中国建设银行(伦敦)有限公司
China Construction Bank (London) Limited

Pillar 3 Disclosures Report
For Financial Year Ended 31st December 2015

1. Overview

1.1. Background

China Construction Bank (London) Limited ('CCBL' or 'the Bank') is a wholly owned subsidiary of China Construction Bank Corporation ('CCBC', domiciled in Beijing, China) It has been authorised and regulated by the Financial Conduct Authority (FCA) since 9 March 2009. It has a passport to operate within the 30 countries of the EEA/EU.

The Bank concentrates on wholesale banking activities - accepting deposits, providing trade finance and lending, foreign exchange, interest rate and foreign exchange derivatives, and bond investments. The Bank's treasury activity performs a liquidity management function, including the management of a portfolio of investments to assist with liquidity. It also provides a service to CCBC to trade foreign exchange and gold on an agency basis. CCBL is not exposed to any market risk on this activity so it does not consume any capital. Syndicated loans are provided for general funding requirements to banks and corporate entities. Bilateral and direct loans to customers are to support working capital financing, capital expenditure and trading activities. In April 2012 the Bank set up a department to provide a marketing service for the investment banking services offered by China Construction Bank International Ltd. CCBL is not exposed to any market or credit risk for this activity.

The European Union Capital Requirements Directive ('CRD') came into effect on 1 January 2007. It introduced consistent capital adequacy standards and an associated supervisory framework in the EU based on the Basel II framework. Implementation of the Directive in the UK was by way of rules introduced by the Financial Conduct Authority ('the FCA')[1] and the Prudential Regulation Authority ("PRA").

Since its authorisation as a licensed financial institution, CCBL has adopted the Standardised Approach for credit, the Standard approach to market risk and the Basic Indicator Approach for operational risk under the Capital Requirements Directive and Capital Requirements Regulation.

On 9 May 2012 the Bank set up a subsidiary Public Limited Company, CCBL Funding PLC, to facilitate the issuance of bonds to fund the activities of the Bank. The financial statements of CCBL Funding PLC are consolidated with those of the Bank to form China Construction Bank (London) Limited (the "Bank"). CCBL Funding PLC is engaged in no activities other than providing funding to the Bank.

During the year, CCBL offered Renminbi clearing services to both CCBC Group and non-CCBC Group Participating Banks. A Sterling clearing service was also provided to CCBC Group clients. From a date in 2016, yet to be determined, these activities will be undertaken by the London Branch.

1.2. Purpose

The purpose of this Pillar 3 disclosures report is to detail the implementation by the Bank of the Basel III framework and risk assessment processes in accordance with the Pillar 3 requirements and the UK interpretation of EU regulations under CRDIV and CRR

Pillar 3 complements the minimum capital requirement ('Pillar 1') and the supervisory review process ('Pillar 2').

1.3. Review

These disclosures have been approved by the Board, but have not been subject to external audit although the underlying positions they are based on have been. The Board, having taken into account the size and complexity of the Bank's operations, believe that an unaudited annual

[1] FCA Handbook – General Prudential sourcebook ("GENPRU") and Prudential Sourcebook for Banks, Building Societies and Investment Firms ("BIPRU").

disclosure is appropriate. Future reviews will be published as soon as practicable after publishing the annual financial statements. More frequent disclosures may be made where considered necessary.

CCBL's accounting year end is 31st December and CCBL's Pillar 3 disclosures have been aligned with its financial reporting. The Pillar 3 disclosures for previous years are available on the Bank's website: www.uk.ccb.com.

The Pillar 3 disclosures together with the Annual Report and Accounts are the main documents in which the Bank makes its public disclosures and the Board approves both of these documents.

2. Risk Management Objectives and Policies

2.1 Strategies and Processes to Manage Risks

The principal risks faced by CCBL are credit risk, liquidity risk, market risk and operational risk. These principal risks are reviewed and reassessed at least annually as a part of the Internal Capital Adequacy Assessment Process ('ICAAP') and the Internal Liquidity Adequacy Assessment Process ('ILAA'). The ICAAP and ILAA analyse capital and liquidity with reference to severe stressed scenarios in order to assess their adequacy.

The Board has adopted a "Three Lines of Defence" model. The first line of defence consists of the business staff that are responsible for adhering to agreed business mandates as well as firm wide policies. The second line of defence is the oversight provided by control functions such as Risk and Compliance who set and monitor adherence to policies and define work practices. The third line of defence is the independent internal audit and risk process overseen by the Board Audit & Risk Committee which has oversight of and undertakes reviews of the overall risk management and compliance practices within CCBL. The Audit and Risk Committee meets quarterly, and more frequently if necessary.

CCBL's risk management is built on a formal governance framework and a process of ongoing identification, measurement and monitoring of risk. It relies on individual responsibility and collective oversight. Ultimate responsibility for risk governance lies with the Board of Directors who is responsible for determining risk strategy and setting risk appetite.

The risk appetite of CCBL reflects the level of risks it is willing to take with its economic capital to achieve its organisational objectives, business plans, and stakeholder expectations. This is accomplished by utilising the skills, resources and technology available to it and is inclusive of defined tolerances for loss or negative events that can be reasonably quantified.

