006.

The bank has availed itself of the exemption election in IAS 27 *Consolidated and Separate Financial Statements* that permits an entity to prepare separate financial statements. The bank is a wholly-owned subsidiary of Bank of China Limited (“BOC”), which produces consolidated financial statements available for public use that comply with IFRSs. BOC is domiciled in the People’s Republic of China (the “PRC”), with its head office located at 1 Fuxingmen Nei Dajie, Beijing 100818 PRC. The consolidated financial statements of the BOC Group are publicly available from this address.

The financial statements were authorised for issue by the Board of Directors (the “Board”) on 10 April 2017.

(b) Basis of measurement

The financial statements have been prepared on a going concern basis under the historical cost convention modified to include the fair valuation of certain financial instruments and contracts to buy or sell non-financial items to the extent required or permitted under accounting standards and as set out in the relevant accounting policies.

The following items are measured at fair value:

- Fixed rate loans
- Derivative financial instruments
- Available for sale financial assets

(c) Functional and presentational currency

These financial statements are presented in Sterling (£), which is the bank’s functional currency. Except as indicated, financial information presented in Sterling has been rounded to the nearest thousand.

(d) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expense. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in Note 4.

Notes to the Financial Statements (continued)

3. Significant accounting policies

(a) Revenue recognition

Interest income and expense are recognised in the income statement for all interest-bearing financial instruments, except for those classified at fair value through profit or loss, using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. The effective interest rate is calculated on initial recognition of the financial asset or liability, estimating the future cash flows after considering all the contractual terms of the instrument but not future credit losses. The calculation includes all amounts paid or received by the bank including fees, expected early redemptions and related penalties and premiums and discounts that are an integral part of the overall return as well as direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss (see Note 3 (h)).

Fees and commissions which are not an integral part of the effective interest rate are recognised when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan.

Dividend income is recognised when the right to receive payment is established.

Other operating income is recognised when the bank is entitled to receive that income.

(b) Available for sale financial assets

Debt securities are classified as available for sale and recognised in the statement of financial position at their fair value. Available for sale investments are those intended to be held for an indeterminate period of time and may be sold in response to need for liquidity or changes in interest rates, exchange rates or bond prices. Gains and losses arising from changes in the fair value of investments classified as available for sale are recognised directly in equity, until the financial asset is either sold, becomes impaired or matures, at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement. Interest calculated using the effective interest method is recognised in the income statement.

The fair values of assets and liabilities traded in active markets are based on current bid and offer prices respectively. If the market is not active the bank establishes a fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and other valuation techniques commonly used by market participants.

Purchases and sales of securities and other financial assets and liabilities are recognised on trade date, being the date that the bank is committed to purchase or sell an asset. Available for sale financial assets are initially recognised at fair value inclusive of transaction costs.

These financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the bank has transferred substantially all risks and rewards of ownership.

(c) Derivative financial instruments

Derivative instruments are held for risk management purposes and do not qualify for hedge accounting according to IAS 39. All derivatives are recognised at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and using valuation techniques, including discounted cash flow, as appropriate. Derivatives are carried in the statement of financial position as assets when their fair value is positive and as liabilities when their fair value is negative. All changes in the fair value of the derivative are recognised immediately in the income statement as a component of net fair value gain on financial instruments.

(d) Foreign currencies

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions are recognised in the income statement. Non-monetary assets that are measured at fair value are translated using the exchange rate at the date that the fair value was determined. Translation differences on monetary items, including available for sale investments, measured at fair value are recognised in the income statement.

Notes to the Financial Statements (continued)

3. Significant accounting policies (continued)

(e) Loans and advances to banks and customers

Loans and advances to banks and customers are initially recognised at fair value and subsequently accounted for at amortised cost using the effective interest method less accumulated impairment losses. Loans and advances are initially recognised when cash is advanced to the borrowers at fair value inclusive of transaction costs. Loans and advances are derecognised when the rights to receive cash flows from them have expired or where the bank has transferred substantially all risks and rewards of ownership.

Loans and advances to banks and customers include residential and commercial mortgages, originated and syndicated loans.

(f) Loans designated at fair value through profit and loss (FVPL)

Loans classified in this category are those that have been designated by management upon initial recognition. Management may only designate an instrument at FVPL upon initial recognition when the designation eliminates, or significantly reduces, the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or losses on them on a different basis.

Loans at FVPL are recorded in the statement of financial position at fair value. Changes in fair value are recorded in net fair value gain on financial instruments in the income statement. Interest earned is accrued in interest income using the effective interest rate method, taking into account any discount/premium and qualifying transaction costs being an integral part of the instrument.

(g) Loan commitments, guarantees and other financial facilities

Provision is made for undrawn loan commitments, guarantees and other financial facilities if it is probable that the facility will be drawn and result in the recognition of an asset as an amount less than the amount advanced.

Issued financial guarantees are initially recognised at fair value and adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequent to initial recognition they are measured at the higher of the amount initially recognised less cumulative amortisation (determined in accordance with IAS 18 Revenue where relevant) and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee. Subsequent to initial measurement, changes in the amount of the guarantee are recognised in the income statement.

(h) Impairment of financial assets

At each reporting date the bank assesses whether, as a result of one or more events occurring after initial recognition, there is objective evidence that a financial asset or group of financial assets has become impaired.

The criteria that the bank uses to determine that there is objective evidence of an impairment loss may include:

- Delinquency in contractual payments of principal and/or interest
- Indications that the borrower or group of borrowers is experiencing significant financial difficulty
- Significant legal or regulatory disputes
- Breach of loan covenants or conditions
- Initiation of bankruptcy proceedings
- Other objective evidence indicating impairment of the financial asset

The estimated period between a loss occurring and its identification is determined by local management for each identified financial asset. In general, the periods used vary between one month and three months.

(i) Assets accounted for at amortised cost

If there is objective evidence that an impairment loss has been incurred, an allowance is established which is calculated as the difference between the carrying amount of the asset and the present value of estimated future cash flows discounted at that asset's original effective interest rate. Allowances are established on a case-by-case basis for all of the bank's lending activities which include residential mortgages, personal lending, credit cards and corporate lending. If an asset has a variable interest rate, the discount rate used for measuring the impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised asset reflects the cash flows that may result from foreclosure less the costs of obtaining and selling the collateral, whether or not foreclosure is probable.

Notes to the Financial Statements (continued)

3. Significant accounting policies (continued)

(h) Impairment of financial assets (continued)

(i) Assets accounted for at amortised cost (continued)

For credit card lending where there is no objective evidence of individual impairment the portfolio is collectively assessed for impairment based on historical loss experience and adjusted for current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, such as an improvement in the borrower's credit rating, the allowance is adjusted and the amount of the reversal is recognised in the income statement.

A loan or advance is normally written off, either partially or in full, against the related allowance when the proceeds from realising any available security have been received or there is no realistic prospect of recovery (as a result of the customer's insolvency, ceasing to trade or other reason) and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses recorded in the income statement.

(ii) Available for sale financial assets

If there is objective evidence that an impairment loss has been incurred, the cumulative loss measured as the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss on that asset previously recognised, is removed from equity and recognised in the income statement.

If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the income statement.

(i) Derivatives that do not qualify for hedge accounting

All gains or losses from the changes in fair value of derivatives that do not qualify for hedge accounting are recognised immediately in the income statement.

(j) Derecognition of financial liabilities

The bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

(k) Subsidiaries

Subsidiaries are entities controlled by the bank. Control exists when the bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

The investment in subsidiaries is accounted for at cost less impairment.

A subsidiary is derecognised when the bank loses control over the subsidiary. The carrying value of the subsidiary is measured against the fair value of the consideration received with any resulting gain or loss being recognised through the income statement.

(l) Property, plant and equipment

Tangible fixed assets are included at cost less accumulated depreciation and accumulated impairment losses. The value of land (included in premises) is not depreciated. Depreciation on other assets is calculated using a straight-line method to allocate the difference between cost and residual value over their estimated useful lives, as follows:

Property (excluding land):

- Freehold/long and short leasehold premises: shorter of 50 years or the remaining period of the lease
- Leasehold improvements: shorter of 10 years or the remaining period of the lease

Equipment:

- Furniture and equipment: 4-5 years
- Computer equipment: 4 years
- Motor vehicles: 4 years

Notes to the Financial Statements (continued)

3. Significant accounting policies (continued)

(l) Property, plant and equipment (continued)

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In the event that an asset's carrying amount is determined to be greater than its recoverable amount it is written down immediately. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

(m) Intangible assets

Software acquired by the bank is stated at cost less accumulated amortisation and accumulated impairment losses.

