SBI Canada Bank

Board Memorandum

Board Meeting Date	March 26, 2020
Title	Annual Audited Financial Statements 2019
Purpose:	Approval of the Board
Last Submitted on	NA
Observations of the Directors, if any	NA
Action taken on the observations/ Replies to the Director's observation	NA
Executive Summary	The Annual Financial Statements for the year ended December 31, 2019 were audited by external auditors (Deloitte) and reviewed by ACB in its meeting on March 11, 2020 and is now being recommended to Board for approval.

Joseph Selvaraj Savier
President & CEO

Amit Goyal
SVP & CFO

March 13, 2020

Financial statements of

SBI Canada Bank

December 31, 2019

SBI Canada Bank
December 31, 2019

Table of contents

Independent Auditor's Report 1-2

Statement of financial position 3

Statement of comprehensive income 4

Statement of changes in equity 5

Statement of cash flows 6

Notes to the financial statements 7-43

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Independent Auditor's Report

To the Shareholder of
SBI Canada Bank

Opinion
We have audited the financial statements of SBI Canada Bank (the "Bank"), which comprise the statement of financial position as at December 31, 2019, and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies (collectively referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at December 31, 2019, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion
We conducted our audit in accordance with Canadian generally accepted auditing standards ("Canadian GAAS"). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements
Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian GAAS will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian GAAS, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

[to be signed Deloitte LLP]

Chartered Professional Accountants
Licensed Public Accountants
March 26, 2020

SBI Canada Bank

Statement of financial position

as at December 31, 2019

(In thousands of Canadian dollars)

	Note	**2019**	2018
		$	$
Assets			
Cash and bank balances:			
Notes and coins		**768**	842
Deposits with banks:			
Interest bearing		**44,092**	33,290
Non-interest bearing		**16,282**	13,107
		61,142	47,239
Investment securities	4	**66,400**	71,925
Loans and advances to customers	5	**1,062,620**	974,627
Derivative assets	19	**2,241**	77
Property and equipment	7	**10,341**	727
Intangible assets	8	**63**	89
Deferred tax assets	13	**1,181**	1,225
Other assets	9	**6,950**	5,003
Total assets		**1,210,938**	1,100,912
Liabilities			
Deposits from banks	10	**74,173**	53,466
Deposits from customers	11	**926,632**	858,835
Derivative liabilities	19	**69**	1,356
Other liabilities	12	**33,589**	18,115
Subordinated debt	16	**20,000**	20,000
		1,054,463	951,772
Shareholder's equity			
Common share capital	17	**117,784**	117,784
Contributed surplus		**5,934**	5,934
Retained earnings		**32,708**	25,875
Accumulated other comprehensive income (loss)		**49**	(453)
		156,475	149,140
Total liabilities and shareholder's equity		**1,210,938**	1,100,912

Approved by the Board of Directors

__________________________ Director

__________________________ Director

The accompanying notes are an integral part of these financial statements.

SBI Canada Bank

Statement of comprehensive income
for the year ended December 31, 2019

(In thousands of Canadian dollars)

	Note	**2019**	2018
		$	$
Interest income:			
Loans		**38,678**	33,685
Deposits		**1,152**	877
Investment Securities		**1,773**	2,234
		41,603	36,796
Interest expense:			
Deposits and other	12	**20,203**	15,419
Subordinated debt		**635**	568
		20,838	15,987
Net interest income		**20,765**	20,809
Other income	14	**4,892**	5,217
Total revenue		**25,657**	26,026
Net impairment loss on loans and advances		**322**	(4,520)
Non-interest expenses:			
Personnel		**6,962**	6,314
Premises and equipment		**1,964**	2,896
Depreciation and amortization	7	**1,329**	246
Other	15	**4,930**	3,800
		15,185	13,256
Net income before income taxes		**10,150**	17,290
Provision for income taxes	13	**2,690**	4,745
Net income for the year		**7,460**	12,545
Other comprehensive income / (loss), net of income tax:			
Change in unrealized losses in investment securities at fair value through other comprehensive income net of income tax expenses of $178 (2018 - recovery of $10)		**492**	(21)
Provision for credit losses in debt securities at fair value through other comprehensive income recognized in income		**10**	46
Total comprehensive income for the year		**7,962**	12,570

SBI Canada Bank

Statement of changes in equity

for the year ended December 31, 2019

(In thousands of Canadian dollars)

2019	**Common share capital**	**Contributed surplus**	**Accumulated other comprehensive Income (loss)**	**Retained earnings**	**Total**
	$	**$**	**$**	**$**	**$**
Balance as at January 1, 2019	**117,784**	**5,934**	**(453)**	**25,875**	**149,140**
Comprehensive income:					
Net income for the year	**-**	**-**	**-**	**7,460**	**7,460**
Other comprehensive income, net of income tax expenses of $178:					
Net amount transferred to the Statement of comprehensive income	**-**	**-**	**82**	**-**	**82**
Net change in unrealized gain on: FVOCI securities	**-**	**-**	**420**	**-**	**420**
Dividend paid				**(627)**	**(627)**
Total comprehensive income	**-**	**-**	**502**	**6,833**	**7,335**
Balance as at December 31, 2019	**117,784**	**5,934**	**49**	**32,708**	**156,475**

2018	Common share capital	Contributed surplus	Accumulated other comprehensive Income (loss)	Retained earnings	Total
	$	$	$	$	$
Balance as at January 1, 2018	117,784	5,934	(478)	13,866	137,106
Impact on adoption of IFRS 9				(536)	(536)
Adjusted balance at beginning of year	117,784	5,934	(478)	13,330	136,570
Comprehensive income:					
Net income for the year	-	-	-	12,545	12,545
Other comprehensive income, net of income tax expenses of $20:					
Net amount transferred to the Statement of comprehensive income	-	-	(2)	-	(2)
Net change in unrealized loss on					
Available-for-sale securities	-	-	127	-	127
FVOCI securities	-	-	(100)	-	(100)
Total comprehensive income	-	-	25	12,545	12,570
Balance as at December 31, 2018	117,784	5,934	(453)	25,875	149,140

SBI Canada Bank

Statement of cash flows
for the year ended December 31, 2019

(In thousands of Canadian dollars)

	2019	2018
	$	$
Operating activities		
Net income for the year	**7,460**	12,545
Adjustments for:		
Provision for (recovery of) credit losses	**327**	(4,520)
Net gain on sale of investment securities	**(46)**	(23)
Depreciation and amortization	**1,329**	246
Loss on disposal of property and equipment	**7**	23
Net interest income	**(20,765)**	(20,809)
Income tax expense	**2,690**	4,745
Addition of Right of Use asset	**(10,678)**	-
Changes in:		
Net change in derivative financial instruments	**(3,451)**	3,500
Loans and advances to customers, net	**(88,318)**	(93,993)
Other assets	**(4,990)**	(4,524)
Deposits from banks, net	**20,707**	4,498
Deposits from customers, net	**67,797**	72,375
Other liabilities and provisions	**14,490**	(1,115)
Interest received	**41,822**	36,091
Interest paid	**(18,969)**	(12,665)
Cash generated from (used in) operating activities	**9,412**	(3,626)
Investing activities		
Net change in interest-bearing deposits	**(10,802)**	762
Proceeds from sale of investment securities	**58,105**	28,780
Purchase of investment securities	**(51,854)**	(15,122)
Purchase of property and equipment	**(246)**	(52)
Cash (used in) generated from investing activities	**(4,797)**	14,368
Financing activities		
Payment of lease liabilities	**(887)**	-
Payment of dividend	**(627)**	-
Cash (used in) financing activities	**(1,514)**	-
Net changes in cash and cash equivalents	**3,101**	10,742
Cash and cash equivalents, beginning of year	**13,949**	3,207
Cash and cash equivalents, end of year	**17,050**	13,949
Represented by:		
Cash and non-interest bearing bank balances	**17,050**	13,949
	17,050	13,949

(in thousands of Canadian dollars)

Notes to the financial statements

		Page			Page
1	Reporting entity	8	15	Other non-interest expenses	30
2	Basis of preparation	8	16	Subordinated debt	30
3	Significant accounting policies	9	17	Common shares capital	30
4	Investment securities	19	18	Capital management	31
5	Loans and advances to customers	20	19	Derivatives	32
6	Allowance for undrawn commitments	21	20	Related party transactions and balances	33
7	Property and equipment	22	21	Geographic information	35
8	Intangible assets	24	22	Fair values of financial instruments	36
9	Other assets	25	23	Commitments and contingencies	38
10	Deposits from banks	25	24	Guarantees	38
11	Deposits from customers	25	25	Interest rate risk and maturity profile	39
12	Other liabilities	26	26	Risk management framework	40
13	Income taxes	27	27	Subsequent event	43
14	Other income	29			

1. Reporting entity

SBI Canada Bank (the "Bank") is a wholly owned subsidiary of State Bank of India (the “parent bank”) and is licensed to operate in Canada as a bank with full banking powers under the Bank Act (Canada) as a foreign bank subsidiary. The Bank’s registered office is at 77 City Centre Drive, Suite 106, Mississauga, Ontario L5B 1M5, Canada. The Bank is involved in corporate and retail banking.