The risk appetite objectives of CCBL may be summarised as follows:

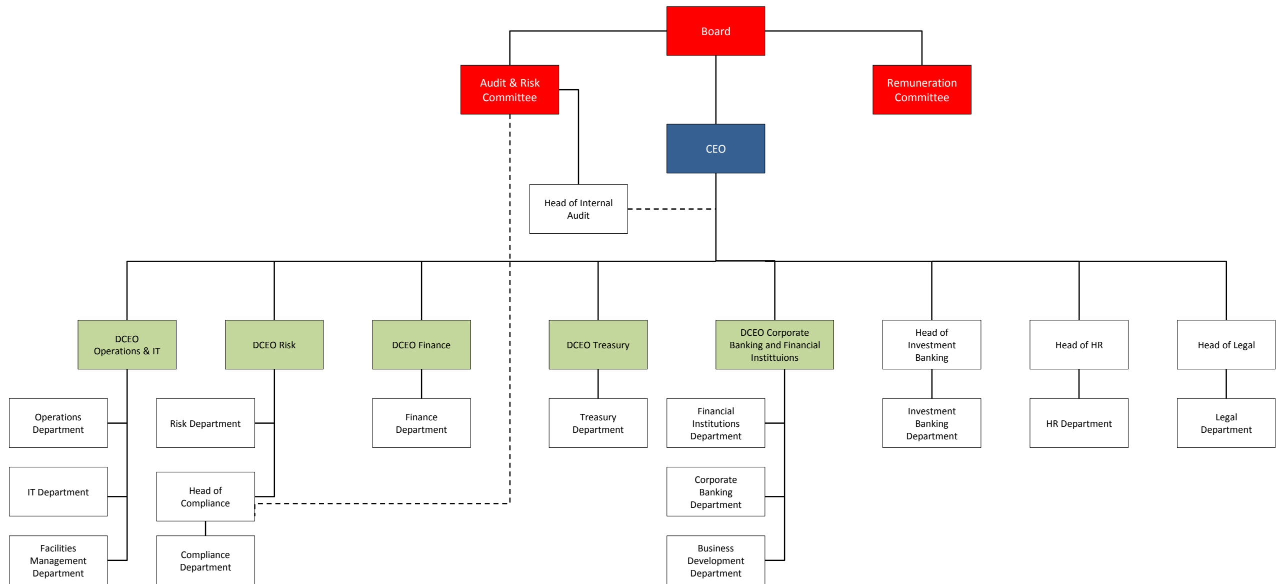
- To protect the ongoing franchise of the business;
- To minimise risks (credit, market, liquidity, operational, legal, reputational) through a thorough understanding of potential counterparties' business;
- To optimise risk and return through appropriate pricing;
- To ensure regulatory and legal compliance.

2.2 Risk Department

The Risk Department is responsible for:

i. Developing and reviewing credit, market and operational risk policies and procedures;
ii. Monitoring and reporting market, credit and operational risk;
iii. Supporting the Credit Committee, Risk and Compliance Committee, Asset and Liability Committee and Executive Committee, the Board Audit and Risk Committee and the Board Remuneration Committee with respect to risk; and
iv. Reviewing and commenting on credit and market risk proposals.

2.3 Structure and Organisation of Governance



2.3.1 The Board

The Board is responsible for strategic direction and overall control of the Bank. The Board is responsible for establishing a clearly defined governance and risk management structure, as well as monitoring and assessing overall effectiveness of these. The Board also considers Branch business as it has responsibility for staffing. The Board has created a risk framework within the Bank's strategic objectives in accordance with CCB Group delegated authorities and UK compliance and legal authorities and has delegated risk approval powers to the Bank's CEO within that framework. The CEO can further delegate these powers and responsibilities as he sees fit. The Board is responsible for providing effective oversight of senior management. The nature of each Director's directorship is kept under review through a process of directorship declarations received at least annually. Board member continuing professional development is co-ordinated by the Chairman.

2.3.2 Board Audit & Risk Committee

The Audit & Risk Committee monitors the integrity of the financial statements of the Bank, monitors the Bank's accounting and financial reporting systems, provides oversight of the Bank's internal and external auditors and risk and compliance functions, thereby assisting the Board in providing an independent review of the effectiveness of processes and internal control systems of the Bank. It is advised of decisions about the product range as described above. Such reviews will be reported to the full CCBL Board, and in appropriate circumstances will be discussed by the Board for final approval. The committee also informs the Board of any suspected abnormality which comes to its attention.

2.3.3 Board Remuneration Committee

The Remuneration Committee agrees the performance management and reward practices of CCBL within Group policy guidelines and those of the FCA/PRA. CCBL reward policies are set with continual recognition of the signals they give staff on the management of current and potential future risk. The Committee agrees appropriate levels of staff remuneration including bonus payments with particular focus on Code staff. Where a non-Group Directors vacancy is identified, the Remuneration Committee will be involved in the recruitment process to ensure that any role definition is appropriate and any appointed individual has the skills, experience and knowledge to undertake the defined role.

2.3.4 Executive Committee (ExCo)

The risk-related responsibilities of the ExCo include monitoring the risk profile of the Bank, and regulatory and legal developments. Major proposed changes to risk powers, policies and the product range are approved by ExCo before submission to the Board Audit and Risk Committee for final approval.

Diversity: The Bank is committed to creating a diverse and inclusive workplace. It arranges annual diversity training and works with recruitment agencies that are committed to diversity.

The Compliance Department ensures the adherence to compulsory compliance training.