Amortisation is recognised in the income statement on a straight-line basis over the estimated useful life of the software, from the date that it is available for use. The estimated useful life of software is three to five years.

Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In the event that an asset's carrying amount is determined to be greater than its recoverable amount it is written down immediately. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

(n) Cash and cash equivalents

For the purposes of these financial statements, cash and cash equivalents comprise; cash, non-mandatory balances with central banks and amounts due from banks with an original maturity of less than three months.

(o) Leases

The bank enters into operating leases as the lessee and rentals on these leases are charged to the income statement on a straight-line basis over the period of each lease. When an operating lease is terminated before the end of the lease period, any payment made to the lessor by way of penalty is recognised as an expense in the period of termination.

(p) Offset

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right of set-off and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(q) Borrowings

Borrowings (which include deposits from banks, customer accounts and subordinated liabilities) are recognised initially at fair value, being their issue proceeds net of transaction costs incurred. Borrowings are subsequently stated at amortised cost using the effective interest method.

(r) Employee benefits

(i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement when they are due.

(ii) Defined benefit plans

The bank is a participant of the Bank of China Pension and Life Assurance scheme offered by Bank of China Limited, London Branch (the "London Branch"). The London Branch is the sponsoring employer. There are no contractual arrangements for charging the net defined benefit cost for this plan. Contributions to the fund are recognised as an expense in the income statement in the accounting period to which they relate. Any unpaid contributions are recognised in the statement of financial position as a liability.

(s) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

Notes to the Financial Statements (continued)

3. Significant accounting policies (continued)

(t) Taxation

Income tax on the profit for the year comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in other comprehensive income or directly in equity, in which case it is recognised in other comprehensive income or equity.

Current tax is the tax expected to be paid on the taxable profit for the year, calculated using tax rates enacted or substantially enacted at the reporting date.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

(u) Provisions

Provisions are recognised in respect of present obligations arising from past events where it is probable that outflows of resources will be required to settle the obligations and they can be reliably estimated.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are not recognised in the financial statements but are disclosed unless they are remote.

(v) Share capital and reserves

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of an equity instrument are deducted from the initial measurement of the equity instrument.

4. Critical estimates and judgements

The bank makes estimates and assumptions concerning the future. The estimates and assumptions that could have significant risk of causing material adjustment to the carrying amounts of assets within the next financial year are highlighted below.

(i) Impairment of loans and advances

The bank reviews its loans and advances on an individual basis to assess impairment on a periodic basis unless a known circumstance occurs at or before the scheduled review date. In determining whether an impairment loss should be recorded in the income statement, the bank makes a judgement as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flow of a loan or advance. This evidence may include observable data indicating that there has been an adverse change in the payment status of the borrower e.g. payment delinquency or default. Additional observable data that would be considered is set out in Note 3(g).

(ii) Impairment of available for sale investments

The bank follows the guidance of IAS 39 to determine when available for sale investment securities are impaired. This determination requires significant judgement. In making this judgement, the bank evaluates, among other factors, the duration and extent to which the fair value of an investment is less than its cost, the extent to which changes in fair value relate to credit events and the financial health of and near-term business outlook for the investee/underlying portfolio, including factors such as industry and sector performance, credit ratings, and counterparty risk.

The methodology and assumptions used for impairment assessments are reviewed regularly. In evaluating impairment of convertible preference shares during the year, the bank continued to use a significant decline in market price to be a key indicator of impairment. The bank also considered other objective evidence of impairment, taking into account that during the year market prices continued to be impacted by liquidity and indicative prices were obtained for certain ABS held by the bank.

Notes to the Financial Statements (continued)

5. New pronouncements

New and amended standards and interpretations:

Issued but not effective for the financial year beginning 1 January 2016 and not early adopted.

- IFRS 9 Financial Instruments, issued in July 2014, introduces new requirements for classifying and measuring financial assets, hedge accounting and impairments and is likely to affect the bank's accounting for financial assets. The standard is effective from 1 January 2018, endorsed by the EU. The bank is currently assessing the requirements of IFRS 9 and aims to finalise an impact analysis, subject to external audit review during 2017.
- IFRS 15 Revenue from contracts with customers replaces existing revenue requirements and outlines a five step model an entity must apply to measure and recognise revenue. The standard is effective for annual periods beginning on or after 1 January 2018. The bank will assess the impact of these requirements in due course.

6. Financial risk management

Introduction and overview

The bank has exposure to the following risks from financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This note presents information about the bank's exposure to each of the above risks, the bank's objectives, policies and procedures for measuring and managing risk, and the bank's management of capital.

Risk management framework

The Board has overall responsibility for the establishment and oversight of the bank's risk management framework. The Board has established the bank's Board Risk Committee ("BRC") which is responsible for the oversight and implementation of risk strategy and risk appetite within the bank, oversight of risk management performance and the executive committees including, Asset and Liability ("ALCO"), Credit Risk Policy, Credit and Operational Risk Committees. These committees are responsible for developing and monitoring the bank's risk management policies in their specified areas. The bank's risk management policies are established to identify and analyse the risks faced by the bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. Internal Audit department undertakes both regular and ad-hoc reviews of the risk management controls and procedures, the results of which are reported to the Audit Committee.

The bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and responsibilities.

(a) Credit risk

Financial risk management

Credit risk is the risk of financial loss to the bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the bank's loans and advances to customers and available for sale financial investments.

Credit risk management framework

The bank has established a set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that arises through the bank's normal business activities. These policies, procedures and limits are regularly reviewed in light of changes in markets and business strategies.

The bank's organisation structure establishes clear authority and responsibilities for monitoring compliance with policies, procedures and limits, based on the principle of 'Three Lines of Defence'.

The business units are responsible for the day-to-day management of credit risk with the Risk Management Department being responsible for risk oversight and ensuring procedural compliance as well as the drafting, reviewing and updating of credit risk management policies and procedures. The Internal Audit function represents the third line of defence.

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(a) Credit risk (continued)

Credit risk management framework (continued)

The Board has the highest credit approval authority for the bank. The Board has delegated its authority to the Board Risk Committee, and the Chief Executive Officer (the “CEO”) of the bank. The CEO of the bank has delegated credit approval authority to Branch Managers, subject to Board approval.

Credit risk measurement and control

Loans and advances

The approval of an individual credit risk proposition requires assessment of the customer, any existing credit exposure to the customer and the credit risks associated with the transaction, at the same time taking into account the reward being offered for the risk and the extent of risk mitigation available to offset the potential loss in the event of default. The Risk Management Department is responsible for making an independent assessment of all credit facilities.

There are three main areas of concentration risk that are monitored, reported and managed by the bank; single customer (group), industrial sector and country risk. The bank monitors changes to counterparties’ credit risk, quality of the credit portfolio and risk concentrations, and reports regularly to the bank’s Executive Management Committee and the Board Risk Committee. Consideration must be taken and compliance must be adhered to these three concentration risk management areas either during initiating a transaction or maintaining and managing the portfolio quality.

The bank’s internal loan grading system divides loans into five categories as follows:

- Category 1: “Performing” represents loans where the borrower is currently meeting their repayment obligations and full repayment of interest and principal is not in doubt.
- Category 2: “Special Mention” represents loans where the borrower is experiencing difficulties which may threaten the bank’s position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.
- Category 3: “Sub-standard” represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.
- Category 4: “Doubtful” represents loans where collection in full is improbable and the bank expects to sustain a loss of principal and/or interest, taking into account the net realisable value of any collateral held.
- Category 5: “Loss” represents loans which are considered un-collectible after all collection options (such as the realisation of collateral or the initiation of legal proceedings) have been exhausted.

Where loans are classified as impaired and impairment allowances are raised, they are separately analysed and excluded from the categories listed above. Impairment usually occurs when loans have been classified in categories 4 or 5.

Debt securities and derivatives

For investment in debt securities and securitisation-backed assets, an external credit rating and assessment on the credit quality of the underlying asset are used for managing the credit risk involved. Credit limits are established on a counterparty and security issuer basis. For derivatives, the bank sets customer limits to manage the credit risk involved and follows the same approval process as loans and advances.

