

FCM Bank Limited

C 50343

Annual Report

2016

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FCM Bank Limited

Directors, officer and other information

| | |
|-------------------------------------|--|
| <i>Directors:</i> | John Soler Ronald Huggett Anthony Mahoney Oyvind Oanes |
| <i>Secretary:</i> | Dr. Stephanie Sciberras |
| <i>Registered office:</i> | Aragon House Business Centre, Dragonara Road, St Julians STJ 3140, Malta. |
| <i>Country of incorporation:</i> | Malta |
| <i>Company registration number:</i> | C 50343 |
| <i>Auditor:</i> | Deloitte Audit Limited, Deloitte Place, Mriehel Bypass, Mriehel BKR 3000, Malta. |

FCM Bank Limited

Directors' report

For the year ended 31 December 2016

The directors present their report and the audited financial statements of the Bank for the year ended 31 December 2016.

Principal activities

The Bank is licensed as a credit institution under the Banking Act, Cap 371.

Performance Review

The operating income for the year increased by 31% from EUR226,635 to EUR296,981. This resulted primarily from material gains on an early redemption of an investment and no impairment loss as recognised in the prior year. The decrease in net interest and dividend income was due to the Bank not fully investing its available funds, and remaining very liquid as it focused its efforts on a change in shareholding.

Notwithstanding a growing local economy, the retail savings landscape remained challenging throughout 2016 with historically low interest rates with the Bank continuing to focus on providing superior customer service to mitigate this. The Bank, while not being able to offer high rates aimed to establish itself as the first choice for savings in Malta given its level of service. This resulted in an increase in customer deposits of almost EUR8m taking total deposits to over EUR56m, despite minimal advertising and lower interest rates being offered.

The Bank recognised a loss for the year of just under EUR1.2m for the year under review compared to a loss of just under EUR1.4m in the prior year for the reasons highlighted above. Throughout the year there was also a successful focus on reducing operating costs. The Bank continued to streamline its operations to cope with the current business environment but carried on investing in its IT systems and robust risk management and governance framework.

The present shareholder continues to support limited growth and in 2016 the Bank increased its issued share capital by a further EUR1.9m, which resulted in total equity of just under EUR8.2m. After regulatory adjustments this translated to total Own Funds of just over EUR7.1m and a strong Capital Adequacy Tier One Ratio of 16%.

The Bank measures the achievement of its objectives through the use of financial and non-financial measures as shown below:

The Bank measures its liquidity risk by way of its minimum regulatory ratio set by BR05 at 30%, and also its Liquidity Coverage Ratio where the minimum is set at 80%. In both cases the Bank's ratios were significantly higher by a multiple factor.

The strength of the Bank's brand is measured partly by assessing the direct cost of marketing spent on raising new deposits, which stood at 0.29% for 2016 versus 0.33% for 2015.

With reduced interest rates, the average deposit cost of the Bank came down from 3.5% at 31 December 2015 to 3.1% at 31st December 2016.

One of the ways customer satisfaction is tracked is by way of the Bank's customer retention statistics which stood at 79% for 2016, which was significantly higher than the 65% achieved for 2015.

FCM Bank Limited

Directors' report (continued)

For the year ended 31 December 2016

The Bank measures its executive commitment by ensuring continuity of senior management and directors, out of which for 2016 only one senior manager left the Bank and there was no change in the Board composition.

The Bank is committed to corporate social responsibility and supported a number of initiatives throughout the year together with the participation of its staff.

Principal risks and uncertainties

The Board has designed a risk management framework and set the risk appetite for the Bank. The Bank's risk management approach depends on the interaction of a number of key components from risk identification through to mitigation, assessment and quantification. This ensures that the Bank's plans are consistent with the Board's risk appetite and ensure that optimal risk-return decisions are taken within appropriate review and challenge structures. The ultimate responsibility for risk management rests with the Directors who have identified the following principal risks and uncertainties facing the Bank:

People risk

With its limited size, the Bank is exposed to people risk arising principally from the loss of, or dependency on, key employees and lack of succession planning. The Bank mitigates the risk of single dependency through ensuring continuity in the absence of any individual.

Strategy risk

A delay in finalising the change in shareholding risks leading to non-maximisation of profits and non-optimal resource allocation. The Bank is well capitalised to sustain this position and has assurances from the existing shareholder to continue to sustain the Bank with required capital until such time as a new investor is approved.

Reputation risk

The Bank's reputation is essential in attracting deposits as any damage to its good standing would negatively impact the trust that depositors require in order to be willing to place their savings at an institution. The Bank is fully focused on developing and maintaining its brand value.

Business risk management

Strategic and Business risk is the risk of losses due to failed or inadequate strategy execution, marketing and sales practices, distribution channels, pricing, handling of customer complaints or late reaction to changes in the business environment. The Bank has a strong governance framework to mitigate this risk.

Financial risk management

Note 24 to the financial statements provides details in connection with the Bank's use of financial instruments, its financial risk management objectives and policies and the financial risks to which it is exposed.

FCM Bank Limited

Directors' report (continued)

For the year ended 31 December 2016

Result and dividends

The result for the year ended 31 December 2016 is shown in the statement of profit or loss and other comprehensive income on page eight. The loss for the year after tax was EUR1,198,611. This is as a result of the Bank being constrained by ongoing discussions with potential new investors during the year resulting in excess liquidity.

No dividend is being recommended.

Post-balance sheet events

At the time of signing the Financial Statements, a Sale and Purchase Agreement was signed with a potential new investor who intends to make an application to the Regulator for a change of control. The Board welcome this approach and are supportive of its proposed business plan. It could be a number of months before the result of this application is known and in the meantime the Board will be conducting business as usual.

Likely future business developments

The new shareholder subject to approval from the Regulator will be looking to change the business plan of the Bank and will be aiming to put the Bank into a profitable position within 12 months. The remainder of 2017 is expected to be taken up by the application process and the smooth transition to the new ownership.

Directors

The directors who served during the period were:

John Soler
Ronald Huggett
Anthony Mahoney
Oyvind Oanes


In accordance with the company's articles of association all the directors are to remain in office.

Auditors

A resolution to reappoint Deloitte Audit Limited as auditor of the Bank will be proposed at the forthcoming annual general meeting.

Approved by the Board of Directors on 20 April 2017 and signed on its behalf by:


John Soler
Director


Ronald Huggett
Director

FCM Bank Limited

Preparation of financial statements and directors' responsibilities

The Directors are required by the Companies Act (Cap.386) to prepare financial statements in accordance with International Financial Reporting Standards as adopted by the EU which give a true and fair view of the state of affairs of the Bank as at the end of the financial year and of the profit or loss of the Bank for the year then ended. In preparing the financial statements, the Directors should:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable; and
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Bank will continue in business as a going concern.

The Directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Bank, and which enable the Directors to ensure that the financial statements comply with the Banking Act (Cap.371) and the Companies Act (Cap.386 of the Laws of Malta). This responsibility includes designing, implementing and maintaining such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error. The Directors are also responsible for safeguarding the assets of the Bank, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

After reviewing the Bank's plans for the coming financial periods, the Directors are satisfied that at the time of approving the financial statements, it is appropriate to continue adopting the going concern basis in preparing the financial statements.

Independent auditor's report

to the members of
FCM Bank Limited

Opinion

We have audited the financial statements of FCM Bank Limited (the Bank), set out on pages 10 to 50, which comprise the statement of financial position as at 31 December 2016, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2016, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and have been properly prepared in accordance with the requirements of the [Maltese] Companies Act (Cap. 386).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). 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 International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Malta, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Information Other than the Financial Statements and the Auditor's Report Thereon

The directors are responsible for the other information. The other information comprises the Bank's information on page 2, the statement of directors' responsibilities on page 6 and the information included in the Directors' report and the Additional regulatory disclosures, but does not include the financial statements and our auditor's report thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information; we are required to report that fact. We have nothing to report in this regard.

With respect to the Directors' report, we also considered whether the Directors' report includes the disclosure requirements of Article 177 of the Companies Act (Cap. 386).

In accordance with the requirements of sub-article 179(3) of the Maltese Companies Act (Cap. 386) in relation to the Directors' Report on page 3 to 5, in our opinion, based on the work undertaken in the course of the audit:

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

In the light of the knowledge and understanding of the Bank and its environment obtained in the course of the audit, we have not identified any material misstatements in the Directors' Report.

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Cassar Torregiani & Associates is a firm of advocates warranted to practise law in Malta and is exclusively authorised to provide legal services in Malta under the Deloitte brand.

Independent auditor's report (continued)

to the members of
FCM Bank Limited

Responsibilities of the Directors for the Financial Statements

As explained more fully in the statement of directors' responsibilities on page 6, the directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Maltese Companies Act (Cap.386), and for such internal control as the directors determine 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, the directors are 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.

The Audit Committee is responsible for overseeing the Company'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 ISAs 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 ISAs, we exercise professional judgment and maintain professional scepticism 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 the directors.
- Conclude on the appropriateness of the directors' 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 the Audit Committee 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.

Independent auditor's report (continued)

to the members of
FCM Bank Limited

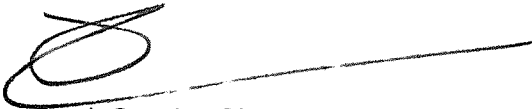
Report on Other Legal and Regulatory Requirements

Under the Maltese Companies Act (Cap. 386), we have responsibilities to report to you if in our opinion:

- Proper accounting records have not been kept;
- Proper returns adequate for our audit have not been received from branches not visited by us;
- The financial statements are not in agreement with the accounting records and returns; or
- We have been unable to obtain all the information and explanations which, to the best of our knowledge and belief, are necessary for the purpose of our audit.

We have nothing to report to you in respect of these responsibilities.

The engagement director on the audit resulting in this independent auditor's report is Sarah Curmi.



Sarah Curmi as Director
in the name and on behalf of
Deloitte Audit Limited
Registered auditor
Mriehel, Malta

20 April 2017

FCM Bank Limited

Statement of profit or loss and other comprehensive income

Year ended 31 December 2016

| | Notes | 2016 EUR | 2015 EUR |
|--|-------|--------------------|--------------------|
| Interest income | 4 | 1,614,165 | 2,085,709 |
| Dividend income | 12 | 128,730 | - |
| Interest expense | 5 | (1,738,855) | (1,620,346) |
| Net interest and dividend income | | 4,040 | 465,363 |
| Fee and commission expense | | (74,003) | (23,967) |
| Net fair value loss on financial assets at fair value through profit or loss | | (58,198) | (37,391) |
| Gains on financial assets not measured at fair value through profit or loss | 6 | 334,731 | - |
| Foreign exchange gains/(losses) | | 13,892 | (349) |
| Other income | | 76,519 | 5,566 |
| Impairment of assets | | - | (182,587) |
| Operating income | | 296,981 | 226,635 |
| Administration expenses | | (919,162) | (1,009,832) |
| Employee compensation and benefits | 7 | (576,430) | (672,960) |
| Loss before income tax | 8 | (1,198,611) | (1,456,157) |
| Income tax credit | 9 | - | 64,747 |
| Loss for the year | | (1,198,611) | (1,391,410) |
| Other comprehensive income | | | |
| <i>Items that may be reclassified subsequently to profit or loss:</i> | | | |
| Available-for-sale investments: | | | |
| - change in fair value | | 468,625 | (319,150) |
| - impairment of available for sale investment | | - | 182,587 |
| - deferred tax thereon | | (163,071) | 47,797 |
| Other comprehensive income/(loss) for the year net of tax | | 305,554 | (88,766) |
| Total comprehensive loss for the year | | (893,057) | (1,480,176) |