2.3.5 Risk and Compliance Committee

The Risk and Compliance Committee has delegated responsibility from the CEO to ensure effective executive day to day oversight of the risk management and compliance framework of CCBL. The Risk and Compliance Committee reports its findings to ExCo. Responsibilities include implementation of risk management policies, reviewing appropriateness of risk management framework and oversight of the implementation of the framework by the First and Second Line functions. This committee also focuses on monitoring and managing individual exposures and assessing the exposures in the credit portfolio.

2.3.6 Credit Committee

The Credit Committee has been delegated authority by the CEO to approve and oversee credit risks within the terms of the Parent Company Delegation of Authority and CCBL Board Authority. It monitors the Bank’s credit risk profile, industry risk, concentration risk and operates an “early alert” procedure to detect any potential weakening of counterparty exposures. It regularly reviews the quality of the credits in the credit portfolio and the adequacy of provisions.

2.3.7 Asset and Liability Committee (ALCo)

The ALCo is granted authority, within the terms of the Parent Company Delegation of Authority and CCBL Board Authority, by the CEO, to review and monitor the Bank’s liquidity and balance sheet structure. The ALCo establishes various trigger limits, control ratios and guidelines in accordance with statutory and local regulatory requirements. ALCo reports to EXCO and the CEO.

3. Capital Resources

a) Capital

The Company's authorised share capital was US$200,000,000 divided into 200,000,000 shares of US$1 and a new class of shares denominated in Renminbi of 1,500,000,000 ordinary share of RM1 each was, authorised, allotted and fully paid by China Construction Bank Corporation on 6th December 2013.

At 31 December 2015 the issued and fully paid up share capital amounted to $446,599,000.

(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.

(USD000s)

	As at 31/12/2015	As at 31/12/2014
Core tier 1 Capital		
Called up share capital	446,599	446,599
Share premium account		-
Retained earnings and other reserves	35,492	24,288
Externally verified profits		
Preference shares		
Perpetual non-cumulative preference shares	-	-
Deductions from tier 1 capital		
Intangible assets	(223)	(407)
Net losses on securities held in the available for sale financial assets category	439	360
Tier 1 capital after deductions	482,307	470,840
Innovative tier 1 instruments	-	-
Tier 2 capital		
Subordinated debt	-	-
Collective provisions	-	-
Deductions from tier 2 capital		
Expected losses	-	-
Tier 2 capital after deductions	-	-
Deductions from total of tier 1 and tier 2 capital	-	-
Total capital resources	482,307	470,840

4. Credit and Counterparty Risk

CCBL identifies five types of credit risk in its business:

- *Default risk*: the risk that an individual counterparty, borrower or issuer defaults on its contractual obligations to CCBL;
- *Group risk*: the risk that one or more members of the CCBC Group defaults on their contractual obligations to CCBL;
- *Settlement risk*: exposure to a counterparty resulting from the failure to settle transactions due to the default of that counterparty;
- *Concentration risk*: the risk of credit losses being larger as a result of large exposures to individual counterparties/borrowers/issuers or to a number of them in the same group or business sector; and
- *Country Risk:* the risk of large exposures to individual counterparties/borrowers/issuers or to a number of them in, or materially exposed to, the same country.

Credit risk arises across CCBL's businesses, from corporate lending, through FX and interest rate derivative transactions, to balances held in nostro accounts and overdrafts in vostro accounts offered to clearing clients. There is no credit exposure to individuals.

Oversight of the credit risk framework is performed by the Credit Committee which approves all credit limits, including country and sector limits within the delegated authority set by the Board.

'Counterparty' refers to any party on whom CCBL takes credit risk.

4.1 Credit risk minimum capital requirement

Basel III provides three approaches of increasing sophistication to the calculation of Pillar 1 credit risk capital requirements. The most basic, the "standardised" approach, requires banks to use external credit ratings to determine the risk weightings applied to rated counterparties, to group other counterparties into broad categories and to apply standardised risk weightings to these categories.

The next level, the internal ratings-based ('IRB') foundation approach, allows banks to calculate their credit risk capital requirements on the basis of their internal assessment of the probability that a counterparty will default, but subjects their quantified estimates of exposure at default and loss given default to standard supervisory parameters. Finally, the IRB advanced approach allows banks to use their own internal assessment in both determining probability of default and quantifying exposure at default and loss given default.

CCBL has adopted the standardised approach for calculating credit risk capital requirements. Under the standardised approach, the amount of capital set aside for each transaction is given by the following equation: Credit Risk Requirement = 8% x Risk Weighted Assets.

The following table shows exposure values associated with each credit quality step for credit exposures in accordance with the PRA's credit quality assessment scale under the Standardised Approach as at 31/12/2015.

	External Credit Risk	Credit Quality Step	Risk Weight	Exposure 31/12/2015	Exposure 31/12/2014
				$000	$000
Central governments or central banks	AAA to AA-	1	0%	963,368	2,111,939
			50%	32,216	-
Institutions with residual maturity less than 3 months	AAA to AA-	1	50%	27,794	32,789
	A+ to A-	2	100%	145,645	1,887,213
		2	50%	30,962	-
		2	20%	636,846	-
	BBB+ to BBB-	3	100%	-	7,863
Institutions with residual maturity greater than 3 months	A to A-	2	100%	-	660,131
	BBB+ to BBB-	3	100%	-	145,579
Corporates	A+ to A-	2	100%	152,315	1,270,980
	BBB+ to BBB-	3	100%	149,901	176,859
	BB+ to BB- and Unrated	4	100%	182,801	146,179
	B+ to B-	5		-	4,423
Other				558,827	364,539
Total Exposure				**2,880,675**	**6,808,493**

The following tables show the credit exposures as at 31/12/2015 by geography, industry sector and residual maturity of the exposure.