Collateral held as security

The bank has established a mechanism to update the value of its main type of collateral, residential properties, with the use of a publicly available index on a portfolio basis.

For loans guaranteed by a third party guarantor, the bank assesses the guarantor’s financial condition, credit history and ability to meet their obligations if called to do so. Collateral held as security cannot be sold or repledged in the absence of a default.

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(a) Credit risk (continued)

Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure without taking account of any collateral held or other credit enhancements. The maximum exposure to credit risk at the reporting date was:

£000	31 December 2016	31 December 2015
On statement of financial position:		
Cash and cash equivalents	310,070	342,358
Loans and advances to banks	24,270	62,633
Loans and advances to customers	1,159,696	810,776
Derivatives and other financial instruments	4,577	8,173
Available for sale financial investments	40,716	35,859
Total financial assets	1,539,329	1,259,799
Loan commitments	250,115	222,505
Guarantees	1,353	1,837
Total contingent liabilities and commitments	251,468	224,342
Total exposure	1,790,797	1,484,141

The fair value of collateral held at 31 December 2016 against amounts due from customers was £1,487,790,000 (31 December 2015: £1,233,614,000). The collateral is in the form of real estate properties and this collateral reduces the maximum amount of credit risk by £573,762,000 as at 31 December 2016 (31 December 2015: £492,921,000).

Cash and cash equivalents include exposures to the parent company of £77,291,000 (31 December 2015: £94,309,000). No other significant concentration of credit risk exposure exists. Cash and cash equivalents exclude cash in hand of £1,847,000 (31 December 2015: £1,661,000) for the purposes of the assessment of credit risk.

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(a) Credit risk (continued)

Credit risk exposure

The tables below present further detail on the bank's exposure to credit risk.

(a) Based on external credit rating system

£000	31 December 2016		31 December 2015	
	Cash and cash equivalents	Available for sale financial investments	Cash and cash equivalents	Available for sale financial investments
-Gross exposure	310,070	40,716	342,358	35,859
Individually impaired	-	-	-	-
Allowance for impairment	-	-	-	-
Carrying amount	-	-	-	-
Past due but not impaired	-	-	-	-
<i>Ageing profile:</i>				
0-3 months	-	-	-	-
4-6 months	-	-	-	-
7-9 months	-	-	-	-
10-12 months	-	-	-	-
Neither past due nor impaired	310,070	40,716	342,358	35,859
<i>Credit rating:</i>				
Aaa	-	-	170,000	26,275
Aa1 - Aa3	218,064	30,035	170,410	-
A1 - A3	89,800	-	1,948	-
Baa1 - Baa3	2,188	10,673	-	9,584
Unrated	18	8	-	-
Total carrying amount	310,070	40,716	342,358	35,859

(b) Based on internal loan grading system mapped against external credit ratings

Loans and advances to banks

£000	31 December 2016	31 December 2015
Gross exposure	24,317	62,714
Allowance for impairment	(47)	(81)
Carrying amount	24,270	62,633
Neither past due nor impaired	24,270	62,633
<i>Credit rating:</i>		
Aa1 – Aa3	-	7,673
A1 - A3	-	-
Baa1 - Baa3	24,316	36,824
Ba1 – Ba3	-	3,380
Unrated	1	14,837
Allowance for Impairment	(47)	(81)
Total carrying amount	24,270	62,633

Unrated exposure relates to loans to banks that only had short-term credit ratings at 31 December 2015. The equivalent long term rating is A1.

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(a) Credit risk (continued)

Loans and advances to customers

£000	31 December 2016	31 December 2015
Gross exposure	1,160,589	811,185
Allowance for impairment	(893)	(409)
Carrying amount	1,159,696	810,776
Individually impaired	3	33
Allowance for impairment	(3)	(33)
Carrying amount	-	-
By age profile		
Neither past due nor impaired	1,147,306	800,575
Past due but not impaired	12,390	10,201
<i>Ageing profile:</i>		
0-3 months	11,060	9,205
4-6 months	1,222	617
7-9 months	2	36
10-12 months	-	343
Over 12 months	106	-
Total carrying amount	1,159,696	810,776
By categories		
Performing	1,110,954	773,835
A1 - A3	-	-
Baa1 - Baa3	9,342	8,111
Ba1 - Ba3	121,899	4,775
Unrated	979,713	760,949
Special mention (unrated)	46,426	26,740
Substandard (unrated)	2,209	-
Doubtful (unrated)	-	-
Loss (unrated)	108	-
Total carrying amount	1,159,696	810,776

(b) Liquidity risk

Liquidity risk is the risk that the bank will not be able to meet its financial obligations as they fall due.

The bank is exposed to the risk that it will be unable to meet its obligations as they fall due, arising from the differing maturity profiles of its assets and liabilities. To mitigate its exposure the bank places limits on the mismatch of maturity dates, and by holding stock of liquid assets which could be sold at short notice if the need arose.

The Board is the ultimate decision-making body and is responsible for compliance with the regulatory requirements. Formulation of the risk management procedures, implementation mechanism and monitoring of the compliance is the main responsibility of the ALCO. Daily management of liquidity is carried out by the Financial Management department who monitor the liquidity risk and provide regular reports to management and the Prudential Regulation Authority (the "PRA").

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(b) Liquidity risk (continued)

The following are the contractual (undiscounted) maturities of financial liabilities, including the next expected interest payments and excluding the effect of any netting agreements if they were in place:

£000	Carrying amount	Contractual cash flows	Less than 1 month	1 to 3 months	3 months to 1 year	More than 1 year
31 December 2016						
Non-derivative financial liabilities:						
Deposits from banks	164,849	(168,811)	(2,923)	(38,431)	(34,244)	(93,213)
Deposits from customers	982,361	(982,741)	(947,673)	(18,797)	(16,267)	(4)
Subordinated liabilities	60,000	(60,100)	-	(100)	-	(60,000)
Derivative financial instruments:	4,150	-	-	-	-	-
Cash outflows		(143,068)	(123,016)	(861)	(2,416)	(16,775)
Cash inflows		123,362	123,362	-	-	-
	1,211,360	(1,231,358)	(950,250)	(58,189)	(52,927)	(169,992)
Loan commitments	250,115	(250,115)	(250,115)	-	-	-
	1,461,475	(1,481,473)	(1,200,365)	(58,189)	(52,927)	(169,992)
31 December 2015						
Non-derivative financial liabilities:						
Deposits from banks	136,736	(138,176)	(14,583)	(151)	(123,442)	-
Deposits from customers	737,724	(738,053)	(698,550)	(23,109)	(16,342)	(52)
Subordinated liabilities	60,000	(60,135)	-	(135)	-	(60,000)
Derivative financial instruments:	11,505	-	-	-	-	-
Cash outflows		(160,896)	(126,465)	(873)	(3,976)	(29,582)
Cash inflows		126,527	126,527	-	-	-
	945,965	(970,733)	(713,071)	(24,268)	(143,760)	(89,634)
Loan commitments	222,505	(222,505)	(222,505)	-	-	-
	1,168,470	(1,193,238)	(935,576)	(24,268)	(143,760)	(89,634)

The previous table shows the undiscounted cash flows on the bank's financial liabilities and unrecognised loan commitments on the basis of their earliest possible contractual maturity. The bank's expected cash flows on these instruments vary significantly from this analysis and hence this table shows a worst case scenario. For example, current accounts and demand deposits from customers are expected to maintain a stable or increasing balance and unrecognised loan commitments are not all expected to be drawn down immediately but to be drawn over a period of time.

The contractual cash flow disclosed in the previous table represents the contractual undiscounted cash flows relating to the principal and interest on the financial liability or commitment. The disclosure for derivatives shows a net amount for derivatives that are settled on a net basis, (e.g. interest rate swaps) but on a gross outflow and inflow basis for derivatives that have simultaneous gross settlement (e.g. forward foreign exchange contracts and currency swaps).

The bank has the benefit of a committed short-term loan facility granted by its parent company. The facility is repayable at call and no amounts were drawn at 31 December 2016 (31 December 2015: £nil).

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(c) Market risk

Foreign exchange risk

Foreign exchange risk is the risk that movements in the various currencies could materially impact the Financial Statements. To manage its exposure to foreign exchange risk the bank enters into derivative transactions.

The following table shows the foreign exchange positions as at 31 December 2016 and 2015.