2. Basis of preparation

a) Statement of compliance

The financial statements have been prepared in accordance with Section 308(4) of the Bank Act (Canada), which states that, except as otherwise specified by the Office of the Superintendent of Financial Institutions Canada (“OSFI”), the financial statements are to be prepared in accordance with generally accepted accounting principles the primary source of which is the Chartered Professional Accountants Canada Handbook (the “Handbook”). The financial statements comply with Part 1 of the Handbook, International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

The financial statements for the year ended December 31, 2019 were authorized for issue by the Bank's Board of Directors on March 26, 2020.

b) Basis of measurement

These financial statements have been prepared on the historical cost basis except for Fair Value through Other Comprehensive Income (“FVOCI”) securities and derivative assets and derivative liabilities which are measured at fair value.

c) Functional and presentation currency

These financial statements are presented in Canadian dollars, which is the Bank's functional currency. Except as otherwise indicated, all financial information presented in Canadian dollars has been rounded to the nearest thousand.

d) Use of estimates and assumptions

The preparation of the financial statements in conformity with IFRS requires management to make subjective estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. Estimates made by management are based on historical experience and other assumptions that are believed to be reasonable. Key sources of estimation uncertainty include the allowance for impairment on loans and advances to customers (see Note 5), income taxes (see Note 13) and determination of fair value of financial instruments (see Note 22). Actual results may differ from those estimates. The estimates and underlying assumptions are reviewed on an ongoing basis and revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

e) Significant judgments

In the preparation of these financial statements, management is required to make significant judgments that affect the carrying amounts of certain assets and liabilities, and the reported amounts of revenue and expenses recorded during the year. Significant judgments have been made in the impairment assessment on loans and advances to customers, income taxes and determination of the fair value of financial instruments.

3. Significant accounting policies

The significant accounting policies used in the preparation of these financial statements, including the accounting requirements of OSFI, are summarized below. These accounting policies conform, in all material respects, to IFRS.

a) *Cash and cash equivalents*

Cash and cash equivalents comprise cash, deposits with banks and highly liquid investments that are convertible to cash and subject to insignificant risk of changes in value. Such investments have an original term to maturity of less than three months from the date of acquisition. Cash and deposits with banks are carried at amortized cost in the statement of financial position.

b) *Financial instruments*

Classification and measurement

In accordance with IFRS 9, Financial Instruments (“IFRS 9”), a financial asset is classified and measured based on the business model in which it is managed and the contractual cash flow characteristics of the financial asset.

The Bank’s loans are measured at amortized cost, securities at either amortized cost or fair value through other comprehensive income (FVOCI), and equity shares at FVOCI less any provision for impairment. Financial liabilities are measured at amortized cost. All other financial instruments have been designated in FVTPL.

For FVOCI investments, gains and losses arising from changes in fair value are recognized directly in equity, until the investment is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognized in equity, determined using the weighted average cost method, is included in the net profit or loss for the period.

The Bank assesses investments for impairment whenever events or changes in circumstances indicate that the carrying value of an investment may not be recoverable. If any such indication of impairment exists, the Bank makes an estimate of the recoverable amount. If the recoverable amount is less than the value of the investment, the investment is considered to be impaired and is written down to its recoverable amount. An impairment loss is recognized immediately in the profit and loss account.

Impairment

The impairment model for measuring impairment of financial assets is the expected credit loss (“ECL”) model. ECL is based on probability of default (“PD”), loss given default (“LGD”) and exposure at default (“EAD”) inputs and takes into account the expected timing of the loss. The ECL model also incorporates forward-looking economic information, primarily forecasts of the Canada unemployment rate, Canada housing price index, Bank of Canada overnight interest rate, the level of the Toronto Stock Exchange index (TSX), the 3-month US Treasury bill rate, the USD/CAD exchange rate as well as the use of experienced credit judgment, where applicable. There is significant management judgment involved in determining the ECL estimate based on the ECL model.

3. Significant accounting policies (continued)

b) Financial instruments (continued)

Impairment (continued)

The Bank's impairment model measures credit loss allowances using a three-stage approach, based on the extent of credit deterioration since origination:

- Stage 1 – for financial assets that have not experienced a significant increase in credit risk since initial recognition, an amount equal to 12 months expected credit loss is recorded. The expected credit loss is computed using a probability of default occurring over the next 12 months.
- Stage 2 – for financial assets that have experienced a significant increase in credit risk, but are not considered to be in default, the allowance is based on the probability of default over the remaining estimated life of the loan. This stage includes loans that are 30 days past due.
- Stage 3 – financial assets that are considered to be in default, which includes those financial assets that are 90 days past due, are included in this stage and the allowance for credit losses captures the lifetime expected credit losses.

The Bank's definition of default used to identify impaired financial assets includes financial assets that are more than 90 days past due. The definition of default used in the measurement of ECL and the assessment for movement between stages is consistent with the definition of default used for internal credit risk management purposes.

Hedge accounting

The Bank has not applied hedge accounting during the years ended December 31, 2019 and 2018.

Allowance for credit losses

The Bank maintains an allowance for credit risk allowances ("allowance") that represents management's estimate of expected credit losses for financial assets as of the date of the Statement of Financial Position. The allowance is a function of PD, LGD and EAD, and incorporates the expected timing of losses.

PD represents the likelihood that a financial asset will default over the following twelve months or, depending on credit deterioration from origination of the financial asset over the expected life of the loan. LGD is the amount that is expected not to be recovered in the event of default. EAD is the estimate of the outstanding amount of credit exposure at the time a default may occur. For undrawn amounts, EAD includes an estimate of any further amounts to be drawn at the time of default. These inputs are modelled based on historical data and reasonable and supportable information about future economic conditions, where appropriate.

Where modelling of a parameter is carried out on a collective basis, the financial assets are grouped on the basis of share risk characteristics that include instrument type, credit risk rating, industry and geographical location of the borrower. The groupings are subject to regular review to ensure that exposures within a particular group remain approximately homogeneous. All loans and other financial instruments except for non-mortgage retail loans are assessed on an individual basis, as per Credit Allowance Policy of the bank.

(in thousands of Canadian dollars)

3. Significant accounting policies (continued)

b) Financial instruments (continued)

Significant increase in credit risk

At each reporting date, the Bank assesses whether there has been a significant increase in credit risk since initial recognition by comparing the risk of default occurring over the remaining expected life from the reporting date and the date of initial recognition. The assessment considers borrower-specific quantitative and qualitative information and the impact of forward-looking macroeconomic factors. For loans and securities, significant increase in credit risk is assessed at the segment level and considers the proportionate change in PD, as well as the absolute change in PD. The thresholds used for PD migration are reviewed and assessed by management at least annually.

The Bank's impairment model measures credit loss allowances using the above-mentioned three-stage approach, based on the extent of credit deterioration since origination. As credit risk changes each period, a financial asset can transfer between stages.

Forward-looking macroeconomic information

The allowance reflects an unbiased, probability-weighted outcome which considers multiple scenarios based on reasonable and supportable forecasts. The inputs used to estimate expected credit losses are modelled based on macroeconomic variables that are most closely related with credit losses associated with the Bank's portfolio.

The measurement of ECL for each stage and the assessment of significant increases in credit risk considers information about past events and current conditions as well as reasonable and supportable forecasts of future events and economic conditions. The estimation and application of forward-looking information relies on the Bank's management to exercise significant judgement.

In evaluating the ECL model output, the Bank relies on a range of forward-looking information. The final determination of ECL is based on the model's output under three scenarios (weightings in brackets): Pessimistic (30%), Base (50%) and Optimistic (20%).