Geographic distribution by Exposure		31-Dec-15 $000	31-Dec-14 $000
Peoples Republic of China	Institutions	466,703	2,223,792
	Corporates	144,165	1,283,709
	PSE	60,989	-
	Central governments or central banks	6,016	39,637
Australia	Institutions	-	4
	Corporates	25,001	25,001
Europe	Multilateral development banks	-	-
	Institutions	15,590	159,059
	Corporates	160,460	144,560
Bermuda	Corporates		32,173
UK	Institutions	169,766	114,190
	Corporates	54,604	112,998
	Other	558,827	364,540
USA	Central governments or central banks	957,353	2,072,301
	Institutions	65,598	98,040
	Corporates	39,798	-
Canada	Institutions	-	9,966
	Corporates	-	-
Switzerland	Institutions	5	-
Russia	Institutions	-	-
Japan	Institutions	16	-
Canada	Institutions	9,976	-
Russia	Institutions	145,645	-
Hong Kong	Institutions	164	-
Dubai	Institutions	-	15,973
Singapore	Institutions	-	112,550
		2,880,675	**6,808,493**

Industrial Sector Distribution by Exposure		31-Dec-15	31-Dec-14
		$000	$000
Central governments or central banks	Liquidity buffer-eligible investments	963,368	2,111,939
Institutions	Banking	841,247	2,733,575
	Liquidity buffer-eligible investments	32,216	-
Corporates	Financial Services	41,768	50,022
	Construction	62,397	124,120
	Manufacturing	111,815	848,799
	Mining	25,001	97,454
	Electricity	7,619	8,524
	Water Supply	-	19,473
	Retail Trade	150,825	321,580
	Transport and Storage	-	98,405
	Real Estate activities	24,603	30,064
PSE	Transport and Storage	60,989	-
Other Items		558,827	364,538
		2,880,675	6,808,493

Residual maturity of Exposure		31-Dec-15	31-Dec-14
		$000	$000
3 months	Corporates	212,762	504,462
	Institutions	841,247	1,329,052
	Central governments or central banks	-	-
Between 3 months & 1 year	Corporates	135,919	763,556
	Institutions	-	1,376,541
	Central governments or central banks	957,353	1,104,968
Between 1 year and 3 years	Corporates	56,336	221,298
	Institutions	-	28,072
	Central governments or central banks	38,231	1,006,971
Between 3 years and 5 years	Corporates	80,000	109,125
Undated	Other	558,827	364,538
		2,880,675	**6,808,493**

4.2 External Credit Assessment Institutions (ECAI)

The following ECAI's have been nominated to calculate credit risk capital requirements for all exposure classes and are recognised under the Capital Requirements Regulations 2006 for purposes of the standardised approach:

- Standard and Poor's;
- Moody's Investor Service; and
- Fitch.

Where multiple ECAIs provide credit ratings, the worst rating of the best two ratings is applied. Where available, the long term senior unsecured rating is applied except where subordinated ratings are used. The issue rating is used for bonds and the issuer rating is used in other instances.

4.3 Monitoring Credit and Counterparty Risk

The following are monitored on a daily basis:

- Counterparty credit exposures and limits;
- Concentration risk (currency, industry and issuer); and
- Country risk exposures.

4.4 Mitigating Credit Risk

CCBL manages its credit risks by:

- Avoiding concentrations of risk by limiting exposures to individual counterparties/borrowers and groups, and diversifying exposure across different counterparties;
- Limiting exposures to individual countries and industry sectors, and diversifying exposure across different countries and sectors;
- Ensuring robust initial and ongoing credit analysis of counterparties, groups and countries by both the First and Second Line of Defence, including setting, and regularly reviewing, internal ratings;
- Settling transactions through assured payment systems or on a delivery-versus-payment basis;
- Setting limits on tenors of transactions with counterparties;
- Ensuring robust documentation of transactions and, where possible, utilising netting, collateral or security agreements, setting appropriate covenants or obtaining CCBC Group or third party guarantees to reduce the risk of loss;
- Monitoring the quality/value of collateral or security taken; and
- Maintaining clear credit policies and procedures.

5. Counterparty Credit Risk for Derivative Transactions

Counterparty credit risk ("CCR") is the risk that the counterparty to a derivative transaction could default before the final settlement of the transaction's cash flows.

The Bank measures the exposure value on counterparty credit exposures under the CCR mark to market method. This exposure value is derived by adding the gross positive fair value of the contract (replacement cost) to the contracts potential future credit exposure, which is derived by applying a multiple based on the contracts residual maturity to the notional value of the contract in accordance with BIPRU 13.4.5 .