£000

31 December 2016	Sterling	US Dollar	Euro	Other	Total
Cash and cash equivalents	239,274	55,876	4,671	12,096	311,917
Loans and advances to banks	-	24,270	-	-	24,270
Loans and advances to customers	712,080	368,646	57,827	21,143	1,159,696
Derivatives financial instruments (asset)	1,498	3,079	-	-	4,577
Available for sale financial investments	8	-	10,673	30,035	40,716
Other assets	7,145	834	166	577	8,722
Deposits from banks	(2,526)	(93,610)	(38,349)	(30,364)	(164,849)
Deposits from customers	(661,320)	(265,625)	(39,842)	(15,574)	(982,361)
Derivatives financial instruments (liability)	(627)	(3,523)	-	-	(4,150)
Other liabilities	(23,338)	(3,612)	(280)	(944)	(28,174)
Subordinated liabilities	(60,000)	-	-	-	(60,000)
Total shareholder equity	(310,763)	-	(36)	435	(310,364)
Net financial assets/(liabilities)	(98,569)	86,335	(5,170)	17,404	-
Net forward foreign exchange positions	(797)	(3,267)	2,828	1,236	-
Loan commitments	65,104	135,654	38,349	11,008	250,115

£000

31 December 2015	Sterling	US Dollar	Euro	Other	Total
Cash and cash equivalents	200,217	98,817	40,064	4,921	344,019
Loans and advances to banks	217	33,017	29,399	-	62,633
Loans and advances to customers	643,252	111,909	55,615	-	810,776
Derivative financial instruments (asset)	390	7,783	-	-	8,173
Available for sale financial investments	-	-	9,584	26,275	35,859
Other assets	25,980	587	153	3,230	29,950
Deposits from banks	(2,988)	(88,016)	(17,307)	(28,425)	(136,736)
Deposits from customers	(555,735)	(132,236)	(32,412)	(17,341)	(737,724)
Derivative financial instruments (liability)	(1,707)	(9,798)	-	-	(11,505)
Other liabilities	(21,596)	(2,948)	(331)	(302)	(25,177)
Subordinated liabilities	(60,000)	-	-	-	(60,000)
Total shareholder equity	(320,479)	-	(408)	619	(320,268)
Net financial assets (liabilities)	(92,449)	19,115	84,357	(11,023)	-
Net forward foreign exchange positions	(7,914)	3,532	3,073	1,309	-
Loan commitments	86,421	102,991	33,093	-	222,505

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(c) Market risk (continued)

Foreign exchange risk (continued)

Sensitivity analysis

A 1% percent weakening of the following currencies against Sterling at 31 December 2016 would have increased (decreased) equity and the income statement by the amounts shown below. This calculation assumes that the change occurred at the reporting date and had been applied to risk exposures existing at that date.

This analysis assumes that all other variables, in particular other exchange rates and interest rates, remain constant

£000	Other Comprehensive Income		Income statement	
	31 December 2016	31 December 2015	31 December 2016	31 December 2015
US Dollars	-	-	(1,140)	(113)
Euro	(6)	4	-	(1,177)
Other	(97)	(7)	(92)	(277)

A 1% percent strengthening of the above currencies against Sterling at 31 December 2016 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(c) Market risk

Exposure to interest rate risk

The bank does not operate a trading book.

The principal exposure is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates. Interest rate risk is managed principally through monitoring the cumulative interest rate gap position and by having pre-approved limits for the time bands. The ALCO is the monitoring body for compliance with these limits and is assisted by the Financial Management department in its day-to-day monitoring activities. A summary of the bank's interest rate gap position is as follows:

£000	Carrying Amount	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	Over 5 years	Non Interest Bearing
31 December 2016							
Assets							
Cash	311,917	311,602	-	-	-	-	315
Loans and advances to banks	24,270	-	1	24,269	-	-	-
Loans and advances to customers	1,159,696	1,755	600,257	16,820	366,265	158,840	15,759
Derivative financial instruments	4,577	-	-	-	-	-	4,577
Available for sale financial investments	40,716	10,681	-	30,035	-	-	-
Other assets	8,722	-	-	-	-	-	8,722
Total assets	1,549,898	324,038	600,258	71,124	366,265	158,840	29,373
Equity and liabilities							
Liabilities							
Deposits from banks	164,849	2,916	38,405	30,308	93,213	-	7
Deposits from customers	982,361	735,154	211,914	19,342	1	-	15,950
Derivative financial instruments	4,150	-	-	-	-	-	4,150
Other liabilities	28,174	-	-	-	-	-	28,174
Subordinated liabilities	60,000	-	60,000	-	-	-	-
Equity							
Shareholders' equity	310,364	-	-	-	-	-	310,364
Total equity and liabilities	1,549,898	738,070	310,319	49,650	93,214	-	358,645
Effect of derivatives held for risk management							
Interest rate sensitivity gap	-	(414,032)	289,939	21,474	273,051	158,840	(329,272)
Cumulative gap	-	(414,032)	(124,093)	(102,619)	170,432	329,272	-

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(c) Market risk (continued)

Exposure to interest rate risk (continued)

£000	Carrying amount	Less than 1 Month	1-3 months	3 months to 1 year	1-5 years	Over 5 years	Non Interest Bearing
31 December 2015							
Assets							
Cash	344,019	342,358	-	-	-	-	1,661
Loans and advances to banks	62,633	18,642	36,824	7,032	-	-	135
Loans and advances to customers	810,776	604,722	156,130	9,977	-	40,413	(466)
Derivative financial instruments	8,173	-	-	-	-	-	8,173
Available for sale financial investments	35,859	-	-	-	35,859	-	-
Other assets	29,950	-	-	-	-	-	29,950
Total assets	1,291,410	965,722	192,954	17,009	35,859	40,413	39,453
Equity and liabilities							
Liabilities	971,142	711,337	82,796	136,494	52	-	40,463
Deposits from banks	136,736	12,068	-	121,026	-	-	3,642
Deposits from customers	737,724	699,269	22,796	15,468	52	-	139
Derivative financial instruments	11,505	-	-	-	-	-	11,505
Other liabilities	25,177	-	-	-	-	-	25,177
Subordinated liabilities	60,000	-	60,000	-	-	-	-
Equity							
Shareholders' equity	320,268	-	-	-	-	-	320,268
Total equity and liabilities	1,291,410	711,337	82,796	136,494	52	-	360,731
Effect of derivatives held for risk management							
	-	(9,463)	-	9,463	-	-	-
Interest rate sensitivity gap	-	244,922	110,158	(110,022)	35,807	40,413	(321,278)
Cumulative gap	-	244,922	355,080	245,058	280,865	321,278	-

The table below indicates the impact on the income statement for possible change in interest rates, with all other variables held constant.

At the reporting date the sensitivity to interest rate risk was projected to be:

£000	100bps parallel Increase	100bps parallel Decrease
Sensitivity of projected net interest income at		
31 December 2016	(1,245)	1,245
31 December 2015	1,240	(1,240)
Sensitivity of reported equity to interest rate movements at		
31 December 2016	100	(100)
31 December 2015	89	(89)

Interest rate movements affect reported equity in the following ways: (i) retained earnings; arising from increases or decreases in net interest income and the fair value changes reported in profit or loss and (ii) fair value reserves; arising from increases or decreases in fair values of available for sale financial instruments reported directly in equity.

Notes to the Financial Statements (continued)

6. Financial risk management (continued)

(d) Capital management

Regulatory capital

Reference is made below to the Prudential Regulation Authority ("PRA") which along with the Financial Conduct Authority ("FCA") are the bank's regulators.

The PRA sets capital requirements for the bank in line with international supervisory standards and guidelines known as Basel III which are contained within legislation passed by the EU, i.e. CRD IV Regulation and Directives. The parent company is directly supervised by their local regulators.

In calculating capital requirements, the bank has adopted the standardised approach for credit risk and the basic indicator approach for operational risk. As the bank does not have a trading book, the capital requirement for the foreign exchange risk inherent in the banking book has been captured as market risk, which is also calculated on the standardised approach.

The bank's regulatory capital resources comprise tier 1 and tier 2 capital as set out in the table below.

The bank does not have any deductions from either tier 1 or tier 2 capital and is not limited by the restriction that qualifying term subordinated loan capital (tier 2) may not exceed 50 percent of tier 1 capital.

Banking operations are categorised as banking book and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The bank has complied with all externally imposed capital requirements throughout the period.