		2019			2018	
	Pessimistic (30%) 12 months	**Base (50%) 12 months**	**Optimistic (20%) 12 months**	**Pessimistic (30%) 12 months**	**Base (50%) 12 months**	**Optimistic (20%) 12 months**
Canada unemployment rate (%)	6.19	5.90	5.61	6.15	5.85	5.57
Canada housing price index	98.94	104.00	109.05	101.42	101.40	111.53
Bank of Canada overnight interest rate (%)	0.98	1.57	2.15	1.17	1.38	2.34
Toronto Stock Exchange index (TSX)	15,040	16,029	17,016	14,869	15,996	16,844
3-month US Treasury bill rate (%)	1.07	1.55	2.21	1.09	1.40	2.23
USD/CAD exchange rate	1.40	1.33	1.26	1.41	1.30	1.26

(in thousands of Canadian dollars)

3. Significant accounting policies (continued)

b) Financial instruments (continued)

Definition of default and write-off

The Bank considers a financial asset to be in default as a result of one or more loss events that occurred after the loss event has a negative impact on the estimated future cash flows of the financial assets that can be reliably estimated. The Bank considers that default has occurred and classifies the financial asset as impaired when it is more than 90 days past due.

The Bank writes-off an impaired financial asset and the related impairment allowance, either partially or in full, when there is no realistic prospect of further recovery.

In subsequent periods, any recoveries of amounts previously written-off as a result of a debt sale or other repayment, the amount is credited to the provision for credit losses.

The following table sets out the Bank's credit risk exposure for all financial assets and loan commitments as at December 31, 2019 and 2018. Stage 1 represents those performing assets with a 12-month expected credit loss allowance, Stage 2 represents performing loans with a lifetime expected credit loss allowance, and Stage 3 represents impaired loans with a lifetime credit loss allowance.

2019				
(Thousands of Canadian dollars)	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Financial Assets				
A. SBIC 0 to 12	990,886	123,639	-	1,114,525
B. SBIC 13	-	15,929	-	15,929
C SBIC 14	-	2,640	-	2,640
D. Impaired	-	-	512	512
Gross Carrying Amount	**990,886**	**142,208**	**512**	**1,133,606**
Loss Allowance	2,146	1,015	75	3,236
Net Carrying Amount	**988,740**	**141,193**	**437**	**1,130,370**

(Thousands of Canadian dollars)	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Loan commitments				
A. SBIC 0 to 12	71,957	8,470	-	80,427
B. SBIC 13	-	-	-	-
C SBIC 14	-	-	-	-
D. Impaired	-	-	-	-
Gross Carrying Amount	**71,957**	**8,470**	**-**	**80,427**
Loss Allowance	2	-		2
Net Carrying Amount	**71,955**	**8,470**	**-**	**80,425**

(in thousands of Canadian dollars)

3. Significant accounting policies (continued)

b) Financial instruments (continued)

Definition of default and write-off (continued)

2018				
(Thousands of Canadian dollars)	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Financial Assets				
A. SBIC 0 to 12	899,048	123,969	-	1,023,017
B. SBIC 13	-	10,017	-	10,017
C SBIC 14	-	16,365	-	16,365
D. Impaired	-	-	-	-
Gross Carrying Amount	**899,048**	**150,351**	**-**	**1,049,399**
Loss Allowance	1,425	1,491		2,916
Net Carrying Amount	**897,623**	**148,860**		**1,046,483**

(Thousands of Canadian dollars)	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Loan commitments				
A. SBIC 0 to 12	88,797	7,418	-	96,215
B. SBIC 13	-	12,196	-	12,196
C SBIC 14	-	-	-	-
D. Impaired	-	-	-	-
Gross Carrying Amount	**88,797**	**19,614**	**-**	**108,411**
Loss Allowance				
Net Carrying Amount	**88,797**	**19,614**	**-**	**108,411**

The following table shows the continuity in the loss allowance for financial assets and loan commitments for the year ended December 31, 2019.

2019	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
	$	**$**	**$**	**$**
Balance at January 1	1,425	1,491	-	2,916
Charges (recovery) for the year	723	(476)	75	322
Balance at December 31	**2,148**	**1,015**	**75**	**3,238**

3. Significant accounting policies (continued)

b) Financial instruments (continued)

Modifications

From time to time the Bank modifies the contractual terms of a loan due to the poor financial condition of the borrower. In this case, the Bank assesses renegotiated loans for impairment consistent with the existing policies for impairment. When renegotiation leads to significant concessions being granted, and the concessions are for economic or legal reasons related to the borrower's financial difficulty that we would not otherwise consider, the loan is classified as impaired. The Bank considers one or a combination of the following to be significant concessions: (1) a reduction of the stated interest rate, (2) an extension of the maturity date or dates at a stated interest rate lower than the current market rate for a new loan with similar terms, or (3) forgiveness of principal or accrued interest. Renegotiated loans are permitted to remain in performing status if the modifications are not considered to be significant, or are returned to performing status when none of the criteria for classification as impaired continue to apply.

The Bank had no financial assets that were so modified as on December 31, 2019 and 2018.

However, as on December 31, 2019 one residential mortgage loan (outstanding balance $512) is classified as Stage 3 asset due to non-payment. The Bank has initiated "Power of Sale" legal action for the same.

c) Derivative financial instruments

Derivative instruments are financial contracts whose value is derived from interest rates, foreign exchange rates, commodity, equity prices or other financial variables.

Derivative financial instruments are recorded on the statement of financial position at fair value and include consideration of credit risk. These are reported as assets when they have a positive fair value and as liabilities when they have a negative fair value. Changes in fair value of derivative financial instruments are recognized in the statement of comprehensive income.The Bank has not designated any derivatives in hedging relationships.

Derivatives may be embedded in other financial instruments. Derivatives embedded in other financial instruments are valued as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host contract; the terms of the embedded derivative would meet the definition of a derivative if it was a free standing instrument; and the combined contract is not classified as held-for-trading or designated at fair value. These embedded derivatives are accounted for depending on their classification and are presented in the statement of financial position together with the host contract.

3. Significant accounting policies (continued)

d) Property and equipment

Property and equipment include furniture and equipment, computers and leasehold improvements. Items of property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. Gains and losses on disposal of these assets are recorded in other income in the year of disposal.

Depreciation is calculated over the depreciable amount, which is the cost of an asset less its residual value and is recognized in the statement of comprehensive income on a declining-balance method over the estimated useful lives of the asset. Depreciation methods, useful lives and residual values are reviewed annually and adjusted if appropriate.

The annual depreciation rates for furniture and equipment and computers are as follows:

Furniture and equipment	20%
Computers	30%

Leasehold improvements are amortized over the term of the related lease using the straight-line method.

e) Intangible assets

Intangible assets are purchased computer software that is not an integral part of the related hardware.

Cost includes expenditure that is directly attributable to the acquisition of the software. Gains and losses on disposal of these assets are recorded in other income in the year of disposal.

Depreciation is calculated over the depreciable amount, which is the cost of the software less its residual value and is recognized in the statement of comprehensive income on a declining-balance method over the estimated useful lives of the asset. Depreciation methods, useful lives and residual values are reviewed annually and adjusted if appropriate.
The annual depreciation rates for various software are as follows:

Banking system software	25%
Other software	30%

f) Acceptances

Acceptances comprise undertakings by the Bank to pay bills of exchange drawn on by customers. The Bank expects most acceptances to be settled simultaneously with the reimbursement from the customers.

The Bank's potential liability under acceptances is reported as a liability in the statement of financial position. The Bank's recourse against the customer in the event of a call on any of these commitments is reported as an asset of the same amount. Fees earned are reported as other income.

3. Significant accounting policies (continued)

g) Provisions

A provision is recognized if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in provisions due to the passage of time is recognized as interest expense in the statement of comprehensive income.

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security, are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of the Bank; or are present obligations that have arisen from past events that are not recognized because it is not probable that settlement will require an outflow of economic benefits, or because the amount of the obligations cannot be reliably measured. Contingent liabilities are not recognized in the financial statements but are disclosed unless the probability of settlement is remote.

h) Guarantees

A guarantee is defined to be a contract that contingently requires the Bank to make payments to a third party based on: (a) changes in an underlying interest rate, foreign exchange rate, equity or commodity instrument, index or other variable, that is related to an asset, a liability or an equity security of the counterparty, (b) failure of another party to perform under an obligating agreement or (c) failure of another third party to pay its indebtedness when due. Significant guarantees that the Bank has provided to third parties include guarantees and standby letters of credit. These are considered guarantees and represent obligations to make payments to third parties, on behalf of customers, if they are unable to make required payments or to meet other contractual requirements. Collateral requirements for guarantees and standby letters of credit are consistent with collateral requirements for loans.

i) Interest

Interest income and expense are recognized in the statement of comprehensive income using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes all fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the statement of comprehensive income include:

- interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis; and
- interest on AFS investment securities calculated on an effective interest basis.

3. Significant accounting policies (continued)

j) Foreign currency transactions

Transactions in foreign currencies are translated into Canadian dollars at the spot exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to Canadian dollars at the exchange rate at that date. Foreign currency non-monetary items that are measured at historical cost are translated into Canadian dollars at historical rates. Foreign currency non-monetary items measured at fair value are translated into Canadian dollars using the rate of exchange at the date the fair value was determined.