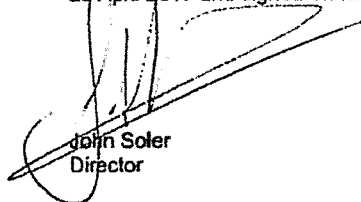
FCM Bank Limited

Statement of financial position

31 December 2016

| | Notes | 2016 EUR | 2015 EUR |
|--|-------|-------------------|-------------------|
| Assets | | | |
| Cash and cash equivalents | 15 | 9,042,019 | 18,388,764 |
| Depositor compensation scheme account with Central Bank of Malta | | 460,823 | 310,048 |
| Financial assets at fair value through profit or loss | 11 | 2,261,896 | 3,795,780 |
| Available-for-sale investments | 12.1 | 34,715,762 | 8,644,587 |
| Held-to-maturity investments | 12.2 | 13,603,710 | 17,149,606 |
| Loans and receivables | 12.3 | 4,059,557 | 6,457,575 |
| Intangible assets | 14 | 191,995 | 217,768 |
| Property, plant and equipment | 13 | 15,385 | 35,169 |
| Deferred tax | 16 | 839,974 | 1,003,045 |
| Prepayments and accrued income | 17 | 520,860 | 665,452 |
| Other assets | | 40,193 | 136,134 |
| Total assets | | 65,752,174 | 56,803,929 |
| Liabilities | | | |
| Amounts owed to customers | 18 | 56,849,001 | 48,906,650 |
| Other liabilities | | 22,991 | 22,034 |
| Trade and other payables | 19 | 699,253 | 701,259 |
| Total liabilities | | 57,571,245 | 49,629,943 |
| Equity | | | |
| Share capital | 20 | 12,250,000 | 10,350,000 |
| Investment revaluation reserve | 21 | 123,879 | (181,675) |
| Accumulated losses | 21 | (4,192,950) | (2,994,339) |
| Total equity | | 8,180,929 | 7,173,986 |
| Total liabilities and equity | | 65,752,174 | 56,803,929 |

The financial statements on pages 8 to 49 were approved by the Board of Directors on 20 April 2017 and signed on its behalf by:


John Soler
Director


Ronald Huggett
Director

FCM Bank Limited

Statement of changes in equity

Year ended 31 December 2016

| | Share capital EUR | Revaluation reserves EUR | Accumulated losses EUR | Total EUR |
|---|-------------------------|--------------------------------|------------------------------|------------------|
| Balance at 1 January 2015 | 9,500,000 | (92,909) | (1,602,929) | 7,804,162 |
| Loss for the year | - | - | (1,391,410) | (1,391,410) |
| Other comprehensive loss, net of tax | | | | |
| Available-for-sale investments: | | | | |
| -Change in fair value, net of tax | - | (207,448) | - | (207,448) |
| -Transfer to profit/loss | | 118,682 | | 118,682 |
| Total comprehensive loss for the year | - | (88,766) | (1,391,410) | (1,480,176) |
| Issue of share capital | 850,000 | - | - | 850,000 |
| Balance at 1 January 2016 | 10,350,000 | (181,675) | (2,994,339) | 7,173,986 |
| Loss for the year | - | - | (1,198,611) | (1,198,611) |
| Other comprehensive income, net of tax | | | | |
| Available-for-sale investments: | | | | |
| -Change in fair value, net of tax | - | 305,554 | - | 305,554 |
| Total comprehensive loss for the year | - | 305,554 | (1,198,611) | (893,057) |
| Issue of share capital | 1,900,000 | - | - | 1,900,000 |
| Balance at 31 December 2016 | 12,250,000 | 123,879 | (4,192,950) | 8,180,929 |

FCM Bank Limited

Statement of cash flows

Year ended 31 December 2016

| | 2016 EUR | 2015 EUR |
|---|-----------------------------|-----------------------------|
| Cash flows from operating activities | | |
| Interest received | 2,014,479 | 2,232,652 |
| Dividend and other income | 205,249 | 5,566 |
| Interest paid | (1,695,146) | (1,726,228) |
| Cash payment to employees and suppliers | (1,195,858) | (1,947,201) |
| | <u> </u> | <u> </u> |
| Operating loss before changes in operating assets and liabilities | (671,276) | (1,435,211) |
| | <u> </u> | <u> </u> |
| Cash flows from operating activities before changes in operating assets and liabilities | | |
| Net increase in deposits from customers | 7,942,351 | 10,476,073 |
| Net increase in other assets | (54,833) | (279,943) |
| Net increase/(decrease) in other liabilities | 953 | (2,495,268) |
| | <u> </u> | <u> </u> |
| <i>Net cash from operating activities</i> | 7,888,471 | 7,700,862 |
| | <u> </u> | <u> </u> |
| Cash flows from investing activities | | |
| Purchase of property, plant and equipment | (2,550) | (1,604) |
| Purchase of intangible assets | (41,787) | (70,235) |
| Acquisition of financial instruments | (29,228,436) | (9,579,680) |
| Proceeds from sale of financial instruments | 10,808,833 | 11,783,676 |
| | <u> </u> | <u> </u> |
| <i>Net cash (used in)/from investing activities</i> | (18,463,940) | 2,132,157 |
| | <u> </u> | <u> </u> |
| Cash flows from financing activities | | |
| Proceeds from issue of share capital | 1,900,000 | 850,000 |
| | <u> </u> | <u> </u> |
| <i>Net cash from financing activities</i> | 1,900,000 | 850,000 |
| | <u> </u> | <u> </u> |
| Increase in cash and cash equivalents | (9,346,745) | 9,247,808 |
| | <u> </u> | <u> </u> |
| Cash and cash equivalents at beginning of the year | 18,388,764 | 9,140,956 |
| | <u> </u> | <u> </u> |
| Cash and cash equivalents at the end of the year (note 15) | 9,042,019 | 18,388,764 |
| | <u> </u> | <u> </u> |

FCM Bank Limited

Notes to the financial statements

31 December 2016

1. Reporting entity

FCM Bank Limited (hereafter 'the Bank') is a limited liability company domiciled in Malta.

2. Summary of significant accounting policies

2.1 Basis of preparation

The financial statements have been prepared and presented in accordance with the provisions of the Banking Act (Cap. 371) and the Companies Act (Cap. 386) enacted in Malta, which requires adherence to International Financial Reporting Standards as adopted by the EU (hereafter referred to "IFRSs as adopted by the EU").

The financial statements have been prepared on the historical cost basis, except for financial instruments classified as at fair value through profit or loss and available-for-sale investments which are stated at their fair values. The significant accounting policies adopted are set out below.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

For financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis, the Company determines when transfers are deemed to have occurred between levels in the hierarchy at the end of each reporting period.

2.2 Initial application of an International Financial Reporting Standard and International Financial Reporting Standards in issue but not yet effective

Initial application of an International Financial Reporting Standard

On 12 December 2013, the IASB issued amendments to IAS 24 Related Party Disclosures (as part of the 'Annual Improvements to IFRSs 2010-2012 cycle'). Clarifying that an entity providing key management personnel services to the reporting entity or to the parent of the reporting entity is a related party of the reporting entity. The standard is applicable for annual periods beginning on or after 1 February 2015.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.2 Initial application of an International Financial Reporting Standard and International Financial Reporting Standards in issue but not yet effective (continued)

Initial application of an International Financial Reporting Standard (continued)

On 18 December 2014, the IASB issued an amendment to IAS 1 Presentation of Financial Statements. The amendments aim at clarifying IAS 1 to address perceived impediments to preparers exercising their judgement in presenting their financial reports. The amendments are designed to further encourage companies to apply professional judgement in determining what information to disclose in their financial statements. The amendments make clear that materiality applies to the whole of financial statements and that the inclusion of immaterial information can inhibit the usefulness of financial disclosures. Furthermore, the amendments clarify that companies should use professional judgement in determining where and in what order information is presented in the financial disclosures. This amendment is applicable for annual periods beginning on or after 1 January 2016.

International Financial Reporting Standards in issue but not yet effective

The final version of IFRS 9 Financial Instruments issued on 24 July 2014 brings together the classification and measurement, impairment and hedge accounting phases of the IASB's project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. The Standard supersedes all previous versions of IFRS 9.

IFRS 9 introduces a logical approach for the classification of financial assets, which is driven by cash flow characteristics and the business model in which an asset is held. This single, principle-based approach replaces existing rule based requirements that are generally considered to be overly complex and difficult to apply. The new model also results in a single, forward-looking 'expected loss' impairment model that will require more timely recognition of expected credit losses.

IFRS 9 is effective for annual periods beginning on or after 1 January 2018.

IFRS 15 Revenue from contracts with customers issued in May 2014 is the result of a convergence project between the IASB and the FASB. IFRS 15 specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18 'Revenue', IAS 11 'Construction Contracts' and a number of revenue-related interpretations. Application of the standard is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions being leases, financial instruments and insurance contracts. By virtue of an amendment issued on 11 September 2015, the effective date of the Standard was deferred by one year to annual periods beginning on or after 1 January 2018, with earlier application being permitted. This Standard has not as yet been endorsed by the EU.

On 19 January 2016, the IASB issued Amendments to IAS 12 to clarify how to account for deferred tax assets related to debt instruments measured at fair value to address diversity in practice. This amendment is effective for annual periods beginning on or after 1 January 2017. This amendment has not yet been endorsed by the EU.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.2 Initial application of an International Financial Reporting Standard and International Financial Reporting Standards in issue but not yet effective (continued)

International Financial Reporting Standards in issue but not yet effective (continued)

The directors are currently assessing the impact that the adoption of these International Financial Reporting Standards will have on the financial statements of the company in the period of initial application.

2.3 Functional and presentation currency

The financial statements are presented in Euro, which currency represents the functional currency of the Bank.

2.4 Foreign currency transactions

Transactions in foreign currencies are translated into the functional currency at the foreign exchange rate prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies at the end of the reporting period are translated to Euro at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the profit or loss. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Euro at foreign exchange rates ruling at the date the fair value was determined.

2.5 Financial assets

The Bank classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables, held-to-maturity financial assets and available-for-sale investments. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets on initial recognition.

2.5.1 Financial assets at fair value through profit or loss

This category comprises two sub-categories: financial assets classified as held for trading, and financial assets designated by the Bank as at fair value through profit or loss upon initial recognition.

A financial asset is classified as held for trading if it is acquired principally for the purpose of selling it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking after initial recognition, financial assets at fair value through profit and loss are measured at their fair value. Gains and losses arising from a change in fair value are recognised in profit or loss in the period in which they arise.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.5 Financial assets (continued)

2.5.2 Held-to-maturity financial assets

Non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity other than those that upon initial recognition are designated as at fair value through profit or loss, those that are designated as available-for-sale financial assets and those that meet the definition of loans and receivables are classified as held-to-maturity investments. If other than an insignificant amount of held-to-maturity assets were to be sold, the entire category would be tainted and reclassified as available-for-sale.

After initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the financial asset is derecognised or impaired and through the amortisation process.

When applying the effective interest method, the annual amortisation of any discount or premium is aggregated with other investment income receivable over the term of the instrument, if any, so that the revenue recognised in each period represents a constant yield on the investment.

2.5.3 Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are either designated in this category by the Bank or not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. After initial recognition, available-for-sale financial assets are measured at their fair value. Gains and losses arising from a change in fair value are recognised in other comprehensive income, except for impairment losses and foreign exchange gains and losses on monetary assets, until the financial asset is derecognised, at which time the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment. Interest calculated using the effective interest method is recognised in profit or loss.