The bank's regulatory capital position at 31 December 2016 and 2015 was as follows:

£000	2016 Actual	2015 Actual
Tier 1 capital		
Ordinary share capital	250,000	250,000
Retained earnings *	24,958	24,958
Tier 2 capital		
Qualifying subordinated liabilities	60,000	60,000
Total regulatory capital	334,958	334,958
		Regulatory Minimum
Risk exposure amount	1,002,116	n.a.
Fully loaded CRD IV CET1 ratio	27.44%	4.5%
Total capital ratio	33.43%	8.0%
Leverage ratio	15.57%	3.0%

* Retained earnings for regulatory capital purposes at the reporting date is restricted to audited retained earnings at 31 December 2015 after recommended 2015 dividend paid in 2016.

The bank maintains a buffer to comparable regulatory minimum capital ratios.

The PRA also sets individual capital guidance ("ICG") for the bank as part of its Supervisory Review and Evaluation Process. The agreed ICG was in force and respected as at the reporting date and remains confidential between each bank and the PRA in accordance with accepted practice.

Notes to the Financial Statements (continued)

7. Financial assets and financial liabilities

Fair values of financial instruments

The bank's valuation methodology is detailed in Note 3.

Fair values

The fair values for each class of financial assets and financial liabilities together with their carrying amounts shown at the reporting date are as follows:

£000	Financial instruments at fair value through profit and loss	Loans and receivables	Available for sale	Other amortised cost	Total carrying amount	Fair value
31 December 2016						
Assets						
Cash and cash equivalents	-	311,917	-	-	311,917	311,917
Cash and balances with banks	-	310,070	-	-	310,070	310,070
Cash in hand	-	1,847	-	-	1,847	1,847
Loans and advances to banks		24,270			24,270	24,270
Loans and advances to customers	-	1,159,696	-	-	1,159,696	1,160,291
Corporate loans and advances	-	586,756	-	-	586,756	587,351
Retail loans and advances	-	572,940	-	-	572,940	572,940
Derivative financial instruments	4,577	-	-	-	4,577	4,577
Interest rate swaps	1,040	-	-	-	1,040	1,040
Cross currency swaps	458	-	-	-	458	458
Other derivatives	3,079	-	-	-	3,079	3,079
Available for sale investments	-	-	40,716	-	40,716	40,716
Debt securities	-	-	40,708	-	40,708	40,708
Convertible preference shares	-	-	8	-	8	8
Total financial assets	4,577	1,495,883	40,716	-	1,541,176	1,541,771
Liabilities						
Deposits from banks	-	-	-	164,849	164,849	164,849
Deposits from customers	-	-	-	982,361	982,361	982,361
Retail customers	-	-	-	569,534	569,534	569,534
Corporate customers	-	-	-	412,827	412,827	412,827
Derivative financial instruments	4,150	-	-	-	4,150	4,150
Interest rate swaps	594	-	-	-	594	594
Cross currency swaps	33	-	-	-	33	33
Other derivatives	3,523	-	-	-	3,523	3,523
Subordinated liabilities	-	-	-	60,000	60,000	60,000
Total financial liabilities	4,150	-	-	1,207,210	1,211,360	1,211,360

Fair valued loans with a carrying value of £37,202,000 (31 December 2015: £40,413,000) are at fixed rate to maturity. The carrying value of all other financial assets and liabilities that are materially equal to their fair value. The interest rates on these financial assets and liabilities re-price on a regular and short-term basis resulting in the fair value calculation being not materially different from the carrying value.

Notes to the Financial Statements (continued)

7. Financial assets and financial liabilities (continued)

Fair values (continued)

£000	Financial instruments at fair value through profit and loss	Loans and receivables	Available for sale	Other amortised cost	Total carrying amount	Fair value
31 December 2015						
Assets						
Cash and cash equivalents	-	344,019	-	-	344,019	344,019
Cash and balances with banks	-	342,358	-	-	342,358	342,358
Cash in hand	-	1,661	-	-	1,661	1,661
Loans and advances to banks	-	62,633	-	-	62,633	62,633
Loans and advances to customers	-	810,776	-	-	810,776	810,907
Corporate loans and advances	-	317,455	-	-	317,455	317,586
Retail loans and advances	-	493,321	-	-	493,321	493,321
Derivative financial instruments	8,173	-	-	-	8,173	8,173
Interest rate swaps	366	-	-	-	366	366
Cross currency swaps	24	-	-	-	24	24
Other derivatives	7,783	-	-	-	7,783	7,783
Available for sale investments	-	-	35,859	-	35,859	35,859
Debt securities	-	-	35,859	-	35,859	35,859
Convertible preference shares	-	-	-	-	-	-
Total financial assets	8,173	1,217,428	35,859	-	1,261,460	1,261,591
Liabilities						
Deposits from banks	-	-	-	136,736	136,736	136,736
Deposits from customers	-	-	-	737,724	737,724	737,724
Retail customers	-	-	-	479,547	479,547	479,547
Corporate customers	-	-	-	258,177	258,177	258,177
Derivative financial instruments	11,505	-	-	-	11,505	11,505
Interest rate swaps	1,026	-	-	-	1,026	1,026
Cross currency swaps	681	-	-	-	681	681
Other derivatives	9,798	-	-	-	9,798	9,798
Subordinated liabilities	-	-	-	60,000	60,000	60,000
Total financial liabilities	11,505	-	-	934,460	945,965	945,965

The table below analyses financial assets and liabilities measured at fair value, by valuation method:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

During the reporting period ending 31 December 2016, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of the Level 3 fair value measurements. The carrying value of short-term receivables and payables are assumed to approximate to their fair values where discounting is not material.

Loans to customers designated at fair value are valued by discounting the amount derived from the gap between their fixed interest rates against floating interest rate swap rates to maturity.

For derivative financial instruments not traded in an active market for which no quoted market price is available the fair value is determined using valuation techniques. Forward currency exchange contracts fair value was determined using quoted forward exchange rates matching the maturities of the contracts. While for interest rate swaps fair value was determined using discounted cash flow analysis at quoted interest rates.

The fair value of other financial assets and borrowings has been calculated by discounting the expected future cash flows at prevailing market interest rates for instruments with substantially the same terms and characteristics.

Notes to the Financial Statements (continued)

7. Financial assets and financial liabilities (continued)

Fair value hierarchy

During the financial years ended 31 December 2016 and 31 December 2015 no financial assets or liabilities were transferred between Level 1, Level 2 or Level 3.

£000

31 December 2016	Level 1	Level 2	Level 3	Total
Financial assets				
Designated fair value loans	-	-	36,607	36,607
Derivative financial instruments:				
Interest rate swaps	-	1,040	-	1,040
Cross currency swaps	-	458	-	458
Other derivatives	-	3,079	-	3,079
	-	4,577	-	4,577
Financial investments available for sale:				
Debt securities	40,708	-	-	40,708
Convertible preference shares	-	-	8	8
	40,708	-	8	40,716
Total assets	40,708	4,577	36,615	81,900
Financial liabilities				
Derivative financial instruments:				
Interest rate swaps	-	594	-	594
Cross currency swaps	-	33	-	33
Other derivatives	-	3,523	-	3,523
Total liabilities	-	4,150	-	4,150

£000

31 December 2015	Level 1	Level 2	Level 3	Total
Financial assets				
Designated fair value loans	-	-	40,544	40,544
Derivative financial instruments:				
Interest rate swaps	-	366	-	366
Cross currency swaps	-	24	-	24
Other derivatives	-	7,783	-	7,783
	-	8,173	-	8,173
Financial investments available for sale:				
Debt securities	35,859	-	-	35,859
Convertible preference shares	-	-	-	-
	35,859	-	-	35,859
Total assets	35,859	8,173	40,544	84,576
Financial liabilities				
Derivative financial instruments:				
Interest rate swaps	-	1,026	-	1,026
Cross currency swaps	-	681	-	681
Other derivatives	-	9,798	-	9,798
Total liabilities	-	11,505	-	11,505

Notes to the Financial Statements (continued)

8. Net interest income

£000	31 December 2016	31 December 2015
Interest income from financial investments	1,216	1,134
Other interest income:		
Cash and cash equivalents	511	1,016
Loans and advances to banks	470	1,189
Loans and advances to customers	32,394	22,306
Total other interest income	33,375	24,511
Total interest income	34,591	25,645
Interest expense:		
Deposits from banks	2,547	1,177
Customers accounts	1,584	1,395
Subordinated liabilities	498	523
Total interest expense	(4,629)	(3,095)
Net interest income	29,962	22,550

Included within various line items under interest income for the year ended 31 December 2016 is a total of £nil (31 December 2015: £nil) accrued for non performing impaired financial assets.