Translation gains and losses related to the Bank's monetary items are recognized in the statement of comprehensive income. Revenues and expenses denominated in foreign currencies are translated using average exchange rates. Translation gains and losses related to changes in the amortized cost of Canadian-dollar denominated monetary asset classified as AFS are recognized in the statement of comprehensive income, and other changes in the carrying amount, except impairment, are recognized in other comprehensive income.

k) Income taxes

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in the statement of comprehensive income except to the extent that it relates to items recognized directly in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

l) Related party transactions

Unless otherwise stated, all related party transactions are considered to be in the normal course of operations and are measured at the exchange amount, being the amount of consideration established and agreed to between the related parties.

m) Share capital

Common shares are classified as common share capital within shareholder’s equity. Incremental costs directly attributable to the issue of common shares are recognized as a deduction from common share capital, net of any tax effects.

3. Significant accounting policies (continued)

n) Standards adopted in the current year

Effective January 1, 2019, the Bank adopted IFRS 16 Leases (“IFRS 16”), which specifies how to recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value.

The Bank assesses whether a contract is, or contains, a lease based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. If a contract contains a lease, the Bank will recognize a right-of-use asset (“ROU”) and a lease liability at the lease commencement date. The ROU asset and lease liability are initially measured as an amount equal to the present value of the remaining lease payments over the lease. The discount rate to be used is the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank’s incremental borrowing rate. The Bank uses its incremental borrowing rate as the discount rate.

The ROU is depreciated to the earlier of the end of the useful life or lease term using the straight-line method as this reflects the expected pattern of use. At each reporting date, the ROU asset is tested for impairment. If an impairment event has occurred, then an impairment loss is recognized.

The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in rates or there is a change in the Bank’s estimate of the amount expected to be payable.

The Bank adopted IFRS 16 using the modified retrospective approach and accordingly the information presented for 2018 has not been restated. It remains as previously reported under IAS 17, Leases. As a practical expedient, IFRS 16 permits a lessee not to separate non-lease components, and instead account for any lease and associated non-lease components as a single arrangement. The Bank has used this practical expedient.

On initial recognition, the Bank has elected to record ROU assets based on the corresponding lease liability. The ROU asset and lease liability of $10,678 is recorded as of January 1, 2019, with no net impact to retained earnings. When measuring the lease liability, the Bank discounted future remaining lease payments using its incremental borrowing rate at January 1, 2019.

(in thousands of Canadian dollars)

4. Investment securities

(a) Carrying Value of securities

(i) FVOCI Securities

As at December 31, the fair value of the FVOCI securities is as shown below:

	2019				2018			
	Amortized cost	**Gross unrealized gains**	**Gross unrealized losses**	**Fair value of securities**	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value of securities
	$	**$**	**$**	**$**	$	$	$	$
Government bonds	**23,379**	**-**	**(92)**	**23,286**	24,013	-	(333)	23,680
Corporate bonds	**42,942**	**96**	**(20)**	**43,018**	26,395	-	(387)	26,008
Corporate equities	**95**	**1**	**-**	**96**	95	42	-	137
	66,416	**97**	**(112)**	**66,400**	50,503	42	(720)	49,825

As at December 31, the composition and maturity profile of FVOCI securities are as follows:

	2019				2018			
	Under 1 year	**2 to 5 years**	**With no specific maturity**	**Total**	Under 1 year	2 to 5 years	With no specific maturity	Total
	$	**$**	**$**	**$**	$	$	$	$
Government bonds	**16,075**	**7,212**	**-**	**23,286**	5,052	18,628	-	23,680
Corporate bonds	**34,036**	**8,982**	**-**	**43,018**	-	26,008	-	26,008
Corporate equities	**-**	**-**	**96**	**96**	-	-	137	137
Total	**50,111**	**16,194**	**96**	**66,400**	5,052	44,636	137	49,825

As at December 31, 2019, interest-bearing bonds with stated interest rates of 2.45% to 5.84% (2018 - 3.13% to 5.84%) are included within the above FVOCI securities, and include $9,431 (2018 - $9,880) denominated in foreign currencies, which are principally U.S. dollar-denominated.

(in thousands of Canadian dollars)

4. Investment securities (continued)

(ii) Amortized cost securities, net of allowance

	2019	2018
Amortized cost securities, net of allowance		
Corporate bonds	-	22,100
Total	-	22,100

As at December 31, the composition and maturity profile of amortized cost securities are as follows:

	2019			**2018**		
	Under 1 year	**2 to 5 years**	**Total**	Under 1 year	2 to 5 years	Total
	$	**$**	**$**	$	$	$
Corporate bonds	**-**	**-**	**-**	22,100	-	22,100
Total	**-**	**-**	**-**	22,100	-	22,100

As at December 31, 2019, included within the above debt securities at amortized cost are interest-bearing bonds with stated interest rates of Nil (2018 - 3.05% to 4.80%), and amortized cost securities include Nil (2018 - $19,109) denominated in foreign currencies, which were principally U.S. dollar-denominated.

5(a). Loans and advances to customers

As at December 31, an analysis of the Bank's loan portfolio by category is as follows:

	2019			2018		
	Gross amount	**Impairment allowance**	**Carrying amount**	Gross amount	Impairment allowance	Carrying amount
	$	**$**	**$**	$	$	$
Retail customers:						
Mortgage lending	**100,980**	**336**	**100,644**	97,436	248	97,188
Personal loans	**28,015**	**6**	**28,009**	23,169	10	23,159
	128,995	**342**	**128,653**	120,605	258	120,347
Corporate customers:						
Mortgage lending	**378,822**	**564**	**378,258**	371,900	426	371,474
Syndication	**549,858**	**2,266**	**547,592**	474,707	2,163	472,544
Other	**8,117**	**-**	**8,117**	10,262	-	10,262
	936,797	**2,830**	**933,967**	856,869	2,589	854,280
	1,065,792	**3,172**	**1,062,620**	977,474	2,847	974,627

As at December 31, 2019, loans and advances to customers include $393,040 (2018 - $317,175) denominated in foreign currencies, which are principally U.S. dollar-denominated.

(in thousands of Canadian dollars)

5(b). Allowance for credit losses for loans and advances to customers

	2019	2018
	$	$
Specific allowance for impairment:		
Balance at January 1	**-**	12,604
Impairment loss for the year:		
Charges (recovery) for the year	**75**	(3,316)
Write-offs	**-**	(9,518)
Other movements	**-**	230
Balance at December 31	**75**	-
Collective allowance for impairment:		
Balance at January 1	**2,847**	3,121
Impairment loss for the year:		
Charges for the year	**250**	(1,185)
Other movements	**-**	911
Balance at December 31	**3,097**	2,847
Total allowances	**3,172**	2,847

6. Allowance for undrawn commitments

	2019	2018
	$	$
Undrawn commitments	**80,428**	95,951
Allowance for undrawn commitments:		
Balance at January 1	-	270
Charges for the year	2	-
Other movements	-	(270)
Balance at December 31	**2**	**-**

The allowance for undrawn commitments is included in other liabilities in the statement of financial position.

(in thousands of Canadian dollars)

7. Property and Equipment (including ROU Assets)

Cost:

	Furniture and equipment	Computers	Leasehold improvements	Right of Use assets	Total
	$	$	$	$	$
Balance at January 1, 2019	**1,743**	**218**	**2,125**	**-**	**4,086**
Acquisitions	**13**	**221**	**12**	**10,678**	**10,924**
Disposals	**10**	**135**	**-**	**-**	**145**
Balance at December 31, 2019	**1,746**	**304**	**2,137**	**10,678**	**14,865**
Balance at January 1, 2018	1,768	252	2,125	-	4,145
Acquisitions	29	23	-	-	52
Disposals	54	57	-	-	111
Balance at December 31, 2018	1,743	218	2,125	-	4,086

Accumulated depreciation:

	Furniture and equipment	Computers	Leasehold improvements	Right of Use assets	Total
	$	$	$	$	$
Balance at January 1, 2019	**1,504**	**172**	**1,683**	**-**	**3,359**
Depreciation for the year	**48**	**46**	**174**	**1,035**	**1,303**
Disposals	**7**	**131**	**-**	**-**	**138**
Balance at December 31, 2019	**1,545**	**87**	**1,857**	**1,035**	**4,524**
Balance at January 1, 2018	1,481	212	1,544	-	3,237
Depreciation for the year	56	15	139	-	210
Disposals	33	55	-	-	88
Balance at December 31, 2018	1,504	172	1,683	-	3,359

Carrying amounts:

	Furniture and equipment	Computers	Leasehold improvements	Right of Use assets	Total
	$	$	$	$	$
Balance at December 31, 2019	**201**	**217**	**280**	**9,643**	**10,341**
Balance at December 31, 2018	239	46	442	-	727

(in thousands of Canadian dollars)

7. Property and Equipment (including ROU Assets) (continued)

Right of Use assets

Cost:	**Premises**	**Equipment**	**Vehicle**	**Total**
	$	**$**	**$**	**$**
Balance at January 1, 2019	**-**	**-**	**-**	**-**
Adoption of IFRS 16 (Note 3 (n))	**10,462**	**187**	**29**	**10,678**
Additions during the year	**-**	**-**	**-**	**-**
Balance at December 31, 2019	**10,462**	**187**	**29**	**10,678**

Accumulated Depreciation:	**Premises**	**Equipment**	**Vehicle**	**Total**
	$	**$**	**$**	**$**
Balance at January 1, 2019	**-**	**-**	**-**	**-**
Charge for the year	**984**	**37**	**14**	**1,035**
Balance at December 31, 2019	**984**	**37**	**14**	**1,035**

Carrying Amount:	**Premises**	**Equipment**	**Vehicle**	**Total**
	$	**$**	**$**	**$**
Balance at December 31, 2019	**9,479**	**149**	**15**	**9,643**

The Bank leases office premises, equipment and vehicles. The lease term on premises ranges from 1 to 10 years with most leases having an option to extend the lease at the end of the lease term. The lease term on equipment and vehicle ranges from 3 to 5 years with no renewal option.

(in thousands of Canadian dollars)

8. Intangible assets

Cost

	Purchased software
	$
Balance at January 1, 2019	**1,208**
Acquisitions	**-**
Balance at December 31, 2019	**1,208**
Balance at January 1, 2018	1,208
Acquisitions	-
Balance at December 31, 2018	1,208

Accumulated depreciation

	Purchased software
	$
Balance at January 1, 2019	**1,119**
Depreciation for the year	**26**
Balance at December 31, 2019	**1,145**
Balance at January 1, 2018	1,083
Depreciation for the year	36
Balance at December 31, 2018	1,119

Carrying amounts

	Purchased software
	$
Balance at December 31, 2019	**63**
Balance at December 31, 2018	89

(in thousands of Canadian dollars)

9. Other assets

	2019	2018
	$	$
Accrued interest receivable	**2,425**	2,644
Prepaid expenses	**2,204**	1,778
Income tax receivable	**1,400**	-
Other	**921**	581
	6,950	5,003

10. Deposits from banks

	2019	2018
	$	$
Current deposits from banks	**2,824**	5,721
Money market term deposits	**71,349**	47,745
	74,173	53,466

As at December 31, 2019, deposits from the parent bank and other related parties was $2,678 (2018 - $5,538).

11. Deposits from customers

Deposits are measured upon initial recognition at their fair value less directly attributable incremental transaction costs. Deposits are subsequently measured at amortized cost using the effective interest method.

	2019	2018
	$	$
Retail customers:		
Term deposits	**254,310**	227,046
Current deposits	**160,883**	164,502
Corporate customers:		
Term deposits	**472,865**	419,996
Current deposits	**38,574**	47,291
	926,632	858,835

At December 31, 2019, $273,496 (2018 - $242,356) of deposits from customers are expected to be settled more than 12 months after the reporting date. Total deposits include $106,219 (2018 - $115,622) denominated in foreign currencies, which are principally U.S. dollar-denominated.

(in thousands of Canadian dollars)

12. Other liabilities

	2019	2018
	$	$
Accrued interest payable	**12,439**	10,570
Lease obligation	**9,813**	-
Loans funding obligation	**7,156**	-
Cheques and other items in transit	**2,340**	1,055
Accounts payable	**1,777**	1,890
Deferred income	**63**	1,921
Allowance for off-balance sheet commitments	**2**	-
Income tax payable	**-**	2,679
	33,589	18,115

As at December 31, 2019, other liabilities include a loan of $ 7,156 (2018 - $Nil) on risk-participation basis which is not funded and reported as loan funding obligation.

As at December 31, 2019, the details relating to the Bank's lease obligation which is included with Other liabilities is as follows:

Lease Liabilities	**2019**
	$
Analysed as:	
Amounts due within 12 months	**884**
Amounts due after 12 months	**8,929**
Balance at December 31, 2019	**9,813**

As at December 31, 2019, the maturity of the lease obligation, on an undiscounted basis, is as follows:

Maturity Analysis	**2019**
	$
Year 1	**1,082**
Year 2	**1,070**
Year 3	**1,047**
Year 4	**1,092**
Year 5	**989**
Onwards	**5,626**
Total undiscounted lease obligation	**10,906**

During the year ended December 31, 2019, the interest expense on lease obligations was $320 which is presented as part of Interest expense: Deposit and others in the Statement of comprehensive income and the total outflow for leases was $1,207. As at December 31, 2019, the Bank does not have any significant liquidity risk with regards to its lease obligations, which are monitored regularly within the Bank's Operations function.

(in thousands of Canadian dollars)

13. Income taxes

a) Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in the statement of comprehensive income, except to the extent that it relates to items recognized directly in equity or in other comprehensive income.

The Bank's income taxes for the year ended December 31 are summarized below:

i) Income tax recognized in the statement of comprehensive income

	2019	2018
	$	$
Current tax:		
In respect of the current year	**2,824**	4,207
Current tax reclassified to other comprehensive income	**(178)**	9
Deferred tax:		
In respect of the current year	**44**	529
	2,690	4,745

ii) Income tax recognized in other comprehensive income

	2019	2018
	$	$
Current tax:		
Fair value remeasurement of available-for-sale financial assets	**148**	(8)
Current tax reclassified to comprehensive income	**30**	(1)
	178	(9)

(in thousands of Canadian dollars)

13. Income taxes (continued)

b) i) Significant components of the Bank's deferred tax assets/(liabilities) as at December 31 are:

			2019			2018
	Assets	**Liabilities**	**Net**	Assets	Liabilities	Net
	$	**$**	**$**	$	$	$
Property and equipment	**35**	**7**	**28**	-	10	(10)
Intangible assets	**-**	**17**	**(17)**	-	24	(24)
Allowances for loan losses	**842**	**-**	**842**	775	-	775
Net unearned fees	**685**	**357**	**328**	808	324	484
Net tax assets/(liabilities)	**1,562**	**381**	**1,181**	1,583	358	1,225

b) ii) The following is the analysis of deferred assets/(liabilities) presented in the statement of financial position:

2019	**Opening balance**	**Impact on adoption on IFRS 9**	**Recognised in profit or loss**	**Recognised in other comprehensive income**	**Closing balance**
	$	$	$	$	$
Property and equipment	**(10)**	**-**	**38**	**-**	**28**
Intangible assets	**(24)**	**-**	**7**	**-**	**(17)**
Allowances for loan losses	**775**	**-**	**67**	**-**	**842**
Net unearned income	**484**	**-**	**(156)**	**-**	**328**
	1,225	**-**	**(44)**	**-**	**1,181**

2018	Opening balance	Impact on adoption on IFRS 9	Recognised in profit or loss	Recognised in other comprehensive income	Closing balance
	$	$	$	$	$
Property and equipment	(16)	-	6	-	(10)
Intangible assets	(33)	-	9	-	(24)
Allowances for loan losses	1,165	194	(584)	-	775
Net unearned income	445	-	39	-	484
	1,561	194	(530)	-	1,225

(in thousands of Canadian dollars)

13. Income taxes (continued)

c) Total income tax expense differs from the amounts computed by applying the combined statutory federal and provincial tax rate of 26.57% (2018- 26.57%) to pre-tax income as a result of the following:

	2019	2018
	$	$
Net income before income taxes	**10,150**	17,290
Income taxes at statutory tax rate	**2,696**	4,594
Increase in income taxes resulting from:		
Non-deductible items	**2**	3
Other	**(8)**	148
Income taxes	**2,690**	4,745
Effective tax rate	**26.50%**	27.44%

14. Other income

	2019	2018
	$	$
Loan fees	**2,305**	2,337
Foreign exchange gain	**881**	1,270
Other	**772**	862
Remittances	**465**	451
Net gains on sale of available-for-sale corporate bonds	**194**	23
Guarantees	**190**	108
Collection charges	**139**	121
Letters of credit	**46**	54
Interest rate contracts	**(100)**	(9)
	4,892	5,217

(in thousands of Canadian dollars)

15. Other non-interest expenses

	2019	2018
	$	$
Insurance	**1,958**	979
Parent bank charges	**480**	520
Professional fees	**468**	233
Other	**449**	709
Communications	**385**	441
Brokerage and bank charges	**304**	60
Travelling	**243**	314
Directors' fees	**150**	150
Advertisement	**143**	102
Association and regulatory	**135**	132
Legal	**125**	67
Printing and stationery	**90**	93
	4,930	3,800

16. Subordinated debt

As at December 31, 2019, the Bank has subordinated debt, issued on December 31, 2010 which, in the event of the winding up of the Bank, is unsecured and subordinated to all of the Bank's deposits liabilities and all other liabilities, issued to its parent bank in the amount of $20,000 (2018 - $20,000). The subordinated debt is measured at amortized cost, using the effective interest method.