2.5.4 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than those that are held for trading or are designated upon initial recognition as at fair value through profit or loss or as available-for-sale financial assets or those for which the company may not recover substantially all of its initial investment other than because of credit deterioration.

2.5.5 Impairment

All assets are tested for impairment except for financial assets measured at fair value through profit or loss and deferred tax assets.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.5 Financial assets (continued)

2.5.5 Impairment (continued)

The Bank assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated

In the case of financial assets that are either carried at amortised cost or classified as available-for-sale investments, objective evidence of impairment includes observable data about the following loss event – significant financial difficulty of the issuer or counterparty.

An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

For loans and receivables or held-to maturity investments, if there is objective evidence that an impairment loss has been incurred, the amount of the 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 that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases, and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through an allowance account, but so that the reversal does not result in a carrying amount that exceeds what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal is recognised in profit or loss.

When a decline in the fair value of an available-for-sale financial asset has been recognised in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative impairment loss that had been recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment and is measured as the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in profit or loss.

2.6 Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into, and the definitions of a financial liability and an equity instrument.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2.6 Financial liabilities and equity instruments (continued)

Financial liabilities are initially measured at fair value plus, in the case of financial liabilities not at fair value through profit or loss, transaction costs that are directly attributable to their issue. Financial liabilities are subsequently measured at amortised cost using the effective interest method, except for financial liabilities at fair value through profit or loss, which are measured at fair value.

Financial liabilities at fair value through profit or loss include financial liabilities classified as held for trading and those designated at fair value through profit or loss upon initial recognition. During the current period the Bank did not designate any financial liabilities as at fair value through profit or loss upon initial recognition.

Financial liabilities that are measured at amortised cost using the effective interest method include amounts owed to customers. The gain or loss on financial liabilities classified as at fair value through profit or loss is recognised in profit or loss.

For financial liabilities carried at amortised cost, the gain or loss is recognised in profit or loss when the financial liability is derecognised and through the amortisation process whereby any difference between the proceeds net of transaction costs, and the settlement or redemption is recognised over the term of the financial liability.

Equity instruments are recorded at the proceeds received, net of direct issue costs.

2.7 Recognition, de-recognition and offsetting of financial assets and financial liabilities

Financial assets and financial liabilities are recognised when the Bank becomes a party to the contractual provisions of the instrument.

All purchases and sales of securities are recognised and derecognised on trade date, which is the date the Bank becomes party to the contract.

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire, or when the Bank transfers the financial asset and the transfer qualifies for derecognition. A financial liability is derecognised when it is extinguished. This occurs when the obligation specified in the contract is discharged, cancelled or expires.

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when the Bank has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

2.8 Classification of financial assets and financial liabilities at fair value through profit or loss upon initial recognition

The Bank considers the statement of comprehensive income to be the primary report of performance within the annual financial statements and ensures that, as far as practicable, all aspects of its performance are wholly and fairly reflected in profit or loss.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.8 Classification of financial assets and financial liabilities at fair value through profit or loss upon initial recognition (continued)

Financial assets and liabilities are designated at fair value through profit or loss on initial recognition where such designation results in more relevant information because either:

- it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an "accounting mismatch") that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or

- a group of financial assets, financial liabilities or both, is managed and its performance is evaluated on a fair value basis, in accordance with the Bank's documented risk management and investment strategy, and information about the group is provided internally on that basis to key management personnel, including the Board of Directors.

2.9 Property, plant and equipment

Property, plant and equipment are classified into the following class – office furniture and fittings.

Property, plant and equipment are initially measured at cost. Subsequent costs are included in the asset's carrying amount when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. Expenditure on repairs and maintenance of property, plant and equipment is recognised as an expense when incurred.

Property, plant and equipment are derecognised on disposal or when no future economic benefits are expected from their use or disposal. Gains or losses arising from de-recognition represent the difference between the net disposal proceeds, if any, and the carrying amount, and are included in profit or loss in the period of de-recognition.

Tangible assets are stated at cost less any accumulated depreciation and any accumulated impairment losses.

2.10 Depreciation

Depreciation on property, plant and equipment commences when these assets are available for use and are charged to profit or loss so as to write off the cost of assets, less any estimated residual value, over their estimated useful life, using the straight line method, on the following bases:

Office furniture and fittings 10% per annum
Computers, hardware and peripherals 33% per annum

The depreciation method applied, the residual value and the useful life are reviewed at the end of each reporting period.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.11 Impairment of property, plant and equipment

At the end of each reporting period the Bank reviews the carrying amount of its property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss. If such indication exists, the recoverable amount is estimated in order to determine the extent of the impairment loss and the carrying amount of the asset is reduced to its recoverable amount, as calculated. The recoverable amount is the higher of fair value less costs to sell and value in use.

An impairment loss is recognised immediately in profit or loss, unless the asset is carried at a revalued amount, in which case the loss is recognised in other comprehensive income to the extent that it does not exceed the amount in the revaluation surplus for that asset. An impairment loss recognised in a prior year is reversed if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, to the extent that it does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years.

Impairment reversals are recognised immediately in profit or loss, unless the asset is carried at a revalued amount, in which case the impairment reversal is recognised in other comprehensive income, unless an impairment loss on the same asset was previously recognised in profit or loss.

2.12 Intangible assets

An intangible asset is recognised if it is probable that the expected future economic benefits that are attributable to the asset will flow to the Bank and the cost of the asset can be measured reliably. Expenditure on an intangible asset is recognised as an expense in the period when it is incurred unless it forms part of the cost of the asset that meets the recognition criteria.

The useful life of intangible assets is assessed to determine whether it is finite or indefinite. Intangible assets with a finite useful life are amortised. Amortisation is charged to profit or loss so as to write off the cost of the intangible asset less any estimated residual value, over their estimated useful lives. The amortisation method applied, the residual value and the useful life are reviewed, and adjusted if appropriate, at the end of each reporting period.

Intangible assets are derecognised on disposal or when no future economic benefits are expected from their use or disposal. Gains or losses arising from de-recognition represent the difference between the net disposal proceeds, if any, and the carrying amount, and are included in profit or loss in the period of de-recognition. Expenditure on research activities is recognised as an expense in the period in which it is incurred.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.12 Intangible assets (continued)

An internally-generated intangible asset arising from the company's development of software is recognised only if all of the following can be demonstrated by the company: the technical feasibility, the availability of resources and the intention and ability of completing the asset so that it will be available for use or sale, how the asset will generate probable future economic benefits, and the ability to measure reliably the expenditure attributable to the asset during its development.

Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred. After initial recognition, internally-generated intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally-generated intangible assets are amortised on a straight-line basis over their estimated useful lives from the date when they become available for use, which is generally assumed to be five years.

2.13 Provisions, contingent liabilities and contingent assets

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Provisions are measured at the directors' best estimate of the expenditure required to settle the present obligation at the end of the reporting period. If the effect of the time value of money is material, 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, where appropriate, the risks specific to the liability. Provisions are not recognised for future operating losses.

A contingent liability is (a) a possible obligation that arises from past events and 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 entity; or (b) a present obligation that arises from past events but is not recognised because: (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability. Contingent liabilities are not recognised. Contingent liabilities are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is a possible asset that arises from past events and 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 entity. Contingent assets are not recognised. Contingent assets are disclosed where an inflow of economic benefits is probable.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.14 Taxation

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the profit or loss except to the extent that it relates to items recognised directly in other comprehensive income or directly in equity, in which case it is also dealt with in the statement of comprehensive income or in equity as appropriate.

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at the end of the reporting period, and any adjustment to tax payable in respect of previous periods. Deferred tax is provided using the balance sheet liability method, providing for 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 the temporary differences when they reverse based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. 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 realised.

Current tax assets and liabilities are offset when the Bank has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Deferred tax assets and liabilities are offset when the Bank has a legally enforceable right to set off its current tax assets and liabilities and the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

2.15 Revenue recognition

Revenue is recognised to the extent that it is probable that future economic benefits will flow to the Bank and these can be measured reliably. The following specific recognition criteria must also be met before revenue is recognised.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the instrument or, when appropriate, a shorter period to that instrument's net carrying amount. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the instrument but not future credit losses. The calculation includes payments and receipts that are an integral part of the effective interest rate, transaction costs and all other discounts or premiums.

FCM Bank Limited

Notes to the financial statements

31 December 2016

2. Summary of significant accounting policies (continued)

2.15 Revenue recognition (continued)

Dividend income from financial assets classified as available for sale are recognised in the statement of profit or loss and other comprehensive income when the Bank's right to receive payment is established. Usually this is the ex-dividend date for equity securities.

Fees and commissions that are earned on the execution of a significant act are recognised as revenue when the significant act has been completed. Fees and commissions that are earned as services are provided to the customer are recognised as revenue as the services are provided. Where fees are charged to cover the cost of a continuing service, these are recognised on an appropriate basis over the relevant period.

2.16 Employee benefits

The Bank contributes towards the state pension in accordance with local legislation. The only obligation of the Bank is to make the required contributions. Costs are expensed in the period in which they are incurred.

2.17 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and deposits repayable on demand or with a contractual period to maturity of less than 90 days; advances to banks repayable within 90 days from the date of the advance; balances with the Central Bank of Malta, excluding reserve deposit requirements and treasury bills with an original maturity of less than 90 days. Amounts owed to banks that are repayable on demand or with a contractual period to maturity of less than 90 days and which form an integral part of the Bank's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

2.18 Dividends payable

Dividends payable on ordinary shares are recognised as liabilities on the date they are declared.

2.19 Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards incidental to ownership to the lessee. All other leases are classified as operating leases. Lease classification is made at the inception of the lease, which is the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease.

Rentals payable under operating leases, less the aggregate benefit of incentives received from the lessor, are recognised as an expense in profit or loss on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

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Notes to the financial statements

31 December 2016

3. Use of estimates and judgements

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

In the process of applying the Bank's accounting policies, management has made no judgements, other than the one disclosed below, which can significantly affect the amounts recognised in the financial statements and, at the end of the reporting period, there were no key assumptions concerning the future, or any other key sources of estimation uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Recognition of deferred tax assets

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that profit will be available against which the losses can be utilised. Management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits. The Bank makes an annual assessment of whether or not it will have sufficient taxable profits in the future to realise the deferred tax assets. This is a matter of careful judgement and based on facts and circumstances available as further explained in note 16.