Table of Potential Future Credit Exposure Percentages in accordance with BIPRU 13.4.5					
Residual maturity	Interest-rate contracts	Contracts concerning foreign currency rates and gold	Contracts concerning equities	Contracts concerning precious metals except gold	Contracts concerning commodities other than precious metals
One year or less	0%	1%	6%	7%	10%
Over one year, not exceeding five years	0.5%	5%	8%	7%	12%
Over five years	1.5%	7.5%	10%	8%	15%

The following table shows the counterparty risk and its relevant capital components as at 31/12/2015 and 31/12/2014

	31 December 2015 ($000's)		31 December 2014 ($000's)	
	Gross positive fair value	Counterparty Risk Capital Component	Gross positive fair value	Counterparty Risk Capital Component
Forward Foreign Exchange contracts	319,856	10,939	138,978	3,274
Interest rate swaps	-	-	-	-
	319,856	10,939	138,978	3,274

6. Market Risk

CCBL identifies four key types of market risk in its business:

- *FX risk*: risk arising from movements in exchange rates across various currencies;
- *Interest rate risk:* risk arising from movements in interest rates and in the basis between interest rates across various currencies;
- *Funding spread risk*: risk arising from movements in CCBL's cost of funding over market benchmark rates.

CCBL is exposed to market risk as a result of transacting customer orders in treasury FX and interest rate products, mismatches between interest rates and tenors on corporate banking and money-market lending assets and their funding, including bond holdings and repo transactions as well as from operational requirements.

Oversight of the market risk management framework is performed by the Risk & Compliance Committee, which approves all market risk limits within the delegated authority set by the Board.

6.1 Interest Rate Risk

Interest rate risk arises principally from mismatches between the future yields on assets and their funding costs, as a result of interest rate changes. Interest rate risk in the non-trading book arises from financial investments designated as available for sale and held to maturity.

The table below shows the impact of a 100 basis point rise or fall in the base rate on net interest income at 31 December 2015:

	31-Dec-15		31-Dec-14	
	100bps parallel Increase **$000's**	100bps parallel Decrease **$000's**	100bps parallel Increase **$000**	100bps parallel Decrease **$000**
Sensitivity of projected net interest income				
USD	(4,304)	4,304	(4,043)	4,043
GBP	139	(139)	(105)	105
CNY	(1,387)	1,387	(4,494)	4,494
EUR	(159)	159	(52)	52
	(5,711)	5,711	(8,694)	8,694

Related to the Bank's capital base, therefore, interest rate risk is minimal.

6.2 Foreign Exchange Risk

The Bank makes loans and takes deposits in a number of currencies. The table below shows the impact of a one cent increase or decrease in the value of the Dollar against other currencies to which the Bank is exposed:

	31 December 2015		31 December 2014	
Change in value of the dollar compared with Sterling, Euros and Renminbi	1 cent Increase	1 cent Decrease	1 cent Increase	1 cent Decrease
$000				
Sensitivity of foreign exchange At 31 December 2015/2014	(2,555)	2,555	(2,342)	2,342

The Bank has an exposure to Foreign Exchange risk with respect to the Renminbi portion of its capital base (RMB1.5bn ($247m). This is monitored on a daily basis with any losses taken to the profit & loss account.

CCBL has approved a Trading Book Policy Statement. As at 31st December 2015, FX Trading is the only permitted trading activity.

6.3 Monitoring Market Risk

The following are monitored on a daily basis:

- Mark-to-market profit and loss;
- Value at Risk (calculated on a one day horizon with a 99% confidence interval);
- Sensitivity to adverse moves in interest rates, foreign exchange rates and funding rates.

6.4 Mitigating Market Risk

CCBL manages its market risk by:

- Concentrating responsibility for managing all market risks in Treasury Department;
- Matching as closely as possible the interest rate terms on corporate banking and money-market lending assets with their funding;
- Matching transactions with clients as closely as possible with offsetting transactions;
- Using hedging instruments such as FX and interest rate derivatives to reduce net sensitivity to market risk factors;
- Setting limits on notional positions and on sensitivities to individual market risk factors e.g. DV01 limits; FX exposure limits;
- Setting maturity and gap mismatch limits;
- Setting limits on portfolio risk measures such as value-at-risk and stress tests;
- Monitoring the results of regular stress tests;
- Ongoing assessment of market conditions; and
- Maintaining clear market risk policies and procedures.

7. Liquidity Risk

CCBL identifies five material sources of liquidity risk in its business:

- *Non-marketable assets*: holding assets that are not easily marketable and funding these assets with funding of a shorter tenor;
- *Reliance on CCBC Group funding sources*: concentration of sources of funding on other CCBC Group companies, exposing CCBL to the liquidity risk of the wider CCBC Group;
- *Intra-day liquidity risk*: differences in the timing of cash inflows and outflows during the day, or disruptions to incoming payments, leading to large intra-day funding requirements;
- *Off-balance sheet liquidity risk*: market movements leading to large collateral calls under collateral arrangements; draw-downs on committed facilities;
- *Marketable assets risk*: holding assets that are considered to be liquid but may not be liquid when required in the amounts expected or as quickly as expected.

CCBL is exposed to liquidity risk as a result of mismatches between expected cash inflows from corporate banking transactions and money-market lending, and the expected cash outflows on funding, and from unexpected drawdowns of committed facilities, holdings of marketable assets which may not be liquidated quickly enough to meet cash outflows on their funding, intra-day liquidity requirements from clearing activities and collateral calls on treasury FX and interest rate transactions which may not be matched by the ability to call collateral on the other side of the trade.

Oversight of the liquidity risk management arrangements is performed by Asset & Liability Committee, which approves all liquidity risk metrics within the delegated authority set by the Board.