9. Net fee and commission income

£000	31 December 2016	31 December 2015
Retail Banking customer fees	1,509	2,580
Corporate Banking credit-related fees	2,511	6,279
Other	9	47
Fee and commission income	4,029	8,906
Inter-bank transaction fees	360	307
Other	416	275
Fee and commission expense	(776)	(582)
Net fee and commission income	3,253	8,324

Corporate Banking credit-related fees included a one off fee of £3,837,000 in 2015.

10. Net fair value gain on financial instruments

£000	31 December 2016	31 December 2015
Net fair value gain (loss) on financial instruments held for risk management purposes:		
Designated fair value loans	106	(1,036)
Interest rate swaps	(463)	254
Cross currency swaps	-	-
Other derivatives	598	1,293
	241	511

There are no financial derivative instruments that qualify for hedge accounting in accordance with IAS39.

At 31 December 2016 unrealised net gain of £27,000 (31 December 2015: unrealised net loss of £15,000), on currency swap derivative instruments, have been recorded against foreign exchange gains and losses in the income statement, reflecting the effects of these derivatives instruments in mitigating the foreign exchange gains and losses on the net non-Sterling assets of the bank held at these dates.

Notes to the Financial Statements (continued)

11. Other operating income

£000	31 December 2016	31 December 2015
Related party service charges	52,160	54,617
Dividends from subsidiaries	-	5,300
Other	2,739	1,137
	54,899	61,054

The related party service charges represents the net amount receivable by the bank for services provided and received under service level agreements with related parties as disclosed in Note 32.

12. Staff costs

£000	31 December 2016	31 December 2015
Wages and salaries	26,405	23,354
Contributions to defined contribution plans	1,716	1,951
Social security costs	3,532	3,052
Other	1,168	1,143
	32,821	29,500
Average number of employees	31 December 2016	31 December 2015
Retail Banking	130	118
Corporate Banking	74	69
Support Functions	206	192
Total average number of employees	410	379

13. Other expenses

£000	31 December 2016	31 December 2015
Administrative	4,859	4,517
Rent on operating leases	511	544
Software licensing and other IT costs	263	300
Other	1,281	1,183
	6,914	6,544

Auditor's remuneration:

£000	31 December 2016	31 December 2015
Fees payable to the company's auditors for the audit of the company's financial statements:		
Current year	141	136
Fees payable to the company's auditor and its associates for other services:		
The audits of the company's subsidiaries, pursuant to legislation	10	10
Other services pursuant to legislation	15	10

Notes to the Financial Statements (continued)

14. Directors' remuneration

£000	31 December 2016	31 December 2015
Remuneration of directors in respect of services rendered:		
Remuneration	734	833
Pension contributions	-	-
Highest paid director:		
Remuneration	283	227
Pension contributions	-	-

15. Income tax expense

£000	31 December 2016	31 December 2015
Current tax expense		
Current period	14,264	10,650
Adjustments for prior years	(27)	(212)
Total current tax	14,237	10,438
Deferred tax expense		
Origination and reversal of temporary differences	(139)	117
Adjustments for prior years	70	209
Total deferred tax	(69)	326
Total income tax expense in income statement	14,168	10,764

The tax on the bank's profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the bank as follows:

Reconciliation of effective tax rate

£000	31 December 2016	31 December 2015
Profit before income tax	49,858	56,214
Income tax using the standard rate of corporation tax in the UK 28.00% (2015: 20.25%)	13,960	11,383
Non-deductible expenses	293	179
Non-taxable income	-	(1,073)
Loss on disposal of subsidiary	-	163
Over (under)-provided in prior years	42	(3)
Other - tax rate adjustment	(127)	115
Total income tax expense in income statement	14,168	10,764

Notes to the Financial Statements (continued)

15. Income tax expense (continued)

Income tax recognised in other comprehensive income

£000	31 December 2016	31 December 2015
Current tax		
UK current tax expense	23	(179)
Adjustments for prior years	-	-
Total current tax	23	(179)
Deferred tax		
Current year deferred tax charge (credit)	(68)	-
Adjustments for prior years	-	-
Total deferred tax	(68)	-
Total income and deferred tax credit in other comprehensive income	(45)	(179)

Reductions in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) and 18% (effective from 1 April 2020) were substantively enacted on 26 October 2015. A banking surcharge tax of 8% also applies to the bank (effective from 1 January 2016) and this change was substantively enacted on 26 October 2015. Deferred tax has been calculated by reference to the most appropriate rate based on forecasts.

In 2016, the UK government announced a further reduction to the rate of corporation tax to 17% from 1 April 2020. This further reduction may impact future current and deferred tax balances when substantively enacted. This rate had not been substantively enacted by the balance sheet date.

16. Cash and cash equivalents

£000	31 December 2016	31 December 2015
Cash and cash equivalents with banks	310,070	342,358
Cash in hand	1,847	1,661
	311,917	344,019

17. Derivative financial instruments

The bank holds derivative instruments for risk management and cross currency funding purposes.

£000	31 December 2016		31 December 2015	
	Assets	Liabilities	Assets	Liabilities
Instrument type:				
Interest rate swap	1,040	594	366	1,026
Cross currency swap	458	33	24	681
Other derivatives	3,079	3,523	7,783	9,798
	4,577	4,150	8,173	11,505

The bank did not designate any derivative financial instruments for hedging purposes during either period presented.

The bank sub-participated a loan but retained the risks and rewards of ownership of the interest strip relating to it. The bank de-recognised the principal element of the loan as it retained none of the risks or rewards associated with it. The bank has unrestricted use of interest received from the interest strip however it has also assumed an obligation to pay interest. The bank is restricted from selling or transferring the interest strip, and associated liability to pay interest. At 31 December 2016, the fair value of the interest strip amounted to £3,079,000 (31 December 2015: £7,783,000) and the associated liability was £3,523,000 (31 December 2015: £9,798,000).

Notes to the Financial Statements (continued)

18. Loans and advances to banks

£000	31 December 2016	31 December 2015
Loans and advances to banks	24,317	62,714
Collective impairment provision	(47)	(81)
	24,270	62,633

At 31 December 2016 £nil (31 December 2015: £nil) of loans and advances to banks are expected to be recovered more than twelve months after the reporting date.

19. Loans and advances to customers

£000	31 December 2016	31 December 2015
Corporate loans and advances	587,645	317,831
Retail loans and advances	572,944	493,354
Gross loans and advances	1,160,589	811,185
Less: specific allowance for impairments	(3)	(33)
collective allowance for impairments	(890)	(376)
Total allowance for impairment	(893)	(409)
Loans and advances to customer net	1,159,696	810,776

At 31 December 2016 £158,840,000 (31 December 2015: £40,413,000) of loans and advances to customers are expected to be recovered more than five years after the reporting date.

Loans and advances to customers at amortised cost

£000	31 December 2016			31 December 2015		
	Gross amount	Impair- ment al- lowance	Carrying amount	Gross amount	Impair- ment al- lowance	Carrying amount
Corporate loans and advances	587,645	(890)	586,755	317,831	(376)	317,455
Retail loans and advances	572,944	(3)	572,941	493,354	(33)	493,321
	1,160,589	(893)	1,159,696	811,185	(409)	810,776

At 31 December 2016, fixed rate loans with a carrying value of £37,202,000 (31 December 2015: £40,413,000) were fair valued at £36,607,000 (31 December 2015: £40,544,000).

Notes to the Financial Statements (continued)

20. Allowances for impairment

(a) Loans and advances to banks and customers

£000	Specific Loans and advances to banks	Specific Loans and advances to customers	Collective Loans and advances to banks	Collective Loans and advances to customers
Balance at 1 January 2016	-	33	81	376
Increase in impairment	-	83	21	574
Recovery	-	(4)	-	-
Reversal of impairment	-	-	(55)	(60)
Charge (release) in income statement	-	79	(34)	514
Amounts written off	-	(109)	-	-
Balance at 31 December 2016	-	3	47	890
Balance at 1 January 2015	-	5	331	405
Increase in impairment	-	134	29	199
Reversal of impairment	-	-	(279)	(228)
Charge (release) in income statement	-	134	(250)	(29)
Amounts written off	-	(106)	-	-
Balance at 31 December 2015	-	33	81	376

Amounts written off during 2016 and 2015 mostly represent fraud losses.