4. Interest income

| | 2016 | 2015 |
|--|------------------|------------------|
| | EUR | EUR |
| On debt and other fixed income instruments | | |
| - available-for-sale | 453,473 | 527,090 |
| - held-to-maturity | 1,009,189 | 1,364,955 |
| - fair value through profit or loss | 127,473 | 102,849 |
| - loans and receivables | 255,254 | 411,135 |
| | <u>1,845,389</u> | <u>2,406,029</u> |
| Amortisation of discounts and premiums | | |
| - available-for-sale | (53,459) | (56,590) |
| - held-to-maturity | (180,361) | (260,109) |
| - loans and receivables | 2,596 | (3,621) |
| | <u>(231,224)</u> | <u>(320,320)</u> |
| | <u>1,614,165</u> | <u>2,085,709</u> |

FCM Bank Limited

Notes to the financial statements

31 December 2016

5. Interest expense

| | 2016 EUR | 2015 EUR |
|------------------------------|------------------|------------------|
| On amounts owed to customers | <u>1,738,855</u> | <u>1,620,346</u> |

6. Gains on financial assets not measured at fair value through profit and loss

| | 2016 EUR | 2015 EUR |
|--|----------------|-------------|
| Gain on redemption of available-for-sale investments | 321,149 | - |
| Gain on redemption of held-to-maturity investments | 13,582 | - |
| | <u>334,731</u> | <u>-</u> |

7. Employee compensation and benefits

7.1 Key management personnel compensation

| | 2016 EUR | 2015 EUR |
|----------------------------|----------------|----------------|
| <i>Short-term benefits</i> | | |
| Directors' emoluments: | | |
| - Directors' fees | 57,000 | 66,712 |
| - Directors' remuneration | 133,712 | 118,747 |
| | <u>190,512</u> | <u>185,459</u> |

7.2 Analysis of personnel expenses for the year

| | 2016 EUR | 2015 EUR |
|-----------------------|----------------|----------------|
| Wages and salaries | 558,424 | 650,731 |
| Social security costs | 18,006 | 22,229 |
| | <u>576,430</u> | <u>672,960</u> |

FCM Bank Limited

Notes to the financial statements

31 December 2016

7. Employee compensation and benefits

7.3 Average number of persons employed for the year including executive and non-executive directors

| | 2016 No. | 2015 No. |
|-------------------------|-------------|-------------|
| Non-executive directors | 3 | 3 |
| Managerial | 4 | 4 |
| Other | 6 | 5 |
| | <u>13</u> | <u>12</u> |

8. Loss before tax

Loss before tax is stated after charging:

| | 2016 EUR | 2015 EUR |
|--|---------------|---------------|
| Total remuneration payable to the Bank's auditors for: | | |
| - the audit of the financial statements | 15,000 | 13,500 |
| - total fees payable to the company's auditor for non-audit services other than other assurance services and tax advisory services | 11,222 | 3,100 |
| | <u>26,222</u> | <u>16,600</u> |

9. Income tax credit

| | 2016 EUR | 2015 EUR |
|---------------------|-------------|---------------|
| Deferred tax credit | - | 64,747 |
| | <u>-</u> | <u>64,747</u> |

FCM Bank Limited

Notes to the financial statements

31 December 2016

9. Income tax credit (continued)

Tax applying the statutory domestic income tax rate and the income tax expense for the year are reconciled as follows:

| | 2016 EUR | 2015 EUR |
|--|-------------|---------------|
| Loss before tax | 1,198,611 | 1,456,157 |
| Tax charge at the applicable rate of 35% | 419,514 | 509,655 |
| <i>Tax effect of:</i> | | |
| Difference between depreciation and amortisation charge and capital allowances | (31,463) | (28,107) |
| Disallowed expenses | (22) | 841 |
| Unabsorbed tax losses for the year | (388,029) | (417,642) |
| Total income tax credit | - | 64,747 |

10. Operating leases

The Bank recognised minimum lease payments under operating leases amounting to EUR48,962 (2015: EUR48,395) as an expense for the year.

Operating lease payments represent rentals payable by the Bank for the use of office premises. The Bank's lease agreement provides for the rental of office premises for three years extendable for a further two years at the lessee's option. The Bank has extended the lease agreement for these further 2 years. The lease agreement is cancellable upon the payment of a penalty equal to one year's rent.

FCM Bank Limited

Notes to the financial statements

31 December 2016

11. Financial assets at fair value through profit or loss

| | 2016 EUR | 2015 EUR |
|--|------------------|------------------|
| Debt and other fixed income instruments | | |
| Issued by public bodies: | | |
| - local government | 1,877,247 | 2,917,783 |
| - foreign government | 384,649 | 877,997 |
| | <u>2,261,896</u> | <u>3,795,780</u> |
| Listing status | | |
| -local listed | 1,877,247 | 2,917,783 |
| -foreign listed | 384,649 | 877,997 |
| | <u>2,261,896</u> | <u>3,795,780</u> |
| Summary of movements during the year: | | |
| At the beginning of the year | 3,795,780 | 1,227,536 |
| Acquisitions | 228,821 | 3,841,822 |
| Matured | (1,589,553) | (1,250,000) |
| Movement in fair value | (173,152) | (23,578) |
| At the end of the year | <u>2,261,896</u> | <u>3,795,780</u> |

Financial assets are designated at fair value through profit or loss on initial recognition where such designation results in more relevant information because either:

- it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an "accounting mismatch") that would otherwise arise from measuring assets or recognising the gains and losses on them on different bases; or

- a group of financial assets is managed and its performance is evaluated on a fair value basis, in accordance with the Bank's documented risk management and investment strategy, and information about the position is provided internally on that basis to key management personnel, including the Credit and Risk Committee.

FCM Bank Limited

Notes to the financial statements

31 December 2016

12. Investments

| | 2016 EUR | 2015 EUR |
|--|-------------------|-------------------|
| Debt and other fixed income instruments | | |
| - available-for-sale | 5,671,494 | 8,644,587 |
| - held-to-maturity | 13,603,710 | 17,149,606 |
| - loans and receivables | 4,059,557 | 6,457,575 |
| | <u>23,334,761</u> | <u>32,251,768</u> |
| Exchange traded debt funds | | |
| - available-for-sale | 29,044,268 | - |
| | <u>52,379,029</u> | <u>32,251,768</u> |

Exchange traded debt funds earn dividend income which is included in the statement of profit and loss and other comprehensive income.

12.1 Debt, other fixed income instruments and fund investments classified available-for-sale

| | 2016 EUR | 2015 EUR |
|---------------------------------------|-------------------|------------------|
| Issued by other issuers: | | |
| - foreign other | 34,715,762 | 8,644,587 |
| | <u>34,715,762</u> | <u>8,644,587</u> |
| Listing status: | | |
| - foreign listed | 34,715,762 | 8,644,587 |
| | <u>34,715,762</u> | <u>8,644,587</u> |
| Summary of movements during the year: | | |
| At the beginning of the year | 8,644,587 | 4,949,739 |
| Acquisitions | 28,999,615 | 3,931,250 |
| Disposals | (3,453,131) | (103,158) |
| Amortisation | (53,459) | (56,590) |
| Movement in foreign exchange | 109,525 | (319,150) |
| Movement in fair value | 468,625 | 425,083 |
| Impairment | - | (182,587) |
| | <u>34,715,762</u> | <u>8,644,587</u> |

During the prior reporting period, one investment classified as available-for-sale was deemed to be impaired and therefore the gains/losses previously recognised in other comprehensive income were reclassified to profit or loss.

FCM Bank Limited

Notes to the financial statements

31 December 2016

12. Investments (continued)

12.2 Debt and other fixed income instruments classified as held-to-maturity

| | 2016 EUR | 2015 EUR |
|---------------------------------------|-------------------|-------------------|
| Issued by other issuers: | | |
| - foreign other | <u>13,603,710</u> | <u>17,149,606</u> |
| Listing status: | | |
| - foreign listed | <u>13,603,710</u> | <u>17,149,606</u> |
| Summary of movements during the year: | | |
| At the beginning of the year | 17,149,606 | 24,068,663 |
| Redemptions | (3,365,535) | (6,658,948) |
| Amortisation | (180,361) | (260,109) |
| At the end of the year | <u>13,603,710</u> | <u>17,149,606</u> |

At 31 December 2016, the fair value of held-to-maturity securities amounted to EUR14,007,138 (2015: EUR17,050,231).

12.3 Debt and other fixed income instruments classified as loans and receivables

| | 2016 EUR | 2015 EUR |
|---------------------------------------|------------------|------------------|
| Issued by other issuers: | | |
| - foreign other | <u>4,059,557</u> | <u>6,457,575</u> |
| Listing status: | | |
| - foreign unlisted | <u>4,059,557</u> | <u>6,457,575</u> |
| Summary of movements during the year: | | |
| At the beginning of the year | 6,457,575 | 8,234,016 |
| Acquisitions | - | 1,998,750 |
| Disposals | (2,400,614) | (3,771,570) |
| Amortisation | 2,596 | (3,621) |
| At the end of the year | <u>4,059,557</u> | <u>6,457,575</u> |

At 31 December 2016, the fair value of loans and receivables amounted to EUR4,063,521 (2015: EUR6,448,144).

FCM Bank Limited

Notes to the financial statements

31 December 2016

13. Property, plant and equipment

| | Furniture and fittings EUR | Computers, hardware and peripherals EUR | Total EUR |
|------------------------------------|-------------------------------|---|---------------|
| Cost | | | |
| At 1 January 2015 | 90,231 | 36,242 | 126,473 |
| Additions | 1,604 | - | 1,604 |
| At 1 January 2016 | 91,835 | 36,242 | 128,077 |
| Additions | - | 2,550 | 2,550 |
| At 31 December 2016 | 91,835 | 38,792 | 130,627 |
| Depreciation | | | |
| At 1 January 2015 | 41,927 | 26,704 | 68,631 |
| Charge for the year | 18,273 | 6,004 | 24,277 |
| At 1 January 2016 | 60,200 | 32,708 | 92,908 |
| Charge for the year | 18,403 | 3,931 | 22,334 |
| At 31 December 2016 | 78,603 | 36,639 | 115,242 |
| Carrying amounts | | | |
| Balance at 31 December 2015 | 31,635 | 3,534 | 35,169 |
| Balance at 31 December 2016 | 13,232 | 2,153 | 15,385 |

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14. Intangible assets

| | Software EUR |
|----------------------------|-------------------------|
| Cost | |
| At 1 January 2015 | 244,681 |
| Additions | 70,235 |
| | <hr/> |
| At 1 January 2016 | 314,916 |
| Additions | 41,787 |
| | <hr/> |
| At 31 December 2016 | 356,703 |
| | <hr/> |
| Amortisation | |
| At 1 January 2015 | 41,117 |
| Charge for year | 56,031 |
| | <hr/> |
| At 1 January 2016 | 97,148 |
| Charge for year | 67,560 |
| | <hr/> |
| At 31 December 2016 | 164,708 |
| | <hr/> |
| Carrying amount | |
| At 31 December 2015 | 217,768 |
| | <hr/> |
| At 31 December 2016 | 191,995 |
| | <hr/> <hr/> |

15. Cash and cash equivalents

Cash and cash equivalents comprise balances with less than three months maturity from the date of acquisition, including cash in hand and deposits held on call with banks.

| | 2016 EUR | 2015 EUR |
|---------------------------------------|---------------------|---------------------|
| Repayable on call and at short notice | 9,042,019 | 18,388,764 |
| | <hr/> <hr/> | <hr/> <hr/> |

Currently, deposit accounts repayable on call and at short notice earn no interest or incur negative interest.

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16. Deferred tax assets

Recognised deferred tax assets

Deferred tax assets are attributable to the following:

| | 2016 EUR | 2015 EUR |
|---|----------------|------------------|
| Tax value of losses and capital allowances carry-forwards | 903,774 | 903,037 |
| Fair value re-measurement of financial instruments | (63,800) | 100,008 |
| | <u>839,974</u> | <u>1,003,045</u> |

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. The directors believe that the Bank is well placed to manage its business risks successfully and have a reasonable expectation that the deferred tax asset will crystallise in the foreseeable future. In assessing whether the deferred tax asset should be recognised, the Directors have taken into account the business plan and commitments made by the incoming investor. The Directors will continue to monitor the position on an ongoing basis.