7.1 Monitoring Liquidity Risk

The following are monitored on a daily basis:

- Wholesale Survival Days;
- Net Stable Funding Ratio;
- Surplus Liquidity Buffer over regulatory requirement;
- Mix of sources of funding.

7.2 Mitigating Liquidity Risk

CCBL manages its liquidity risk by:

- Managing mismatches between expected cash inflows on non-marketable assets and the expected cash outflows on their funding within limits set on liquidity risk metrics;
- Agreeing direct funding support from other CCBC Group companies, including committed overdraft facilities with certain CCBC Group companies;
- Entering agreements to allow CCBL to extend the tenor of deposits from CCBC Group by up to 3 months if required;
- Maintaining a portfolio of unencumbered marketable assets which can be liquidated to provide same-day or next-day funds in CCBL's main currencies;
- Maintaining a Contingency Funding Plan, reviewed regularly by the Asset & Liability Committee, laying out management actions and roles and responsibilities in the event of CCBL facing a liquidity issue;
- Monitoring CCBL's liquidity situation and assessing liquidity conditions in its funding markets, and escalating any adverse developments; and
- Maintaining clear liquidity risk management policies and procedures.

8. Operational Risk

CCBL defines operational risk as the risk of an economic loss, a disruption to business, an adverse impact on reputation or on client relationships or of legal action arising from inadequate or failed internal processes, people and systems, or from external events. This includes legal risk but excludes strategic or reputational risk. Within this broad classification, CCBL identifies a number of categories of operational risk in its business:

- *Fraud risks*: losses resulting from fraudulent activity or transactions, carried out either internally or externally;
- *Systems risks*: failure of computer or communication systems, risk of unauthorised access to systems; cybercrime;
- *Data risks*: corruption or loss of data, incorrect data entry, failure to protect data adequately, including client data, and misusing client information;
- *Processing risks*: errors in executing trades or client orders; errors in processing payments or settlements
- *Collateral risks*: failure to call collateral in a timely way, failure to value collateral correctly;
- *Booking risks*: failure to book transactions or the details of products fully or accurately;
- *Tax risks*: failure to structure transactions or arrange business to ensure appropriate tax treatment, changes to tax rules leading to additional tax charges, failure to determine tax liabilities correctly; structuring of transactions in a way which may lead to an accusation of facilitating tax avoidance or evasion;
- *Legal risks*: risk of transactions not proceeding as expected due to documentation issues or issues with enforceability/interpretation in the relevant legal jurisdiction;
- *Client risks*: failure to carry out KYC checks adequately, failure to meet FATCA requirements adequately; failure to manage bribery & corruption risks adequately;
- *Compliance risks*: failure to meet UK or Chinese legal or regulatory requirements applicable to CCBL's activities; failure to arrange for adequate training to ensure awareness amongst staff of the laws and regulations applying to the Bank's activities; impact of change in regulatory rules;
- *Valuation risks*: incorrect valuation of transactions in financials accounts due to inaccurate market data;
- *Accounting risks*: incorrect financial statements due to inappropriate accounting treatment or inadequate disclosure;
- *Model risks*: incorrect valuation of transactions in financials accounts due to inaccurate valuation models, incorrect reporting of risks due to inaccurate risk models; incorrect regulatory capital or liquidity reporting due to incorrect regulatory models;
- *Project risks*: risks from poor implementation of material projects, new products, system changes;
- *Outsourcing risks*: loss of expertise; performance of the supplier; compliance of the supplier to regulatory or legal requirements;
- *Health & Safety risks*: employee and visitor safety, inability to access offices; and
- *Staff risks*: key man risk, lack of succession planning, remuneration risk and staff knowledge and competency.

Operational risk arises in all of CCBL's business and corporate activities. It is CCBL's policy to mitigate as far as possible operational risks, though management recognises that some operational risks cannot be fully eliminated. Where operational risks cannot be effectively mitigated, CCBL manages its business to keep losses from operational risks within the agreed level of risk appetite through controls on, for example, volumes or keeping business strictly back-to-back.

Oversight of the operational risk management framework is performed by the Risk & Compliance Committee.

8.1 Mitigating Operational Risk

CCBL manages its operational risk by each business unit and supporting function:

- Carrying out a Risk Control Self-Assessment to identify, document and quantify the operational risks arising in their activities;
- Identifying actions to mitigate those operational risks and enact policies and procedures to implement those actions;
- Communicating these risks and mitigating actions to Risk Management Department and senior management;
- Identifying operational risk events occurring in their area and reporting these to Risk Management Department and senior management, and, where appropriate, identifying and implementing actions to remedy any control failures;
- Maintaining detailed departmental procedures and operational manuals, including the maintenance of end-to-end process maps, defining and documenting, for all products, the business processes and controls; and
- Maintaining clear operational risk management policies and procedures.

Operational risk losses in 2015 were $17,000 (2014: $80,302).

9. Capital adequacy

In assessing the adequacy of its capital, the Bank considers its risk appetite, the risk types to which the Bank is exposed and the appropriate management strategies for each of the Bank's material risks. In addition to capital adequacy quarterly reporting to the FCA, an internal capital adequacy assessment is performed daily in order to assess the Bank's capital adequacy and to determine the levels of capital required going forward to support the current and future risks of the Bank's growing business. Capital adequacy reports are produced by the Finance Department and reviewed, monthly, by ALCo and Senior Management. If the daily surplus capital falls within a predetermined, (currently 20%) of the Individual Capital Guidance ('ICG' – a prudential measure specific to each financial institution set by the PRA), ALCo is notified immediately. ALCo will then monitor the situation closely and make any necessary recommendations to ExCo who will decide what actions are required to rectify the situation.