The subordinated debt bears interest at the rate of six months CDOR plus 1% per annum, payable semi-annually in arrears, until its maturity date of December 31, 2025. At the Bank's option, the subordinated debt may be redeemed or purchased by the Bank, with the prior written approval of OSFI to such redemption or purchase, on or after December 31, 2020.

On February 23, 2013, the Bank in discussions with OSFI and its parent bank amended certain terms of the subordinated debt instrument to comply with the requirements of Basel III and the guidance issued by OSFI whereby, under certain triggering events, the amount outstanding under the subordinated debt together with accrued and unpaid interest will automatically be converted into newly issued and fully paid common shares of the Bank.

17. Common share capital

Authorized:

An unlimited number of common shares at par value of $100

Issued and fully paid up:

		2019		2018
	Number	Amount	Number	Amount
		$		$
Balance, beginning of year	**470,090**	**117,784**	470,090	117,784
Balance, end of year	**470,090**	**117,784**	470,090	117,784

(in thousands of Canadian dollars)

18. Capital management

Capital levels for Canadian banks are regulated pursuant to guidelines issued by OSFI. Regulatory capital is allocated to two tiers: Tier 1 and Tier 2. Total capital is defined as the total of Tier 1 and Tier 2 capital less deductions as prescribed by OSFI.

As at December 31, the Bank is in compliance with the requirements for assets to capital multiple and risk-based Tier 1 and capital ratios.

	Basel III as at December 31, 2019	Basel III as at December 31, 2018
	$	$
Regulatory capital and capital ratios:		
Common Equity Tier 1 capital:		
Common shares	**117,784**	117,784
Contributed surplus	**5,934**	5,934
Retained earnings	**32,708**	25,875
Accumulated other comprehensive income / (loss)	**49**	(453)
Common Equity Tier 1 capital before regulatory adjustments	**156,475**	149,140
Total regulatory adjustments to Common Equity Tier 1	**(46)**	(65)
Total Tier 1 capital	**156,429**	149,075
Tier 2 capital:		
Subordinated debt	**20,000**	20,000
Total regulatory capital	**176,429**	169,075
Capital ratios:		
Tier 1 capital	**13.95%**	14.21%
Total capital	**16.01%**	16.39%

Capital ratios are calculated by dividing Tier 1 and Total capital by risk-weighted assets ("RWA"). The calculation of RWA is determined by OSFI prescribed rules relating to on-balance sheet and off-balance sheet exposures and includes an amount for the market risk exposure associated with the Bank's derivative portfolio.

In addition to the Tier 1 and Total capital ratios, Canadian banks are required to ensure that their leverage ratio, which is calculated by dividing capital measure (Tier 1 capital) by exposure measure (the sum of on-balance sheet items and specified off-balance sheet items, net of specified adjustments), meets or exceeds a minimum level prescribed by OSFI. Capital measure and exposure measure are defined in OSFI's Leverage Requirements guideline. An analysis of leverage ratio is as follows:

	2019	2018
	$	$
On-balance sheet items and specified off-balance sheet items, net of specified adjustments	**1,250,911**	1,165,440
Leverage Ratio	**12.51%**	12.79%

(in thousands of Canadian dollars)

19. Derivatives

In the ordinary course of business, the Bank uses derivative financial instruments, primarily over-the-counter foreign exchange contracts and interest rate contracts to manage its exposure to currency and interest rate fluctuations, as part of the Bank's asset liability management program.

The Bank economically hedges exposure on its assets and liabilities by entering into foreign exchange contracts and interest rate contacts. These derivatives are not designated for hedge accounting and are carried at fair value, with changes in fair value being recorded in other income.

Notional amounts of derivative contracts serve as reference for calculating payments and are a common measure of business volume. The following is a summary of the notional amounts, by remaining term to maturity, of the Bank's derivative positions at the statement of financial position date:

The following is a summary of the Bank's derivative positions and related credit exposures as at December 31:

				2019	2018
	Within 1 year	**1 to 5 years**	**Over 5 years**	**Total**	Total
	$	**$**	**$**	**$**	$
Foreign exchange contracts	**224,037**	**-**	**-**	**224,037**	189,538
Interest rate contracts	**11,486**	**7,000**	**-**	**18,486**	18,821
	235,523	**7,000**	**-**	**242,523**	208,359

The following is a summary of the fair value of the Bank's derivative portfolio at the statement of financial position date classified by positive and negative fair values:

			2019			2018
	Positive fair value	**Negative fair value**	**Net fair value**	Positive fair value	Negative fair value	Net fair value
	$	**$**	**$**	$	$	$
Foreign exchange contracts	**3,954**	**(2)**	**3,952**	1	(1,354)	(1,353)
Interest rate contracts	**12**	**(67)**	**(55)**	76	(2)	74
	3,966	**(69)**	**3,897**	77	(1,356)	(1,279)
Variation Margin	**(1,725)**	**-**	**(1,725)**	-	-	-
	2,241	**(69)**	**2,172**	**77**	**(1,356)**	**(1,279)**

To reduce adverse liquidity shocks and in order to effectively mitigate counterparty credit risk, variation margin is calculated and exchanged for non-centrally cleared derivatives subject to a single, legally enforceable netting agreement.

(in thousands of Canadian dollars)

19. Derivatives (continued)

Current Replacement Cost is the fair value of the outstanding derivative financial instruments net of collateral, which represent the bank’s derivative credit exposure.

Credit equivalent amount is the current replacement cost for favourable contracts plus an amount for the future credit exposure associated with the potential future changes in currency rates for the contracts. Future credit exposure is calculated using a formula prescribed by OSFI.

Risk-weighted amount represents the credit equivalent amount weighted according to the creditworthiness of the counterparty, using factors prescribed by OSFI.

The following is a summary of the Bank's derivative positions and related credit exposures as at December 31:

			2019			2018
	Current replacement cost	**Credit equivalent amount**	**Risk-weighted amount**	Current replacement cost	Credit equivalent amount	Risk-weighted amount
	$	**$**	**$**	$	$	$
Canada						
Foreign exchange contracts	**1,601**	**5,194**	**1,039**	-	1,451	290
Interest rate contracts	**2**	**33**	**7**	76	170	61
Other Countries						
Foreign exchange contracts	**626**	**2,441**	**488**	1	409	85
Interest rate contracts	**-**	**37**	**37**	-	-	-
	2,230	**7,704**	**1,570**	77	2,030	436

20. Related party transactions and balances

The Bank is a wholly-owned subsidiary of State Bank of India (the “parent bank”) which is incorporated under the State Bank of India Act, 1955, and has its registered office in Mumbai, India. The largest and smallest group which includes the Bank, and which prepares publicly available consolidated financial statements is the parent bank.

a) Parent and its related parties

The Bank enters into transactions with its parent bank and entities under common control by the parent bank in the normal course of business and on commercial terms which are recorded by the Bank at the exchange amount, being the amount of consideration established and agreed to among the related parties. The Bank relies on its parent bank for a certain portion of its funding requirement.

(in thousands of Canadian dollars)

20. Related party transactions and balances (continued)

a) Parent and its related parties (continued)

During the year ended December 31, the balances and transactions with the parent bank and entities under common control by the parent bank are as follows:

	2019	2018
	$	$
Assets:		
Deposits with banks	**1,311**	2,330
Liabilities:		
Deposits from banks	**74,026**	53,283
Derivative liabilities	**57**	2
Other liabilities	**452**	520
Subordinated debt	**20,000**	20,000
Statement of comprehensive income		
Interest income	**19**	68
Interest expenses	**3,239**	2,858
Other income	**22**	16
Non-interest expenses	**564**	617
Derivatives		
Foreign exchange contracts	**-**	294

b) Central Government of India related entities

The Bank enters into transactions with other entities under common control by The Central Government of India, which controls a number of government entities, including the Bank's parent bank. These transactions are entered into in the normal course of business and on commercial terms which are recorded by the Bank at the exchange amount, being the amount of consideration established and agreed to among the related parties.