17. Prepayments and accrued income

| | 2016 EUR | 2015 EUR |
|------------------|----------------|----------------|
| Accrued income | 362,131 | 531,221 |
| Prepaid expenses | 158,729 | 134,231 |
| | <u>520,860</u> | <u>665,452</u> |

18. Amounts owed to customers

| | 2016 EUR | 2015 EUR |
|------------------|-------------------|-------------------|
| Term deposits | 54,705,409 | 47,492,597 |
| Savings accounts | 2,143,592 | 1,414,053 |
| | <u>56,849,001</u> | <u>48,906,650</u> |

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19. Trade and other payables

| | 2016 EUR | 2015 EUR |
|------------------|----------------|----------------|
| Interest payable | 632,971 | 589,262 |
| Accrued expenses | 66,282 | 111,997 |
| | <u>699,253</u> | <u>701,259</u> |

20. Share capital

| | 2016 EUR | 2015 EUR |
|---|-------------------|-------------------|
| Authorised: | | |
| Ordinary shares at EUR1 each | <u>20,000,000</u> | <u>20,000,000</u> |
| Issued and paid up: | | |
| Ordinary shares at EUR1 each fully paid | <u>12,250,000</u> | <u>10,350,000</u> |

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

On 29 February 2016, 26 May 2016, 5 October 2016 and 6 December 2016, the issued share capital was increased by EUR500,000, EUR500,000, EUR400,000 and EUR500,000 respectively. The EUR1,900,000 increase in issued and called up share capital was effected via cash.

21. Reserves

21.1 Investment revaluation reserve

The revaluation reserve is used to record movements in fair value of available for sale investments net of deferred tax thereon. The revaluation reserve is not available for distribution.

21.2 Accumulated losses

Accumulated losses represent the total value of losses incurred by the Bank since incorporation.

Accumulated losses include an amount of EUR460,823 (2015: EUR310,048) allocated to the Depositor Compensation Scheme Reserve. This reserve is excluded for the purposes of Own Funds calculation.

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22. Related parties

Related party transactions during the year were as follows:

| | 2016 EUR | 2016 Total EUR | 2016 % of total |
|---|-------------|----------------------|--------------------|
| Interest expense on deposits | 2,404 | 1,738,855 | 0.1% |
| Compensation to key management personnel | | | |
| Directors' fee and remuneration | 180,512 | 180,512 | 100% |
| Balances with related parties | | | |
| Other assets | 39,478 | 40,193 | 98% |
| Deposits from customers | 93,631 | 54,705,409 | 0.17% |
| Accrued interest on deposits from customers | 1,132 | 632,971 | 0.18% |
| Transaction with related parties | | | |
| Operating expenses | 72,249 | 395,918 | 18% |

Related party transactions during the year were as follows:

| | 2015 EUR | 2015 Total EUR | 2015 % of total |
|---|-------------|----------------------|--------------------|
| Interest expense on deposits | 2,085 | 1,620,346 | 0.1% |
| Compensation to key management personnel | | | |
| Directors' fee and remuneration | 185,459 | 185,459 | 100% |
| Balances with related parties | | | |
| Other assets | 37,033 | 136,135 | 27% |
| Deposits from customers | 84,875 | 48,906,650 | 0.17% |
| Accrued interest on deposits from customers | 1,062 | 589,262 | 0.18% |
| Transaction with related parties | | | |
| Operating expenses | 75,698 | 487,501 | 16% |

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22. Related parties (continued)

No expense has been recognised in the year for bad and doubtful debts in respect of amounts due from related parties and there are no provisions for doubtful debts in respect of outstanding amounts due by related parties (2015: *EUR Nil*).

The immediate and ultimate parent company of the Bank is Gramercy Match Trust and the ultimate controlling party is Timothy Charles Babich.

23. Fair values of financial assets and financial liabilities

At 31 December 2016 the fair value of amounts owed to customers amounted to EUR57,768,000 (2015: EUR49,799,417).

The fair values of held-to-maturity investments amounted to EUR14,007,138 at the end of the reporting period (2015: EUR17,050,231). The fair value of loans and receivables amount to EUR4,057,271 (2015: EUR6,448,144) at the end of the reporting period.

At 31 December 2016 and 2015 the carrying amounts of financial assets and financial liabilities, other than those described above, approximated their fair values due to the short term maturities of these assets and liabilities.

| | Level 1 EUR | Level 2 EUR | Level 3 EUR | Total EUR |
|--|-------------------|-------------------|----------------|-------------------|
| 2016 | | | | |
| Financial assets at fair value through profit or loss | | | | |
| - foreign listed debt instruments | 384,649 | - | - | 384,649 |
| - local listed debt instruments | 1,877,247 | - | - | 1,877,247 |
| | <u>2,261,896</u> | <u>-</u> | <u>-</u> | <u>2,261,896</u> |
| Available-for-sale investments | | | | |
| - foreign listed debt instruments | 21,481,980 | - | - | 21,481,980 |
| - foreign exchange traded debt funds | 13,233,782 | 15,810,486 | - | 29,044,268 |
| | <u>34,715,762</u> | <u>15,810,486</u> | <u>-</u> | <u>50,526,248</u> |
| Total | <u>36,977,658</u> | <u>15,810,486</u> | <u>-</u> | <u>52,788,144</u> |

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23. Fair values of financial assets and financial liabilities (continued)

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3.

| | Level 1 EUR | Level 2 EUR | Level 3 EUR | Total EUR |
|--|--------------------------|-----------------|-----------------|--------------------------|
| 2015 | | | | |
| Financial assets at fair value through profit or loss | | | | |
| - local listed debt instruments | 2,956,645 | - | - | 2,956,645 |
| - foreign listed debt instruments | 876,055 | - | - | 876,055 |
| | <u>3,832,700</u> | <u>-</u> | <u>-</u> | <u>3,832,700</u> |
| Available-for-sale investments | | | | |
| - foreign listed debt instruments | 8,644,587 | - | - | 8,644,587 |
| | <u>8,644,587</u> | <u>-</u> | <u>-</u> | <u>8,644,587</u> |
| Total | <u>12,477,287</u> | <u>-</u> | <u>-</u> | <u>12,477,287</u> |

The following table provides an analysis of financial instruments that are not measured subsequent to initial recognition at fair value, other than those with carrying amounts that are reasonable approximations of fair value, grouped into Levels 1 to 3

| | Level 1 EUR | Level 2 EUR | Level 3 EUR | Total EUR |
|-------------------------------------|-------------------|------------------|----------------|-------------------|
| 2016 | | | | |
| Held-to maturity investments | | | | |
| - foreign listed debt instruments | 14,007,138 | - | - | 14,007,138 |
| Loans and receivables | | | | |
| - foreign unlisted debt instruments | - | 4,063,521 | - | 4,063,521 |
| | <u>14,007,138</u> | <u>4,063,521</u> | <u>-</u> | <u>18,070,659</u> |
| 2015 | | | | |
| Held-to maturity investments | | | | |
| - foreign listed debt instruments | 17,149,606 | - | - | 17,149,606 |
| Loans and receivables | | | | |
| - foreign unlisted debt instruments | - | 6,457,575 | - | 6,457,575 |
| | <u>17,149,606</u> | <u>6,457,575</u> | <u>-</u> | <u>23,607,181</u> |

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24. Financial risk management

24.1 Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- *Credit risk*: Credit risk stems from the possible non-prompt repayment or non-payment of existing and contingent obligations by the Bank's counterparties, resulting in the loss of equity and profit, as well as risk that deterioration in the financial condition of a borrower will cause the asset value to decrease or be extinguished. Country risk and settlement risk are included in this category. Country risk refers to the risk of losses arising from economic or political changes that affect the country from which the asset originates. Settlement risk refers to the risk of losses through failure of the counterparty to settle outstanding dues on the settlement date owing to bankruptcy or other causes.

- *Market risk*: Risk of losses arising from unfavourable changes in the level and volatility of interest rates, foreign exchange rates or investment prices.

- *Liquidity risk*: Liquidity risk may be divided into two sub-categories:

(1) Market (product) liquidity risk: Risk of losses arising from difficulty in accessing a product or market at the required time, price and amount.

(2) Funding liquidity risk: Risk of losses arising from a timing mismatch between investing, placements and fund raising activities resulting in obligations missing the settlement date or satisfied at higher than normal rates.

- *Operational risk*: Risk of damage resulting from the lack of skilful management or good governance within the Bank and the inadequacy of proper control, which might involve internal operations, personnel, the system or external occurrences that in turn affect the income and capital funds of financial institutions. The Bank has adopted an operational risk management framework and procedures, which provide for the identification, assessment, management, monitoring and reporting of the Bank's operational risks.

The Bank's approach to management of credit, market and liquidity risks is addressed in this note.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

FCM Bank Limited

Notes to the financial statements

31 December 2016

24. Financial risk management (continued)

24.2 Credit risk management

In order to minimise the credit risk undertaken, counterparty credit limits are defined with respect to investment activities, which limits consider a counterparty's creditworthiness, the value of collateral and guarantees pledged, which can reduce the overall credit risk exposure, as well as the type and the duration of the credit asset. In order to examine a counterparty's creditworthiness, country risk, quantitative and qualitative characteristics, as well as the industry sector in which the counterparty operates are considered. The Board of Directors has the final say in the approval process of new and existing assets or credit facilities.

The Bank manages, limits and controls concentrations of credit risk wherever they are identified – in particular, to individual counterparties and groups, and to industries and countries. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one counterparty and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, industry sector and country are approved regularly by the Board of Directors.

The Bank's main exposures to credit risk on financial instruments can be classified in the following categories:

- Financial assets recognised on-balance sheet and cash at bank. The maximum exposure to credit risk of these financial assets equals their carrying amount.

The Bank's credit risk exposures relating to on-balance sheet assets by IAS 39 categorisation, reflecting the maximum exposure to credit risk before collateral held or other credit enhancements are analysed as follows:

| | 2016 | 2015 |
|--|-------------------|-------------------|
| | EUR | EUR |
| Financial assets at fair value through profit and loss | 2,261,896 | 3,795,780 |
| Held-to-maturity investments | 13,603,710 | 17,149,606 |
| Available-for sale investments | 34,715,762 | 8,644,587 |
| Loans and receivables | 4,059,557 | 6,457,575 |
| Cash and cash equivalents | 9,042,019 | 18,388,764 |
| Depositor compensation scheme account with Central Bank of Malta | 460,823 | 310,048 |
| Accrued income | 362,131 | 531,221 |
| Other assets | 40,193 | 136,135 |
| | <u>64,546,091</u> | <u>55,413,716</u> |

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24. Financial risk management (continued)

24.2 Credit risk management (continued)

Concentrations of credit risk

The Bank monitors concentrations of credit risk by sector, industry and by geographical location. An analysis of concentrations of credit risk at the reporting date is shown below:

| | 2016 EUR | 2015 EUR |
|--------------------------------|-------------------|-------------------|
| Concentration by sector | | |
| Central Government | 6,302,066 | 19,460,538 |
| Institutions | 5,462,672 | 3,070,974 |
| Collective investment schemes | 29,044,268 | - |
| Corporates | 23,737,085 | 32,882,204 |
| | <u>64,546,091</u> | <u>55,413,716</u> |

Exposures analysed by location

As at 31 December 2016

| | North America EUR | Europe EUR | Total EUR |
|-------------------------------|----------------------|-------------------|-------------------|
| Central Government | - | 6,302,066 | 6,302,066 |
| Institutions | - | 5,462,672 | 5,462,672 |
| Collective investment schemes | - | 29,044,268 | 29,044,268 |
| Corporates | 1,057,770 | 22,679,315 | 23,737,085 |
| | <u>1,057,770</u> | <u>63,488,321</u> | <u>64,546,091</u> |

As at 31 December 2015

| | North America EUR | Europe EUR | Total EUR |
|--------------------|----------------------|-------------------|-------------------|
| Central Government | - | 18,999,715 | 18,999,715 |
| Institutions | - | 3,531,797 | 3,531,797 |
| Corporates | 1,767,277 | 31,114,927 | 32,882,204 |
| | <u>1,767,277</u> | <u>53,646,439</u> | <u>55,413,716</u> |

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Notes to the financial statements

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24. Financial risk management (continued)

24.2 Credit risk management (continued)

Asset quality

The Bank assigns risk weights to the credit risk of the investments portfolio in accordance with the rating assigned by Fitch, Moody's and S&P, all of which are eligible External Credit Assessment Institutions (ECAIs), in accordance with article 135 of the Capital Requirements Regulation.