The Risk department is responsible for ensuring that the Bank's current and expected future risks are reflected in the Internal Capital Adequacy Assessment Process (ICAAP) document which is approved, at least, annually by the Board. The Finance and Risk departments are jointly responsible for ensuring that sufficient capital is maintained to provide the Bank with adequate headroom to cover expected risks of current and potential business activities and stress testing scenarios.

The amount and composition of the Bank's capital requirements is determined by assessing the minimum capital requirements under Pillar 1 of the Capital Requirements Directive (CRD), the applicable approach for risk assessment being the Standardised Approach for credit risks and the Basic Indicator Approach for operational risk and the ICG of the Bank.

CCBL's assessment of its credit risks versus capital resources is set out in the latest version of its Internal Capital Adequacy Assessment Process (ICAAP).

The following table shows the Bank's Pillar 1 capital requirement by asset class:

Credit Risk - Standardised Approach	31 December 2015		31 December 2014	
(USD000s)	Exposure Value	Capital Requirement	Exposure Value	Capital Requirement
Central governments or Central Banks	963,368	-	2,111,939	-
Multilateral Development Banks	-	-	-	-
Institutions	873,463	18,935	2,733,575	36,918
Corporates	424,028	28,600	1,598,441	103,892
PSE	60,989	4,879	-	-
Short term claims on institutions and corporates	5,109	409	2,298	184
Other items	553,718	18,627	362,241	17,861
Capital Component for Credit Risk	2,880,675	71,450	6,808,494	156,855
Operational risk – Basic Indicator Approach		6,791		5,697
Counterparty Risk Capital Component		10,939		3,274
Foreign exchange PRR		21,112		18,743
Interest PRR		2,453		3,882
Credit Valuation Adjustment		4,977		
Concentration Risk		20,209		
Total Pillar 1 capital requirement		137,931		188,451
Total capital resources		482,307		471,247
Excess capital resources over Pillar1 capital requirement		**344,376**		**282,796**

10. Impairments and Provisions

In the first instance, the Relationship Manager is responsible for monitoring loan covenants and identifying overdue or non-performing loans for his/her customers. The Risk Department is responsible for classifying the loans and notifying the appropriate committees and Head Office. The committees recommend courses of action following the *Early Alert* Process which is discussed below.

10.1 Definition of Impaired

CCBL recognises impairment if objective evidence of a risk problem exists as a result of one or more events that occur after the initial recognition of the asset and those events have an impact on the estimated future cash flows of the financial asset that can be reliably estimated. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the holder of the asset as a result of the following events:

- Significant financial difficulty of the issuer or obligor;
- A breach of contract, such as default or delinquency in interest or principal payments;
- The lender, for economic or legal reasons relating to the borrower's financial difficulty, grants the borrower a concession to weaken the original terms of the transaction;
- Weakening of security taken against a counterparty transaction;
- It becoming probable that the borrower will enter bankruptcy or financial reorganization;
- The disappearance of an active market for the financial asset because of financial difficulties; or
- A measurable decrease in the estimated future cash flows because of observable data including:
  a. adverse changes in the payments status of borrowers; or
  b. national or local economic conditions.

10.2 Definition of Past Due

Past due refers to amounts that are unsettled on the scheduled or expected date and refers to all payment types including principal, interest and fee payments and failed collateral calls.

10.3 Impairment Reporting

The Risk Department prepares a monthly loan impairment report for Head Office. This report consolidates all loan accounts with details such as loan nature, loan grading, company class, country risk, final maturity date and security. This report also provides an analysis on the exposure to each industry and the exposure distribution to each company class, loan grading, nature of loan facilities, country risk, final maturity and security.

10.4 Provisioning Process

An account is considered non-performing (or non-accrual) if:

- There is a question as to the obligor's ability or willingness to pay interest or principal. The Risk Department, or a member of the Credit Committee can recommend that an account be placed on non-performing status to the Credit Committee;
- Principal and / or interest remains unpaid for ninety days after its due date or more; or
- The account is classified Substandard or Doubtful or Loss through the Account Classification Process (see definitions below).

The Bank's Credit Policy details the valuation process for impairments.

The amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses) discounted at the original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount shall be reduced either directly or through use of an allowance account and the loss shall be recognised in profit or loss.

When a decline in the fair value of an available-for-sale financial asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity shall be removed from equity and recognised in profit or loss.

Any accrued and unpaid interest/commission on a non-performing exposure is not recognized as income.

Once an account is put on non-performing status, it is classified at Substandard or lower (see definitions below). It can be restored to performing status only after all outstanding payments of principal and interest have been received in cash or a suitable restructuring/rescheduling agreement has been signed and the obligor has fulfilled all its obligations under the revised agreement. This is accompanied by evidence of a relative improvement in the Obligor's condition and debt service capacity and clear commitment to repay. An important factor is a reasonable period of demonstrated payment performance in accordance with the modified terms.

Under the Asset Classification process, the Relationship Managers and Risk Department, have the ongoing responsibility to identify signs of weakness or other signs of deterioration in each credit. The recommendations are presented to the Credit Committee.