During the year ended December 31, the balances and transactions with the Central Government of India related entities are as follows:

	2019	2018
	$	$
Assets:		
Loan and advances to customers	**-**	-
Liabilities:		
Deposits from customers	**7,557**	5,092
Statement of comprehensive income		
Interest income	**-**	-
Interest expenses	**60**	37

(in thousands of Canadian dollars)

20. Related party transactions and balances (continued)

c) Key management personnel

Key management personnel ("KMP") are those persons who have authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly. The definition of KMP in IAS 24, *Related Party Disclosures*, specifies a role and is not limited to a person. KMP include directors (both executive and non-executive) and other members of the management team with significant authority and responsibility for planning, directing and controlling the Bank's activities. The Bank pays no post-employment benefits to KMP.

The following table summarizes the compensation paid to the KMP during the year ended December 31:

	2019	2018
	$	$
Short-term benefits	**1,998**	1,603

In addition, during the year ended December 31, 2019 the Bank disbursed interest free personal loans to KMP in the amount of $3 (2018 - Nil). As at December 31, 2019, the loan balance outstanding from KMP is $1,979 (2018 - $2,012) at rates of interest ranging from 2.19% to 3.13% (2018 – 3.13%).

21. Geographic information

An analysis of the Bank's aggregate outstanding cash and cash equivalents, securities, loans and other assets, by geography, on the basis of the location of ultimate risk is as follows:

a) Assets

	2019	2018
	$	$
Canada	**1,048,632**	943,118
United States	**149,313**	125,298
India	**10,550**	31,183
Other countries	**2,443**	1,313
	1,210,938	1,100,912

b) Interest income:

An analysis of the total interest income on the basis of location is as follows:

	2019	2018
	$	$
Canada	**33,422**	30,748
United States	**7,549**	4,237
India	**630**	1,727
Other countries	**2**	84
	41,603	36,796

(in thousands of Canadian dollars)

22. Fair values of financial instruments

Fair value measurements of financial assets and liabilities are classified using fair value hierarchy that has the following levels:

- Level 1 - quoted prices in active markets for identical assets and liabilities;
- Level 2 - inputs other than quoted prices that are observable for the asset or liability; and
- Level 3 - inputs that are not based on observable market data.

The fair value measurements are categorized in their entirety as determined on the basis of the lowest level input that is significant to each fair value measurement.

Financial assets, consisting of securities as described in Note 4, and trading financial assets and liabilities, namely the derivatives, are all categorized as Level 2 in the fair value hierarchy.

An analysis of the classification of the Bank's financial instruments within the fair value hierarchy at December 31 is as follows:

2019	**Level 1**	**Level 2**	**Level 3**	**Total**
	$	**$**	**$**	**$**
Financial assets:				
Securities				
Financial assets at fair value through OCI	-	**66,400**	-	**66,400**
Debt securities at amortized cost	-	-	-	-
Derivatives				
Foreign exchange contracts	-	**3,954**	-	**3,954**
Interest rate contracts	-	**12**	-	**12**
	-	**70,366**	-	**70,366**
Financial liabilities				
Derivatives				
Foreign exchange contracts	-	**2**	-	**2**
Interest rate contracts		**67**	-	**67**
	-	**69**	-	**69**

2018	Level 1	Level 2	Level 3	Total
	$	$	$	$
Financial assets:				
Securities				
AFS securities	-	49,825	-	49,825
HTM securities	-	22,270	-	22,270
Derivatives				
Foreign exchange contracts	-	1	-	1
Interest rate contracts	-	76	-	76
	-	72,172	-	72,172
Financial liabilities				
Derivatives				
Foreign exchange contracts	-	1,354	-	1,354
Interest rate contracts	-	2	-	2
	-	1,356	-	1,356

(in thousands of Canadian dollars)

22. Fair values of financial instruments (continued)

The carrying values and fair values of financial instruments are as follows:

	2019			2018		
	Carrying value	**Fair value**	**Fair value over carrying value**	Carrying value	Fair value	Fair value over carrying value
	$	**$**	**$**	$	$	$
Assets						
Cash and bank balances	**61,142**	**61,142**	**-**	47,239	47,239	-
Investment securities	**66,400**	**66,400**	**-**	71,925	72,082	157
Loans and advances to customers	**1,062,620**	**1,062,301**	**(319)**	974,627	972,963	(1,664)
Other assets	**10,372**	**10,372**	**-**	7,121	7,121	-
	1,200,534	**1,200,215**	**(319)**	1,100,912	1,099,405	(1,507)
Liabilities						
Deposits from banks	**74,173**	**74,173**	**-**	53,466	53,466	-
Deposits from customers	**926,632**	**930,854**	**4,222**	858,835	860,461	1,626
Other liabilities	**33,658**	**33,732**	**74**	19,471	19,471	-
Subordinated debt	**20,000**	**20,000**	**-**	20,000	20,000	-
	1,054,463	**1,058,759**	**4,296**	951,772	953,398	1,626

Due to their short-term nature, the carrying values of certain financial instruments are assumed to approximate their fair values. These financial instruments include cash resources, other assets and other liabilities.

The estimated fair value of loans reflects changes in credit risk and general interest rates that have occurred since the loans were originated. The particular valuation methods used are as follows:

(a) For floating rate loans, fair value is assumed to be equal to book value as the interest rates on these loans automatically reprice to market.

(b) For all other loans, fair value is determined by discounting the expected future cash flows of the loans at market rates for loans with similar terms and credit risks.

The fair values of demand deposits are assumed to be equal to their carrying values. The estimated fair values of fixed rate deposits payable on a fixed date are determined by discounting the contractual cash flows using market interest rates currently offered for deposits with similar terms and risks.

The fair value of subordinated debt approximates carrying value as the interest rate automatically reprices to market.

(in thousands of Canadian dollars)

23. Commitments and contingencies

Letters of credit commitments

In the normal course of its business, the Bank issues various unfunded credit-related facilities, including letters of credit and commitments, to extend credit on behalf of its customers. These amounts, which are not included in the statement of financial position, are as follows:

	2019	2018
	$	$
Commitments to extend credit	**68,609**	93,696
	68,609	93,696

Litigation

The Bank is involved in matters involving litigation arising out of the ordinary course and conduct of its business. Management assesses such claims and where considered likely to result in a material exposure and, where the amount of the claim is quantifiable, provisions for loss are made based on management's assessment of the likely outcome. The Bank does not provide for claims that are considered unlikely to result in a significant loss, claims for which the outcome is not determinable or claims where the amount of the loss cannot be reasonably estimated. Any settlements or awards under such claims are provided for when reasonably determinable. As at December 31, 2019 and 2018, management considers that the aggregate liability resulting from such litigation and other matters is not material to the Bank’s financial position or results of operations.

24. Guarantees

As at December 31, the guarantees issued and outstanding are as follows:

	2019	2018
	$	$
Maximum potential future payment:		
Bank Guarantee	**11,819**	14,715

As many of these guarantees will expire or terminate without being drawn upon and do not take into consideration the possibility of recovery by means of recourse provisions or from collateral held or pledged, the contractual amounts are not indicative of future cash requirements or credit risk and may not bear any relationship to the Bank's expected losses from these arrangements.

(in thousands of Canadian dollars)

25. Interest rate risk and maturity profile

An analysis of the Bank's interest rate risk by the contractual repricing or maturity dates, whichever is earlier, as at December 31, 2019, is as follows:

	Floating rate	3 months or less	3months to 1 year	1 to 5 years	Over 5 years	Non-rate sensitive	Total
	$	**$**	**$**	**$**	**$**	**$**	**$**
Assets							
Cash and bank balances	30,000	14,092	-	-	-	17,050	61,142
Investment securities	-	-	45,145	16,194	-	5,061	66,400
Loans and advances to customers	76,764	519,687	58,341	410,973	-	27	1,065,792
Allowance for credit losses	-	-	-	-	-	(3,172)	(3,172)
Other assets	-	-	-	-	-	20,776	20,776
	106,764	533,779	103,486	427,167	-	39,742	1,210,938
Liabilities and Shareholder's Equity							
Deposits from banks	-	32,431	38,918	-	-	2,824	74,173
Deposits from customers	181,979	96,609	357,068	273,496	-	17,480	926,632
Other liabilities	-	-	-	-	-	33,658	33,658
Subordinated debt	-	-	20,000	-	-	-	20,000
Shareholder's equity	-	-	-	-	-	156,475	156,475
	181,979	129,040	415,986	273,496	-	210,437	1,210,938
Excess (deficiency) of assets over liabilities and shareholder's equity	(75,215)	404,739	(312,500)	153,671	-	(170,695)	-
Off-balance sheet position							
Swap assets	-	-	-	-	-	-	-
Swap liabilities	-	12,000	(5,000)	(7,000)	-	-	-
Off-balance sheet gap	-	12,000	(5,000)	(7,000)	-	-	-
Total gap	(75,215)	416,739	(317,500)	146,671	-	(170,695)	-