The credit quality of the securities as determined by the nominated ECAIs is as follows:

| | 2016 EUR | 2015 EUR |
|--------------|-------------------|-------------------|
| A or higher | 2,266,345 | 839,135 |
| BBB- | - | 11,959,058 |
| BB+ or lower | 23,330,313 | 32,251,768 |
| Total | 25,596,658 | 45,049,961 |

Cash at bank is placed with reliable financial institutions rated BBB and higher.

As at 31 December 2016, the Bank held shares in exchange traded debt funds with a carrying value of EUR29,044,268 (2015: EURNil). The credit risk attributable to this holding depends on the underlying funds' portfolio. 54.53% of the underlying exchange traded debt funds invest predominantly in covered bonds which are rated as Aa1 or higher by Moody whilst the remaining underlying funds invest predominantly in corporate bonds rated between BB+ and B- in accordance with Standard and Poor.

24.3 Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from an inability to sell a financial asset quickly at close to its fair value.

Liquidity risk management

The Bank monitors and manages this risk by maintaining sufficient cash and, where possible, financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs. The Bank is exposed to calls on its available cash resources from maturing term deposits and withdrawals from savings. In order to ensure that maturing funds are always available to meet expected demand for cash, the Board sets parameters within which maturities of assets and liabilities may be mismatched. Unmatched positions potentially enhance profitability, but also increase the risk of losses. In addition, the Bank manages its risk to a shortage of funds by monitoring forecast and actual cash flows, by monitoring the availability of raising funds to meet commitments associated with financial instruments and by holding financial assets which are expected to generate cash inflows that will be available to meet cash outflows on liabilities.

FCM Bank Limited

Notes to the financial statements

31 December 2016

24. Financial risk management (continued)

24.3 Liquidity risk (continued)

The Bank uses four key liquidity measures to monitor its liquidity risk, namely the ratio of liquid assets to deposit liabilities, the maturity ladder which comprises projected cash flows, the Liquidity Coverage Ratio ('LCR'), the Net Stable Funding Ratio ('NSFR') and an internal cash flow model, which is a minimum buffer of liquid assets set based on expected gross outflows.

As at both 31 December 2016 and 31 December 2015, the Bank's liquidity ratios were significantly above the regulatory liquidity ratios of 30% prescribed by Banking Rule 5 and 60% prescribed by the Capital Requirements Regulation.

The table below analyses the Bank's financial liabilities into relevant maturity groupings, based on the remaining period at the reporting date to the contractual maturity date

| | Carrying amount EUR | Gross outflow/(inflow) EUR | Less than 1 month EUR | 1-3 months EUR | 3 months - 1 year EUR | 1-5 years EUR |
|----------------------------|------------------------|-------------------------------|--------------------------|-------------------|--------------------------|------------------|
| At 31 December 2016 | | | | | | |
| Deposits from customers | (56,849,001) | (56,849,001) | (4,511,669) | (3,411,091) | (9,827,834) | (39,098,407) |
| At 31 December 2015 | | | | | | |
| Deposits from customers | (48,906,650) | (49,495,912) | (3,788,882) | (3,140,944) | (10,254,850) | (32,311,235) |

Assets available to meet these liabilities, and to cover outstanding commitments, include cash at bank and marketable securities.

The table below analyses the principal assets and liabilities that are recognised in the statement of financial position into relevant maturity groupings, based on the remaining period at balance sheet date to their contractual maturity date.

| | Less than 3 months EUR | 3 months - 1 year EUR | 1-5 years EUR | 5+ years EUR | Other EUR | Total EUR |
|--|---------------------------|--------------------------|-------------------|------------------|-------------------|---------------------|
| As at 31 December 2016 | | | | | | |
| Financial Assets at fair Value through profit or loss | 2,261,896 | - | - | - | - | 2,261,896 |
| Available-for-sale investments | - | - | 3,449,419 | 2,222,075 | 29,044,268 | 34,715,762 |
| Held-to-maturity investments | - | - | 12,315,649 | 1,288,061 | - | 13,603,710 |
| Loans and receivables | - | - | 2,079,215 | 1,980,342 | - | 4,059,557 |
| Cash and Cash equivalents | 9,042,019 | - | - | - | - | 9,042,019 |
| Depositor compensation scheme account with Central Bank of Malta | - | - | - | - | 460,823 | 460,823 |
| Accrued income | 362,131 | - | - | - | - | 362,131 |
| Other assets | 40,193 | - | - | - | - | 40,193 |
| | <u>11,706,239</u> | <u>-</u> | <u>17,844,283</u> | <u>5,490,478</u> | <u>29,505,091</u> | <u>64,546,091</u> |
| Liabilities | | | | | | |
| Amounts owed to customers | <u>7,922,760</u> | <u>9,827,834</u> | <u>39,098,408</u> | <u>-</u> | <u>-</u> | <u>(56,849,001)</u> |

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Notes to the financial statements

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24. Financial risk management (continued)

24.3 Liquidity risk (continued)

| | Less than 3 months EUR | 3 months - 1 year EUR | 1-5 years EUR | 5+ years EUR | Other EUR | Total EUR |
|---|------------------------------|-----------------------------|---------------------|--------------------|----------------|-------------------|
| As at 31 December 2015 | | | | | | |
| Financial Assets at Fair Value | | | | | | |
| through profit or loss | 3,795,780 | - | - | - | - | 3,795,780 |
| Available-for-sale investments | - | - | 2,727,946 | 5,916,641 | - | 8,644,587 |
| Held-to-maturity investments | - | - | 12,384,324 | 4,765,282 | - | 17,149,606 |
| Loans and receivables | - | - | 3,433,621 | 3,023,954 | - | 6,457,575 |
| Cash and Cash equivalents | 18,388,764 | - | - | - | - | 18,388,764 |
| Depositor compensation scheme account with Central Bank of Malta | - | - | - | - | 310,048 | 310,048 |
| Accrued income | 531,221 | - | - | - | - | 531,221 |
| Other assets | 136,135 | - | - | - | - | 136,135 |
| | <u>22,851,900</u> | <u>-</u> | <u>18,545,891</u> | <u>13,705,877</u> | <u>310,048</u> | <u>55,413,716</u> |
| Liabilities | | | | | | |
| Amounts owed to customers | <u>6,819,006</u> | <u>10,190,315</u> | <u>31,897,329</u> | <u>-</u> | <u>-</u> | <u>48,906,650</u> |

24.4 Market risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's/issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Exposure to interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or in different amounts. Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with the Bank's business strategies.

Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for re-pricing bands.

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24. Financial risk management (continued)

24.4 Market risk (continued)

Exposure to interest rate risk (continued)

The following table sets out the carrying amount, by reference to the earlier of the next contractual interest rate re-pricing date and maturity of interest bearing financial instruments:

| | Less than 3 months EUR | 3 months - 1 year EUR | 1-5 years EUR | 5+ years EUR | Others EUR | Total EUR |
|--|------------------------------|-----------------------------|---------------------|--------------------|----------------|-------------------|
| At 31 December 2016 | | | | | | |
| Financial assets at fair value through profit or loss | 142,099 | 31,097 | 925,313 | 1,163,387 | - | 2,261,896 |
| Available-for-sale investments | 1,171,413 | 29,043,667 | 2,270,788 | 2,229,895 | - | 34,715,762 |
| Loans and receivables | 4,059,567 | - | - | - | - | 4,059,567 |
| Held-to-maturity investments | 1,000,337 | - | 11,321,349 | 1,282,024 | - | 13,603,710 |
| Cash and cash equivalents | 9,042,019 | - | - | - | - | 9,042,019 |
| Depositor compensation scheme account with Central Bank of Malta | - | - | - | - | 460,823 | 460,823 |
| Accrued income | - | - | - | - | 362,131 | 362,131 |
| Other assets | - | - | - | - | 40,193 | 40,193 |
| | 15,415,425 | 29,074,764 | 14,517,450 | 4,675,306 | 863,147 | 64,546,091 |
| Liabilities | | | | | | |
| Amounts owed to customers | 7,922,760 | 9,827,834 | 39,098,408 | - | - | 56,849,001 |
| Gap | 7,492,665 | 19,246,930 | (24,580,958) | 4,675,306 | 863,147 | |
| Cumulative Gap | 7,492,665 | 26,739,595 | 2,158,637 | 6,833,943 | 7,697,090 | |
| At 31 December 2015 | | | | | | |
| Financial assets at fair value through profit or loss | - | 1,740,801 | 397,722 | 1,657,257 | - | 3,795,780 |
| Available-for-sale investments | 1,285,123 | - | 1,453,918 | 5,905,546 | - | 8,644,587 |
| Loans and receivables | 6,457,575 | - | - | - | - | 6,457,575 |
| Held-to-maturity investments | 2,010,024 | 3,378,963 | 6,981,813 | 4,778,806 | - | 17,149,606 |
| Cash and cash equivalents | 18,388,764 | - | - | - | - | 18,388,764 |
| Depositor compensation scheme account with Central Bank of Malta | - | - | - | - | 310,048 | 310,048 |
| Accrued income | - | - | - | - | 531,221 | 531,221 |
| Other assets | - | - | - | - | 136,135 | 136,135 |
| | 28,141,486 | 5,119,764 | 8,833,453 | 12,341,609 | 977,404 | 55,413,716 |
| Liabilities | | | | | | |
| Amounts owed to customers | 6,819,006 | 10,190,315 | 31,897,329 | - | - | 48,906,650 |
| Gap | 21,322,479 | (5,070,551) | (23,063,876) | 12,341,609 | 977,404 | |
| Cumulative gap | 21,322,479 | 16,251,929 | (6,811,947) | 5,529,662 | 6,507,066 | |

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Notes to the financial statements

31 December 2016

24. Financial risk management (continued)

24.4 Market risk (continued)

At the end of the reporting period the interest rate profile of the Bank's interest bearing financial instruments was as follows:

| | Rate Instruments | |
|---|---------------------|--------------------|
| | Fixed | Variable |
| | EUR | EUR |
| As at 31 December 2016 | | |
| Interest earning assets | | |
| Financial assets at fair value through profit or loss | 2,261,896 | - |
| Available-for-sale investments | 4,500,081 | 1,171,413 |
| Held-to-maturity investments | 12,603,373 | 1,000,337 |
| Loans and receivables | - | 4,059,557 |
| Cash and cash equivalents | - | 9,042,019 |
| | <u>19,365,350</u> | <u>15,273,326</u> |
| Interest bearing liabilities | | |
| Amounts owed to customers | <u>(56,849,001)</u> | <u>(1,414,053)</u> |
| As at 31 December 2015 | | |
| Interest earning assets | | |
| Financial assets at fair value through profit or loss | 3,795,780 | - |
| Available-for-sale investments | 7,359,464 | 1,285,123 |
| Held-to-maturity investments | 15,139,582 | 2,010,024 |
| Loans and receivables | - | 6,457,575 |
| Cash and cash equivalents | 9,696,399 | 8,692,365 |
| | <u>35,991,225</u> | <u>18,445,087</u> |
| Interest bearing liabilities | | |
| Amounts owed to customers | <u>47,492,597</u> | <u>1,414,053</u> |
| | <u>47,492,597</u> | <u>1,414,053</u> |

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Notes to the financial statements

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24. Financial risk management (continued)

24.4 Market risk (continued)

For financial instruments held or issued, the Bank has used a sensitivity analysis technique that measures the change in the fair value and cash flows of the Bank's financial instruments at the end of the reporting period for hypothetical changes in the relevant market risk variables. The sensitivity due to changes in the relevant risk variables is set out below. The amounts generated from the sensitivity analysis are forward-looking estimates of market risk assuming certain market conditions. Actual results in the future may differ materially from those projected results due to the inherent uncertainty of global financial markets. The sensitivity analysis is for illustrative purposes only, as in practice market rates rarely change in isolation and are likely to be interdependent.