(b) Available for sale financial investments

£000	Note	Movement before tax in fair value recognised in equity	Impairment
Balance at 1 January 2016		210	-
Changes in fair values		189	-
Reversal in impairment		-	-
Amounts written off		-	-
	21	189	-
Exchange-rate movements		-	-
Balance at 31 December 2016		399	-

The cumulative tax credit on this fair value amounts to £115,000 (31 December 2015: £70,000).

Balance at 1 January 2015		(676)	-
Changes in fair values		886	-
Reversal in impairment		-	-
Amounts written off		-	-
	21	886	-
Exchange-rate movements		-	-
Balance at 31 December 2015		210	-

Notes to the Financial Statements (continued)

20. Allowances for impairment (continued)

(c) Impairment charges

£000	31 December 2016	31 December 2015
Loans and advances to customers		
Specific	(79)	(134)
Collective	(514)	29
Loans and advances to banks		
Specific	-	-
Collective	34	250
Available for sale financial investments	-	-
Foreign exchange movement	32	10
Total impairment (charges) releases in income statement	(527)	155

21. Available for sale investments

At 31 December 2016 there were £8,000 of available for sale investments (31 December 2015: £35,859,000) which are expected to be recovered more than twelve months after the reporting date and £40,708,000 of available for sale investments (31 December 2015: £nil) which are expected to be recovered within twelve months of the reporting date. The available for sale investments balance is comprised of fixed/floating interest rate bonds and convertible preference shares.

£000	Note	31 December 2016	31 December 2015
Debt securities		40,708	35,859
Convertible preference shares		8	-
		40,716	35,859
Balance at 1 January 2016		35,859	37,469
Accrued interest		76	(22)
Disposals through sale and redemptions		-	-
Acquisition		8	-
Loss from changes in fair value recognised in equity	20 (b)	(189)	(886)
Movements in impairment amounts	20 (b)	-	-
Amortisation of premium		4	3
Exchange-rate movement		4,958	(705)
Balance at 31 December 2016		40,716	35,859

Notes to the Financial Statements (continued)

22. Property, plant and equipment

£000	Property, plant and fixtures	Furniture and equipment	Computer equipment	Motor vehicles	Total
Cost					
Balance at 1 January 2016	5,627	1,646	1,386	214	8,873
Additions	346	225	115	-	686
Disposals	-	(2)	(27)	-	(29)
Balance at 31 December 2016	5,973	1,869	1,474	214	9,530
Balance at 1 January 2015	4,889	1,496	1,336	138	7,859
Additions	738	175	100	76	1,089
Disposals	-	(25)	(50)	-	(75)
Balance at 31 December 2015	5,627	1,646	1,386	214	8,873
Depreciation					
Balance at 1 January 2016	3,187	1,048	1,002	122	5,359
Additions	357	300	257	4	918
Depreciation for the year	-	-	3	-	3
Disposals	-	(1)	(25)	-	(26)
Balance at 31 December 2016	3,544	1,347	1,237	126	6,254
Balance at 1 January 2015	2,854	758	760	97	4,469
Additions	-	-	-	-	-
Depreciation for the year	333	315	292	25	965
Disposals	-	(25)	(50)	-	(75)
Balance at 31 December 2015	3,187	1,048	1,002	122	5,359
Net carrying values at					
31 December 2016	2,429	522	237	88	3,276
31 December 2015	2,440	598	384	92	3,514

As at 31 December 2016 and 31 December 2015 the bank identified no events or circumstances that would indicate that the bank's tangible fixed assets might be impaired.

23. Intangible assets

£000	IT Software	Total
Cost		
Balance at 1 January 2016	1,818	1,818
Additions	86	86
Disposals	-	-
Balance at 31 December 2016	1,904	1,904
Balance at 1 January 2015	1,818	1,818
Additions	-	-
Disposals	-	-
Balance at 31 December 2015	1,818	1,818

Notes to the Financial Statements (continued)

23. Intangible assets (continued)

Amortisation

Balance at 1 January 2016	1,638	1,638
Amortisation for the year	144	144
Disposals	-	-
Balance at 31 December 2016	1,782	1,782
Balance at 1 January 2015	1,492	1,492
Amortisation for the year	146	146
Disposals	-	-
Balance at 31 December 2015	1,638	1,638
Net carrying value at		
31 December 2016	122	122
31 December 2015	180	180

As at 31 December 2016 and 31 December 2015 the bank identified no events or circumstances that would indicate that the bank's intangible assets might be impaired.

24. Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

£000	31 December 2016			31 December 2015		
	Assets	Liabilities	Net	Assets	Liabilities	Net
Property and equipment, and software	96	-	96	39	-	39
Available for sale investments	68	-	68	-	-	-
Deferred employees' benefits	532	-	532	441	-	441
Other	(134)	-	(134)	(55)	-	(55)
Net deferred tax assets	562	-	562	425	-	425

There were no unrecognised deferred tax assets as at 31 December 2016 and 31 December 2015.

Movements in temporary differences during the year

£000	Opening balance 1 January 2016	Recognised In income	Recognised in equity	Closing balance 31 December 2016
Property and equipment, and software	39	57	-	96
Available for sale investments	-	-	68	68
Deferred employees' benefits	441	91	-	532
Other	(55)	(79)	-	(134)
	425	69	68	562
£000	Opening balance 1 January 2015	Recognised In income	Recognised in equity	Closing balance 31 December 2015
Property and equipment, and software	42	(3)	-	39
Available for sale investments	-	-	-	-
Deferred employees' benefits	709	(268)	-	441
Other	-	(55)	-	(55)
	751	(326)	-	425

Notes to the Financial Statements (continued)

25. Prepayments, accrued income and other assets

£000	31 December 2016	31 December 2015
Accrued income	1,989	1,579
Prepaid expenses	512	381
Receivable from related party	635	19,368
Other	1,626	4,503
	4,762	25,831

26. Deposits from banks

£000	31 December 2016	31 December 2015
From fellow group companies	-	-
Other deposits from banks	164,849	136,736
	164,849	136,736

At 31 December 2016 £nil (31 December 2015: £nil) of deposits from banks are expected to be settled more than twelve months after the reporting date.

27. Deposits from customers

£000	31 December 2016	31 December 2015
Retail customers:		
Term deposits	145,268	133,577
Notice deposits	112,185	84,011
Current deposits	311,482	260,917
Other	599	1,042
	569,534	479,547
Corporate customers:		
Notice deposits	91,103	36,769
Current deposits	319,509	204,646
Other	2,215	16,762
	412,827	258,177
	982,361	737,724

At 31 December 2016 £1,000 (31 December 2015: £52,000) of deposits from customers are expected to be settled more than twelve months after the reporting date.

Notes to the Financial Statements (continued)

28. Subordinated liabilities

£000	31 December 2016	31 December 2015
Subordinated note issued	60,000	60,000
	60,000	60,000

On 20 September 2007 the bank issued a £60,000,000 subordinated loan. Interest is payable on 31 March, 30 June, 30 September and 31 December at the three-month London Interbank Bank Offered Rate plus 30 basis points. The rate applicable to the loan as at the reporting date was 0.67% (31 December 2015: 0.89%). The loan is repayable upon giving 5 years and one day's notice.

The above liabilities will, in the event of the winding-up of the bank, be subordinated to the claims of depositors and all other creditors of the bank.

29. Other liabilities

(a) Other liabilities

£000	31 December 2016	31 December 2015
Creditors and accruals	13,338	15,263
Other	282	1,882
	13,620	17,145

(b) Defined benefit obligations

The bank makes contributions to a group defined benefit scheme, the Bank of China Pension & Life Assurance Scheme (the "Scheme"), that provides pension benefits for employees upon retirement. The Scheme entitles a retired employee to receive an annual payment equal to 1/60th of final salary for each year of service the employee provided. The Scheme is sponsored by Bank of China Limited, London Branch and was closed to new employees on 31 December 2004.

The following tables set out details of the Scheme as at 31 December 2016 and 2015. This disclosure is for the scheme as a whole and does not represent the bank's allocation of the Scheme's assets and liabilities due to its participation in the Scheme. The Scheme prepares its financial statements as at 31 December annually.