26. Risk management framework

As a financial intermediary, the Bank is exposed to various types of risks. The Bank has an Enterprise Risk Management ("ERM") framework, embedded in which is the Operational Risk Management ("ORM") framework, that consists of:

- A formal risk governance structure;
- Risk Policies and procedures;
- Risk appetite and limit structure;
- Risk assessment tools;
- A common taxonomy of risk terms;
- New product and initiatives process;
- Reporting of enterprise wide risks;
- Independent review and assessment of risks; and
- Training

The Bank's ERM framework ensures that effective processes are in place for:

- Identifying current and emerging risks;
- Developing risk assessment and measurement systems
- Establishing policies, practices and other control mechanisms to manage risks;
- Developing risk tolerances limits for approval by Senior Management, the Risk Management Committee of the Board ("RMCB") and the Board of Directors;
- Continual evaluation of risk appetite and tolerance, managed through setting risk limits and monitoring utilization limits;
- Identifying corrective action plans where needed; and
- Integrated reporting of enterprise risk monitoring to Senior Management, the RMCB and the Board of Directors

The guiding principles behind the risk management practices at the Bank include:

- Establishing a "strong tone at the top";
- Defining the risk appetite;
- Risk assessment and measurement, including scenario and stress consideration;
- Integrating risk management into organizational decision making at all levels and optimizing the risk-reward balance in all decision making; and
- Portfolio diversification

26. Risk management framework (continued)

The Bank has adopted the three lines of defence model for risk management. The branches, Credit Processing Cell, and other departments at Corporate Office not specifically identified as the second or third lines of defence constitute the first line of defence in the management of risks pertaining to their area of operations. The first line is responsible for the day to day risk management and control. The Chief Risk Officer and the Chief Compliance Officer are the second line of defence. The Internal Auditor is the third line of defence and provides independent assurance.

The key risks that the Bank is primarily exposed to include credit, market (including interest rate risk, foreign exchange risk and liquidity risk) and operational risk. The approach of management to handle the key risks facing the Bank is outlined below:

a) *Credit risk*

Credit risk is the risk that unexpected losses may arise as a result of the Bank's borrowers or market counterparties failing to meet their obligations to pay. The Bank's Credit Risk Management Policy (the "CRMP"), which is approved by its Board of Directors describes the principles that underlie and drive the Bank's approach to credit risk management, together with the systems and processes through which it is implemented and administered. The CRMP aims to maximize the Bank's risk-adjusted rate of return whilst maintaining the Bank's credit risk exposure within limits and parameters, as approved by the Board of Directors of the Bank.

The Bank takes a three-tier approach to assessment of credit risk - a commercial officer proposing the transaction (first tier) followed by an independent challenge by the risk department (second tier) and finally an independent credit committee (third tier) for assessment and adjudication of the same. The CRMP lays down a structured and standardized credit approval process, which includes a well-established procedure of independent and comprehensive credit risk assessment and the assignment of an internal risk rating to the borrower. The risk rating is a critical input for the credit approval process and is also an input in arriving at the credit risk spread and level of credit allowance for the proposal.

The approval process is delegated to various officials and committees as per the guidelines approved by the Board of Directors. Credit proposals are approved by these officials and committees based on, among other things, the amount and internal risk rating of the facility. There is a Corporate Credit Committee (the "CCC") which recommends all proposals that are beyond its powers for consideration of the Risk Management Committee of the Board/Board of Directors.

Monitoring credits, whilst ongoing, can also be triggered by any material credit event coming to the Bank's notice through either primary or secondary sources. All borrower accounts are reviewed at least on an annual basis.

Credit risk is also managed at the portfolio level by monitoring and reporting to the CCC and the RMCB and the Board of Directors the key parameters of risk concentration; namely, product specific exposures, large exposures, industry / sectoral exposures and country/geographical exposures.

As at December 31, 2019, the Bank’s exposure to credit risk is described in Notes 3b)(iv) and 5a) on the gross loans outstanding and in Note 22 on the fair value of financial instruments.

26. Risk management framework (continued)

b) Market risk

Market risk is the uncertainty of earnings faced by the Bank as a result of volatility in market factors (i.e., interest rates, exchange rates, asset prices, etc.). The policies approved by the Board of Directors for addressing market risk are Security and Investment Policy and Enterprise Risk Management Policy. The Asset Liability Management Committee ("ALCO") considers various investment and treasury operations matters, including the implementation of risk mitigation measures. Furthermore, an independent Treasury/Back Office is set up to monitor and report the various risk limits.

The key risks to which the Bank is exposed from a market risk perspective relate to:

i) Interest rate risk:

Interest rate risk is defined as the exposure of a bank's financial condition to adverse movements in interest rates. Earnings from interest-sensitive investments and the overall value of the investment portfolio will be impacted by changes in interest rates. The Enterprise Risk Management Policy currently sets out the measurement process to include the use of repricing gap reports and estimation of the sensitivity of the Bank's net interest income to a 200-basis-point adverse change in the level of interest rates. The adverse impact of a 200-basis-point parallel shift in interest rates shall not exceed 5% of the Bank's net capital funds as at the end of the previous year. The Bank uses interest rate contracts to manage its exposure to interest rate fluctuations as described in Note 19 and the Bank's interest rate risk is presented in Note 25.

ii) Foreign exchange risk:

The risk arises due to positions in non-Canadian dollar-denominated assets and liabilities in those currencies. The risk originates as a result of the impact on revenue due to the potential revaluation of non-Canadian dollar assets and liabilities. The aggregate net overnight open exchange position across all foreign currencies as per the Enterprise Risk Management Policy shall not exceed U.S. $6 million. The Bank uses foreign exchange contracts to manage its exposure to currency fluctuations as described in Note 20. The Bank's main exposure to foreign exchange risk, primarily US dollars, is described in Notes 4, 5, 6 and 12. As at December 31, 2019, the impact of a 10 percent change in the Canadian dollar relative to the US dollar would have a $171(December 31, 2018 - $304) impact on net income before income taxes.

iii) Liquidity risk:

Liquidity risk relates to the potential difficulty in accessing financial markets in order to meet payment obligations. It includes both the risk of unexpected increase in the cost of funding the assets and the risk of being unable to liquidate investments in a timely manner at a reasonable price. Treasury ensures that adequate liquidity is maintained at all times through systematic funds planning and maintenance of liquid investments, In addition, liquidity stress testing analysis is regularly performed to assess the Bank's ability to withstand an extreme crisis situation. The maturity profile of the Bank's financial assets and liabilities is presented in Note 25.

26. Risk management framework (continued)

Treasury is responsible for managing the market risk of treasury positions and the day- to-day liquidity of the Bank. It is subject to periodic review by Internal Audit, and is approved by the Board of Directors. Senior management also regularly monitors the positions taken on a daily basis. The ALCO and the RMCB undertake a periodic review of the market risk and liquidity position of the Bank.

c) *Operational risk:*

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems or from external events.

The Bank has developed and implemented an Operational Risk Management framework which is embedded in the Enterprise Risk Management Policy. The Operational Risk Management framework covers the aspects pertaining to minimizing losses due to process failures, losses due to fraud, impact of failures in technology/systems and continuity in the Bank's operations.

The Risk Management Committee ("RMC"), comprising senior management, is responsible for the development, implementation, maintenance and review of the Operational Risk Management framework. The Bank has implemented operational risk management tools such as Risk and Control Self Assessments, Business Process Mapping, Loss Data monitoring, etc to identify and ensure effective control of its operational risks.

To identify operational risks in new products/processes, all such proposals are examined by the Bank Management Committee, comprising senior management, after obtaining inputs from all the relevant groups and control functions in the Bank.

The Bank has developed and implemented a Business Continuity Plan ("BCP"). This plan is designed to facilitate continuity in critical business operations in the event of a disaster or an emergency situation. The BCP has been formulated on the basis of a business impact analysis carried out for the individual groups involving identification of critical activities and determination of their recovery time objectives.

The Bank has developed and implemented an Outsourcing Policy to mitigate outsourcing risks and ensure the application of a standardized approach for all outsourcing arrangements entered into by the Bank. All proposed outsourcing arrangements are assessed for their criticality prior to outsourcing, and the proposal is approved by the Board of Directors.

Group risk management framework:

The Bank is subject to the group risk management framework, which has been developed by the parent bank, in order to identify, evaluate and manage key risks on a group-wide basis. The framework is applicable to all overseas bank entities, including the subsidiaries, of the parent.

27. Subsequent Event

At its meeting on March 26, 2020, the Board of Directors approved a dividend of $373 to its parent bank.