The net effect of an immediate 200 basis point increase/decrease in yields at the end of 2016 was estimated at EUR131,787 (EUR117,533 at the end of 2015).

Exposure to foreign currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Board of Directors sets limits on the level of exposure by currency and in total.

The Bank was not materially exposed to currency risk through transactions in foreign currencies at the end of the reporting period.

Price risk

Price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

24.5 Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risk such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Bank's operations.

FCM Bank Limited

Notes to the financial statements

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24. Financial risk management (continued)

24.5 Operational risk (continued)

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management. This responsibility is supported by the development of overall standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions
- requirements for the reconciliation and monitoring of transactions
- compliance with regulatory and other legal requirements
- documentation of controls and procedures
- requirements for the periodic assessment of operational risks faced and the adequacy of controls and procedures to address the risks identified
- requirements for the reporting of operational losses and proposed remedial action
- development of contingency plans
- training and professional development
- ethical and business standards
- risk mitigation, including insurance where this is effective.

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risk such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Bank's operations.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management. This responsibility is supported by the development of overall standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions
- requirements for the reconciliation and monitoring of transactions
- compliance with regulatory and other legal requirements
- documentation of controls and procedures
- requirements for the periodic assessment of operational risks faced and the adequacy of controls and procedures to address the risks identified
- requirements for the reporting of operational losses and proposed remedial action
- development of contingency plans
- training and professional development
- ethical and business standards
- risk mitigation, including insurance where this is effective.

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Notes to the financial statements

31 December 2016

24. Financial risk management (continued)

24.6 Capital risk management (continued)

On 1 January 2014 the Capital Requirements Directive (CRD) and the Capital Requirements Regulations (CRR) came into effect, constituting the European implementation of the Basel capital and liquidity agreement of 2010. The Bank has made necessary changes in order to ensure that it is compliant with Pillar I capital requirements set by the CRR. Other material risks are also allocated capital as part of the Internal Capital Adequacy Process (ICAAP) embedded in the Pillar II process. This process helps to measure with greater risk sensitivity the amount of regulatory capital which the Bank requires to cover risks assumed in the course of its business, including risks not covered in Pillar I.

During the financial year, the Bank has monitored adequacy of its capital and gave strategic direction on the most efficient use of capital.

During the year under review and during the comparative period, the Bank has complied with the externally imposed capital requirements.

The following table shows the components and basis of calculation of the Bank's capital adequacy ratios:

| | 2016 | 2015 |
|--|-------------------------|-------------------------|
| | EUR | EUR |
| Original own funds | | |
| Ordinary shares | 12,250,000 | 10,350,000 |
| Accumulated losses | (4,192,950) | (2,994,339) |
| Depositor compensation reserve | (460,823) | (310,048) |
| Investment revaluation reserve | 123,879 | (181,675) |
| Deductions | | |
| Intangible assets | (191,995) | (217,768) |
| Deferred tax assets that rely on future profitability and arise from temporary differences | (839,974) | (1,003,045) |
| Other transitional adjustments | 418,168 | 700,622 |
| Total Tier 1 Capital | <u>7,106,305</u> | <u>6,343,747</u> |
| Total own funds | <u><u>7,106,305</u></u> | <u><u>6,343,747</u></u> |

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Notes to the financial statements

31 December 2016

24. Financial risk management (continued)

24.6 Capital risk management (continued)

Minimum capital requirements are computed for credit, market and operational risks. The MFSA requires a bank to maintain a ratio of total regulatory capital to risk-weighted assets and instruments (the capital requirements ratio) at or above the prescribed minimum of 8%. The capital requirements ratio expresses own funds as a proportion of risk-weighted assets and off-balance sheet items in relation to credit risk together with notional risk-weighted assets in respect of operational risk and market risk.

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposures, with some adjustments to reflect the more contingent nature of the potential losses. Risk-weighted assets are measured using the 'standardised approach' for credit risk with risk weights being assigned to assets and off-balance sheet items according to their asset class and credit assessment. For the determination of credit assessments, independent rating agencies are nominated as required.

Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 (i.e. the reciprocal of the minimum capital ratio of 8 per cent) and adding the resulting figures to the sum of risk-weighted assets for credit risk.

The capital adequacy ratio at 31 December 2016 stood at 15.9% (15.27% at 31 December 2015).

25. Contingent liability

The Bank has received a litigation claim from a former member of staff relating to alleged unfair dismissal. The Bank is of the opinion this claim will not succeed but in the unlikely event of the decision going against the Bank, any award is not thought to be material.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

1. Risk management

1.1 Overview of risk disclosures

These disclosures have been prepared in accordance with the Pillar 3 quantitative and qualitative disclosure requirements as governed by Banking Rule 07: Publication of Annual report and Audited Financial Statements of Credit Institutions BR/07/2014 authorised under the Banking Act, 1994, issued by the Malta Financial Services Authority. These disclosures will be published by the Bank on an annual basis as part of the Annual Report.

As per banking regulations, this report is not subject to an external audit, except to the extent that any disclosures are equivalent to those made in the Financial Statements which adhere to International Financial Reporting Standards (IFRS) as adopted by the EU. The Bank is satisfied that internal verification procedures ensure that these Additional Regulatory Disclosures are presented fairly.

In accordance with the Bank's Pillar 3 disclosure policy which sets out the disclosure process, verification and frequency, this report is currently published once a year.

1.2 Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Bank has in place a Credit and Risk Committee that is responsible for developing and monitoring the Bank's risk management policies in its specific areas. The Credit and Risk Committee met 12 times in 2015. The aim of risk management is to create value for shareholders by supporting the Bank in achieving its goals and objectives, and ultimately ensuring that the risks are commensurate with the rewards.

The Bank considers risk management a core competency that helps produce consistently high returns for its various stakeholders. The Bank's business involves taking on risks in a targeted manner and managing them professionally. The Bank aims to manage all major types of risk by applying methods that meet best practice. The Bank considers it important to have a clear distribution of responsibilities within risk management. One of the main tasks of the Bank's executive management is to set the framework for this area. The core functions of the Bank's risk management are to identify all key risks for the Bank, measure these risks, manage the risk positions and determine capital allocations. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and best market practice.

1.3 Key risk components

The Bank's Board of Directors is empowered to set out the overall risk policies and limits for all material risk types. The Board also decides on the general principles for managing and monitoring risks.

To ensure coherence between the Bank's strategic considerations regarding risk-taking and day-to-day decisions, from time to time, the Bank establishes risk appetite as a strategic tool. Risk appetite is the maximum risk that the Bank is willing to assume to meet business targets. The Bank's risk appetite is set in a process based on a thorough analysis of its current risk profile. The Bank identifies a number of key risk components and for each, determines a target that represents the Bank's perception of the component in question.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

1. Risk management (continued)

1.3 Key risk components (continued)

The Bank has exposure to the following risks from its use of financial instruments:

- *Credit risk*: Credit risk stems from the possible non-prompt repayment or non-payment of existing and contingent obligations by the Bank's counterparties, resulting in the loss of equity and profit, as well as risk that deterioration in the financial condition of a borrower will cause the asset value to decrease or be extinguished. Country risk and settlement risk are included in this category. Country risk refers to the risk of losses arising from economic or political changes that affect the country from which the asset originates. Settlement risk refers to the risk of losses through failure of the counterparty to settle outstanding dues on the settlement date owing to bankruptcy or other causes.

- *Market risk*: Market risk is the risk of reductions in earnings and/or asset values arising from unexpected changes in financial prices, including interest rates, exchange rates and equity prices. It is managed by a variety of different techniques.

- *Liquidity risk*: Liquidity risk may be divided into two sub-categories:

(1) Market (product) liquidity risk: Risk of losses arising from difficulty in accessing a product or market at the required time, price and amount.

(2) Funding liquidity risk: Risk of losses arising from a timing mismatch between investing, placements and fund raising activities resulting in obligations missing the settlement date or satisfied at higher than normal rates.

- *Operational risk*: Risk of damage resulting from the lack of skilful management or good governance within the Bank and the inadequacy of proper control, which might involve internal operations, personnel, the system or external occurrences that in turn affect the income and capital funds of financial institutions. The Bank has adopted an operational risk management framework and procedures, which provide for the identification, assessment, management, monitoring and reporting of the Bank's operational risks.

2. Credit risk

Credit risk is the risk of suffering financial loss, should any of the Bank's customers, clients or market counterparties fail to fulfil their contractual obligations to the Bank. Credit risk arises from deposits with other banks and on its securities portfolio.

The Credit and Risk Committee is responsible for approving all acquisitions of securities and placements of deposits with banks. In accordance with policies set by the Board decisions are based on the Bank's insight into the counterparty's financial position which is regularly monitored and reported to the Board.

In order to minimise the credit risk undertaken, counterparty credit limits are defined, which consider a counterparty's creditworthiness. In order to examine a counterparty's creditworthiness, country risk, quantitative and qualitative characteristics, as well as the industry sector in which the counterparty operates are considered.

Concentration risk arises as a result of the concentration of exposures within the same category, whether it is geographical locations, industry sector or counterparty type. These risks are managed through adherence to Board approved investment criteria. As at 31 December 2016, no securities were deemed to be prohibited large exposures.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

2. Credit risk (continued)

Country risk

The Bank runs the risk of loss of funds due to the possible political, economic and other events in a particular country where funds have been placed or invested with several counterparties. Countries are assessed according to their size, economic data and prospects and their credit ratings from international rating agencies. Existing country credit risk exposures are monitored and reviewed periodically.

Exposures analysed by location

| | North America EUR | Europe EUR | Total EUR |
|-------------------------------|----------------------|-------------------|-------------------|
| Central government | - | 6,302,066 | 6,302,066 |
| Institutions | - | 5,462,672 | 5,462,672 |
| Collective investment schemes | - | 29,044,268 | 29,044,268 |
| Corporate | 1,057,770 | 22,679,315 | 23,737,085 |
| | <u>1,057,770</u> | <u>63,488,321</u> | <u>64,546,091</u> |

Exposures analysed by residual maturity

| | Less than 1 year EUR | 1-5 years EUR | 5+ years EUR | Other EUR | Total EUR |
|-------------------------------|----------------------------|-------------------|------------------|-------------------|-------------------|
| Central Government | 3,752,543 | 925,313 | 1,163,387 | 460,823 | 6,302,066 |
| Institutions | 5,462,672 | - | - | - | 5,462,672 |
| Collective investment schemes | - | - | - | 29,044,268 | 29,044,268 |
| Corporate | 402,324 | 17,844,283 | 5,490,478 | - | 23,737,085 |
| | <u>9,617,539</u> | <u>18,769,596</u> | <u>6,653,865</u> | <u>29,505,091</u> | <u>64,546,091</u> |

Exposures analysed by sector

| | Central government EUR | Institutions EUR | Corporate EUR | Collective investment schemes EUR | Total EUR |
|-------------------------------|------------------------------|---------------------|-------------------|--|-------------------|
| Central Government | 6,302,066 | - | - | - | 6,302,066 |
| Institutions | - | 5,462,672 | - | - | 5,462,672 |
| Collective investment schemes | - | - | - | 29,044,268 | 29,044,268 |
| Corporate | - | - | 23,737,085 | - | 23,737,085 |
| | <u>6,302,066</u> | <u>5,462,672</u> | <u>23,737,085</u> | <u>29,044,268</u> | <u>64,546,091</u> |

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

2. Credit risk (continued)

Asset quality

The Bank assigns risk weights to the credit risk of its assets in accordance with the rating assigned by Fitch, Moody's and S&P, all of which are MFSA eligible External Credit Assessment Institutions (ECAIs), in accordance with article 3.9 of Appendix 2 – Section 1.4 Credit Risk Standardised Approach – BR 04.