Changes in the present value of the Scheme's liabilities:

£000	31 December 2016	31 December 2015
Benefit obligations at beginning of year	47,976	47,237
Interest costs	1,869	1,750
Current service costs	203	922
Members' contributions	31	122
Actuarial (gain) loss	10,038	(1,114)
Insured annuitants	16,478	-
Effects of curtailments or settlements	242	-
Benefits paid	(692)	(941)
Benefit obligations at the end of the year	76,145	47,976

Notes to the Financial Statements (continued)

29. Other liabilities (continued)

(b) Defined benefit obligations (continued)

The benefit obligations arising from Schemes that are wholly un-funded and wholly or partly funded are as follows:

£000	31 December 2016	31 December 2015
Un-funded (surplus) obligations	(2,371)	3,205
Wholly or partly funded obligations	-	-
Total	(2,371)	3,205

Changes in Scheme assets:

£000	31 December 2016	31 December 2015
Market value of assets at beginning of year	44,771	43,548
Expected return on Scheme assets	1,777	1,623
Insured annuitants	16,478	-
Actuarial (loss) gain	13,929	(997)
Members' contributions	2,239	1,439
Employer's contributions	31	122
Administration Expenses	(17)	(23)
Benefits paid	(692)	(941)
Market value of assets at end of year	78,516	44,771

Scheme assets as a percentage of total assets:

	31 December 2016	31 December 2015
Equities	23.70%	49.00%
Bonds	23.70%	12.30%
Property	2.10%	5.10%
Cash	50.50%	33.60%

Principal actuarial assumptions:

The overall expected return on assets has been derived by considering the long-term expected rate of return for each asset class and taking the average rates weighted by the proportion invested in each asset class at the year end.

	31 December 2016	31 December 2015
Discount rate	2.85%	3.90%
Price inflation	3.36%	3.30%
Rate of increase in salaries	2.36%	2.90%
Rate of increase for pensions in payment (LPI)	3.26%	3.20%
Post retirement mortality table	S2PA adjusted CMI 2014	PCMA00 adjusted for CMI 2011
	(Long Cohort)	(Long Cohort)
Expected return on assets	2.85%	3.90%

The bank expects to pay £nil (31 December 2016: £227,000) in contributions to defined benefit plans in 2017.

Notes to the Financial Statements (continued)

30. Accruals and deferred income

£000	31 December 2016	31 December 2015
Deferred income	5,246	4,078
Accrued interest	628	434
	5,874	4,512

31. Equity

(a) Capital

At 31 December 2016 the authorised share capital comprised 250,000,000 ordinary shares (31 December 2015: 250,000,000). These instruments have a par value of £1 and are all issued shares and fully paid.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the bank.

(b) Available for sale reserve

The available for sale reserve includes the cumulative net change in the fair value of available for sale investments, excluding impairment losses, until the investment is derecognised or impaired.

(c) Dividends

A dividend of £35,690,000 has been recommended for the year ended 31 December 2016 (31 December 2015: £45,450,000)

32. Related parties

(a) Parent and ultimate controlling party

The immediate parent company of the bank is Bank of China Limited (a company incorporated in the People's Republic of China). The ultimate holding company is China Investment Corporation Limited.

The largest and smallest group which includes the bank and which prepares publicly available consolidated financial statements is the Bank of China Limited. Copies of its consolidated financial statements are publicly available from the Head Office of the Bank of China Limited, 1 Fuxingmen Nei Dajie, Beijing 100818, People's Republic of China.

During the year ended 31 December 2016 there were no transactions which resulted in there being a change in the ultimate controlling party of the bank.

The bank regards the following as being related parties that exercise significant influence:

- Bank of China Limited
- China Investment Corporation Limited

Significant companies of the bank are; subsidiaries of the bank, subsidiaries and associated companies of the immediate parent company.

Notes to the Financial Statements (continued)

32. Related parties (continued)

Related party transactions occurred between the bank and the London Branch of Bank of China Limited. At 31 December 2016 the bank received £161,926,000 (31 December 2015: £122,351,000) which is 14% (31 December 2015: 14%) of its funding from Bank of China Limited, London Branch in the form of short-term funding. The funding is interest-bearing at market rate for the term and currency borrowed, and is repayable in accordance with the contractual maturity date of the deposit.

£000	Nature of related party	
	Significant influence	Significant company
Balance at 31 December 2016		
Cash and cash equivalents	80,942	-
Loans and advances to banks		
Loans and advances to customers	4	1
Derivative financial instruments	1,498	-
Prepayments, accrued income and other assets	4,603	-
Deposits from banks	161,926	-
Deposits from customers	-	10,014
Derivative financial instruments	627	-
Other liabilities	3,615	-
Subordinated liabilities	60,000	-
Included in the income statement for the period		
Interest receivable	110	-
Interest payable	(3,541)	-
Other operating income	52,149	54
Net loss on derivative financial instruments	(1)	-
Balance at 31 December 2015		
Cash and cash equivalents	94,309	-
Loans and advances to banks	-	-
Loans and advances to customers	13,229	1
Derivative financial instruments	390	-
Prepayments, accrued income and other assets	19,302	66
Deposits from banks	122,351	-
Deposits from customers	-	7,488
Derivative financial instruments	1,707	-
Other liabilities	6,562	-
Subordinated liabilities	60,000	-
Included in the income statement for the period		
Interest receivable	75	-
Interest payable	(581)	-
Other operating income	54,456	5,461
Net loss on derivative financial instruments	(1,810)	-

(b) Investment in non-consolidated subsidiaries

	Country of incorporation	Ownership interest	
		31 December 2016	31 December 2015
China Bridge Group (UK) Limited	United Kingdom	100%	100%
China Visa Services Italy SRL ¹	Italy	100%	100%

¹Indirect holding via China Bridge Group (UK) Limited

At 31 December 2016, the bank held an investment of £1 in China Bridge Group (UK) Limited (31 December 2015: £1). This entity is wholly-owned, with headquarters at 12 Old Jewry, London, United Kingdom. The bank has availed itself of the consolidation exemption (refer to Note 2) and therefore does not consolidate this subsidiary.

Notes to the Financial Statements (continued)

32. Related parties (continued)

(c) Key management compensation

Key management is comprised of directors and the members of the Executive Management Committee of the bank.

Key management personnel compensation for the period ended 31 December 2016 comprised of salaries and other short-term benefits in the amount of £1,540,000 (31 December 2015: £1,971,000).

The bank does not provide non-cash benefits to any of the key management personnel.

(d) Transactions with key management

£000	31 December 2016	31 December 2015
Loans and advances	-	1

33. Contingent liabilities and commitments

(a) Loan commitments, guarantees and other financial facilities

£000	31 December 2016	31 December 2015
Loan commitments	250,115	222,505
Guarantees	1,353	1,837
Total	251,468	224,342

(b) Operating lease commitments

Where the bank is the lessee, the future aggregate minimum lease payments under non-cancellable operating leases on buildings are as follows:

£000	31 December 2016	31 December 2015
Less than one year	555	494
Between one and five years	1,874	1,859
More than five years	925	105
Total	3,354	2,458

(c) Legal claims

On the 20 July 2012 the bank entered into a sale and purchase agreement ("SPA") to dispose of its investment in Bank of China (Suisse) S.A. ("BOCS"). The SPA contained provisions for the purchaser to be indemnified against additional costs relating to third party claims in two circumstances.

Firstly, for litigation claims identified at the date of the SPA and where the cost of settlement or court judgement exceeded the provisions made for these claims as recorded in the accounts of BOCS as at the closing date.

Secondly, for any claim, action, arbitration, investigation or proceeding by or before any court, tribunal or arbitral body, administrative board, commission or other authority against BOCS by third parties for events that occurred whilst the bank had control of BOCS. The period of this indemnity is for 5 years starting from the closing date being 1 October 2012. At the date of approval of these financial statements certain matters have been advised by the purchaser to the bank under this clause. At present it is not possible to predict the ultimate outcome of these claims, including the financial impact, and no provision has been recognised in respect of these items because the bank does not currently expect the final outcome of any such claims to have a material adverse effect on the bank's financial position.

34. Going concern assessment

The Board has given its consideration to the going concern status of the bank as at the reporting date. After due consideration the Board is of the opinion that the bank will continue as a going concern for the foreseeable future, generating cash flows from its continuing operations, but also taking additional comfort from a two year financial forecast.