The Asset Classification Process may lead to placing the account on any of the following statuses:

- Pass
- Special-mention;
- Substandard;
- Doubtful; or
- Loss

Pass: assets showing no sign of weakness or quality deterioration

Special-mention: assets subject to conditions that, if left uncorrected, could raise concerns about full repayment are to be classified "Special-mention". Examples of such conditions are weaknesses in the customer's financial condition or deterioration in the security or weaknesses that have been detected in the documentation. These require more than normal attention by the client relationship managers.

Substandard: assets that do not have adequate protection (e.g. obligor net worth or collateral) and/or interest or principal or both are more than 90 days overdue. No loss is foreseen, but a protracted workout is a possibility. Prompt corrective action is required to strengthen the Bank's position as a creditor, to reduce its exposure and to ensure that the customer takes adequate remedial measures. All non-performing accounts are classified as Substandard at best.

Doubtful: assets for which collection / liquidation in full is determined by the Bank's management to be improbable due to current conditions and/or interest or principal or both are overdue more than 180 days. Assets in this category are considered impaired but are not yet considered total losses because some pending factors may strengthen the asset's quality (e.g. merger, new financing or capital injection). Placing the account on non-accrual is normally required. The principal should be reserved or written off to the extent deemed necessary, after obtaining the approval of the Credit Committee.

Loss: an asset is classified Loss when management considers the facility to be virtually not collectible and/or when loans may have some recovery value but it is neither practical nor desirable to defer write off. A Loss classification does not mean that there is no potential for eventual recovery. The client relationship manager is expected to continue a vigorous collection effort until it is decided that no further repayment or recovery is possible.

11.Remuneration

11.1 Overview

The terms of the Prudential Regulatory Authority (PRA) guidance on remuneration apply to all aspects of remuneration which could have a bearing on effective risk management in the Bank including salary, long-term incentive plans, pensions and severance arrangements. The Bank's reward structure reflects the requirements of the PRA and addresses these issues in a manner tailored to the needs of the business. The remuneration disclosures are presented as required by BIPRU 11.5.18.

11.2 The Remuneration Committee and the Remuneration Policy

The Remuneration Committee (the 'Committee') shall be appointed by the Board of CCBL (the 'Board') and shall comprise of not less than two members of the Board who must be Non-Executive Directors of the Bank able to exercise independent judgment. The Chairman of the Committee shall be appointed by the Chairman of the Board.

The Committee is authorized by the Board of the Bank to ensure the implementation of effective remuneration governance and related risk management practice within China Construction Bank (London) Ltd. (the 'Bank'), and determine and adopt a remuneration policy which is in line with the FCA Remuneration Code and to review its implementation at least annually for compliance.

The Decision Making Process and the Link between Pay and Performance

The financial reward offered by the Bank comprises three components: base pay, variable pay and non-contractual benefits. Variable pay includes non-contractual and discretionary overtime and may also include annual discretionary bonus awards. Benefits consist of a standard non contractual benefits package.

11.3 Key Performance Indicators

The Bank's overall performance is evaluated against key performance indicators ('KPI's) set by the Head Office of China Construction Bank Corporation and agreed with the Board Remuneration Committee of CCBL.

11.4 Variable Components

The variable pay (discretionary bonus) is based upon a combination of assessments of performance against the following:

- The performance of the Bank;
- The performance of departments;
- The performance of employees in the context of the annual objectives of their role; and
- External compensation benchmarks

The Bank may award employees with annual discretionary bonuses. Where a bonus is paid, the amount is wholly at the discretion of the Bank and payments made will be non –pensionable awards that are subject to tax and National Insurance. The annual cash discretionary bonus allocation for senior executives and all other staff whose base pay exceeds £120,000 per annum needs to be agreed by both CCB Head Office and the Board Remuneration Committee. The intention of the Bank's bonus scheme is to motivate employees by providing a fair return for additional effort or exceptional performance, as well as to attract and retain talented staff.

11.5 Quantitative Information

By the end of 2015, the Bank had 107 employees who were eligible for variable pay in respect of their services during 2015. Code Staff, as defined by the Financial Conduct Authority Remuneration Code, are employees who have a material impact on the Bank's risk profile, including persons who perform significant influence functions, senior Managers and risk takers. At the end of 2015 fifteen employees were identified as Code Staff.

Total staff remunerations costs (including base pay and variable pay) during 2015 were $12,065k (£8,136k) (excluding National Insurance) of which the remunerations cost of Senior Management and Code Staff was $4,179k (£2,818k). The total cost of variable pay in 2015 was $1,399k (£904k) of which $542k (£365k) was allocated to Senior Management and Code Staff.

*1GBP=1.48295 USD for 2015

The aggregate remuneration broken down by base pay & variable pay and senior management & members of staff whose actions have a material impact on the risk profile of the Bank.(USD'000)

	Senior Management	Code Staff	Non-Code Staff	Total
Number of relevant employees	9	15	92	107
Base pay	2,027	3,637	7,029	10,666
Variable pay	333	542	857	1,399
Total	2,360	4,179	7,886	12,065

11.6 Deferred Remuneration

The Bank is in "Proportionality Level Three". It has decided to dis-apply the deferral rule (SYSC19A.3.49R) under the "remuneration principles proportionality rule".

11.7 Severance Payments

The Bank did not make any 'sign–on' or severance payments during the year of 2015.