The credit quality of the securities as determined by the nominated ECAIs is as follows:

| | Central Government EUR | Institutions EUR | Collective investment schemes EUR | Corporate EUR | Total EUR |
|-----------------------|------------------------------|---------------------|--|------------------|-------------------|
| Credit Quality Step 1 | - | 381,753 | 6,942,916 | - | 7,324,669 |
| Credit Quality Step 2 | 5,924,762 | - | - | - | 5,924,762 |
| Credit Quality Step 3 | - | 3,087,192 | 886,276 | - | 3,973,468 |
| Credit Quality Step 4 | - | 2,375,480 | 7,660,955 | 16,570,443 | 26,606,878 |
| Credit Quality Step 5 | - | - | 3,692,980 | 6,657,592 | 10,350,572 |
| Credit Quality Step 6 | - | - | 316,326 | 103,480 | 419,806 |
| Not rated | - | - | 9,543,613 | 402,324 | 9,945,937 |
| | | | | | <u>64,546,092</u> |

3. Market risk

Market risk for the Bank consists of three elements:

- Interest rate risk, which is the risk of losses through changes in interest rates;
- Currency risk, which is the risk of losses on the Bank's positions in foreign currency through changes in exchange rates; and
- Price risk which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

3.1 Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or at different amounts. The Bank places deposits with Banks at both fixed and floating rates and for varying maturity periods. This risk is managed through the matching of the interest resetting dates on assets and liabilities as much as it is practicable. However, the Bank seeks to manage its net interest spread, after considering the cost of capital by investing funds in a portfolio of securities with a longer tenure than the liabilities (therefore carrying a negative maturity gap position).

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

3. Market risk (continued)

3.1 Interest rate risk (continued)

The net effect of an immediate 200 basis point increase/decrease in yields at the end of 2016 was estimated at *EUR131,787* (*EUR117,533* at the end of 2015).

At the end of the reporting period the interest rate profile of the Bank's interest bearing financial instruments is as follows:

| | Fixed EUR | Variable EUR |
|---|--------------|-----------------|
| As at 31 December 2016 | | |
| Interest earning assets | | |
| Financial Assets at fair value through profit or loss | 2,261,896 | - |
| Available-for-sale investments | 4,500,081 | 1,171,413 |
| Held-to-maturity investments | 12,603,373 | 1,000,337 |
| Loans and receivables | - | 4,059,557 |
| Cash and cash equivalents | | 9,042,019 |
| | 19,365,350 | 15,273,326 |

The following table sets out the carrying amount, by reference to the earlier of the next contractual interest rate repricing date and maturity:

| | Less than 3 months EUR | 3 months - 1 year EUR | 1-5 years EUR | 5+ years EUR | Others EUR | Total EUR |
|--|------------------------------|-----------------------------|---------------------|--------------------|---------------|--------------|
| At 31 December 2016 | | | | | | |
| Financial assets at fair value through profit or loss | 142,099 | 31,097 | 925,313 | 1,163,387 | - | 2,261,896 |
| Available-for-sale investments | 1,171,413 | 29,043,667 | 2,270,788 | 2,229,895 | - | 34,715,762 |
| Loans and receivables | 4,059,557 | - | - | - | - | 4,059,557 |
| Held-to-maturity investments | 1,000,337 | - | 11,321,349 | 1,282,024 | - | 13,603,710 |
| Cash and cash equivalents | 9,042,019 | - | - | - | - | 9,042,019 |
| Depositor compensation scheme account with Central Bank of Malta | - | - | - | - | 460,823 | 460,823 |
| Accrued income | - | - | - | - | 362,131 | 362,131 |
| Other assets | - | - | - | - | 40,193 | 40,193 |
| | 15,415,425 | 29,074,764 | 14,517,460 | 4,675,306 | 863,147 | 64,546,091 |
| Liabilities | | | | | | |
| Amounts owed to customers | 7,922,760 | 9,827,834 | 39,098,408 | - | - | 56,849,001 |
| | 7,922,760 | 9,827,834 | 39,098,408 | - | - | 56,849,001 |
| Gap | 7,492,665 | 19,246,930 | (24,580,958) | 4,675,306 | 863,147 | |
| Cumulative Gap | 7,492,665 | 26,739,595 | 2,158,637 | 6,833,943 | 7,697,090 | |

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

3. Market risk (continued)

3.2 Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Board of Directors sets limits on the level of exposure by currency and in total.

The Bank was not exposed to significant currency risk through transactions in foreign currencies at the end of the reporting period.

4. Liquidity risk

Liquidity risk is defined as the risk of losses due to:

- the Bank's funding costs increasing disproportionately;
- lack of funding prevents the Bank from establishing new business; and
- lack of funding will ultimately prevent the Bank from meeting its obligations.

Liquidity risk may result from an inability to sell a financial asset quickly at close to its fair value. The objective of the Bank's liquidity and funding management is to ensure that all foreseeable funding commitments and deposit withdrawals can be met when due. It is the Bank's objective to maintain a diversified and stable funding base with the objective of enabling the Bank to respond quickly and smoothly to unforeseen liquidity requirements.

The Bank manages this risk by ensuring that its assets and liabilities are matched in terms of maturities as much as is practicable. The Bank holds significant liquid assets in the form of cash and bonds. In order to ensure that maturing funds are always available to meet unexpected demand for cash, the Board sets parameters within which maturities of assets and liabilities may be mismatched. Unmatched positions potentially enhance profitability, but also increase the risk of losses. The Board of Directors monitors the Bank's Liquidity Gap analysis on a monthly basis. In addition, it maintains an on-going oversight of forecast and actual cash flows, by monitoring the availability of funds to meet commitments associated with financial instruments.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

4. Liquidity risk (continued)

The table below analyses Bank financial assets and financial liabilities into relevant maturity groupings, based on the remaining period at the reporting date to the contractual maturity date.

| | Less than 3 months EUR | 3 months - 1 year EUR | 1-5 years EUR | 5+ years EUR | Total EUR |
|---|------------------------------|-----------------------------|---------------------|--------------------|-------------------|
| As at 31 December 2016 | | | | | |
| Financial Assets at fair value through profit or loss | 2,261,896 | - | - | - | 2,261,896 |
| Available-for-sale investments | - | - | 32,493,687 | 2,222,075 | 34,715,762 |
| Held-to-maturity investments | - | - | 12,315,649 | 1,288,061 | 13,603,710 |
| Loans and receivables | - | - | 2,079,215 | 1,980,342 | 4,059,557 |
| Cash and cash equivalents | 9,502,842 | - | - | - | 9,502,842 |
| Accrued income | 362,131 | - | - | - | 362,131 |
| Other assets | 40,193 | - | - | - | 40,193 |
| | <u>12,167,062</u> | <u>-</u> | <u>46,888,551</u> | <u>5,490,478</u> | <u>64,546,091</u> |
| Liabilities | | | | | |
| Amounts owed to customers | <u>7,922,760</u> | <u>9,827,834</u> | <u>39,098,407</u> | <u>-</u> | <u>56,849,001</u> |

Assets available to meet these liabilities, and to cover outstanding commitments, include cash deposits and marketable securities.

5. Operational risk

Operational risk is the risk of direct or indirect losses arising from a variety of causes associated with the Bank's processes such as:

- deficient or erroneous internal procedures
- human or system errors
- external events, including legal events
- internal and external fraud
- employment practices and workplace safety
- clients, products and business practices
- damage to physical assets
- business disruption and system failures
- execution, delivery and process management

Operational risk is thus often associated with specific and one-off events, such as failure to observe business or working procedures, defects or breakdowns of the technical infrastructure, criminal acts, fire and storm damage or litigation.

Operational risks are, thus, non-financial risks. Operational risk management relies on a framework of policies overseen by the Board of Directors.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

5. Operational risk (continued)

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity while maintaining risk taking within a tolerable limit.

A financial measurement of this risk is arrived at by the Bank for the purpose of allocating risk capital using the Basic Indicator Approach. The capital requirement for operational risk under this method was calculated at *EUR43,221*.

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the consolidated statement of financial position, are:

- To comply with the capital requirements set by the Malta Financial Services Authority (MFSA) with respect to the Bank's operations;
- To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

Accordingly, the purpose of the Bank's capital management is essentially that of ensuring efficient use of capital taking cognisance of the Bank's risk appetite and profile as well as its objectives for business development.

6. Capital management

6.1 Capital adequacy

The Bank is subject to externally imposed capital requirements only in respect of the Bank's activities as a credit institution.

On 1 January 2014 the Capital Requirements Directive (CRD) and the Capital Requirements Regulations (CRR) came into effect, constituting the European implementation of the Basel capital and liquidity agreement of 2010. The Bank has made necessary changes in order to ensure that it is compliant with Pillar I capital requirements set by the CRR. Other material risks are also allocated capital as part of the Internal Capital Adequacy Process (ICAAP) embedded in the Pillar II process. This process helps to measure with greater risk sensitivity the amount of regulatory capital which the Bank requires to cover risks assumed in the course of its business, including risks not covered in Pillar I.

The following is an analysis of the Bank's capital base in accordance with the CRD's requirements:

Minimum capital requirements are computed for credit, market and operational risks. The MFSA requires a bank to maintain a ratio of total regulatory capital to risk-weighted assets and instruments (the capital requirements ratio) at or above the prescribed minimum of 8%. The capital requirements ratio expresses own funds as a proportion of risk-weighted assets and off-balance sheet items in relation to credit risk together with notional risk-weighted assets in respect of operational risk and market risk.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

6. Capital management (continued)

6.1 Capital adequacy (continued)

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposures, with some adjustments to reflect the more contingent nature of the potential losses. Risk-weighted assets are measured using the 'standardised approach' for credit risk with risk weights being assigned to assets and off-balance sheet items according to their asset class and credit assessment. For the determination of credit assessments, independent rating agencies are nominated as required.

Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 (i.e. the reciprocal of the minimum capital ratio of 8 per cent) and adding the resulting figures to the sum of risk-weighted assets for credit risk.

| | Carrying Amount EUR | Risk Weighted Amount EUR | Capital Requirement EUR |
|----------------------------------|------------------------------------|---|--|
| Central governments | 6,302,066 | - | - |
| Institutions | 5,462,672 | 1,092,534 | 87,403 |
| Corporates | 23,737,085 | 27,125,593 | 2,170,044 |
| Collective Investment schemes | 29,044,268 | 15,043,079 | 1,203,446 |
| Other items | 1,206,083 | 641,834 | 51,347 |
| Total credit risk | 65,752,174 | 43,903,040 | 3,512,243 |
| Foreign exchange risk | | - | - |
| Operational risk | | 540,267 | 43,221 |
| Total | | 44,443,307 | 3,565,173 |
| Own funds | | 7,106,305 | |
| Capital adequacy ratio | | 15.99% | |

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

6. Capital management (continued)

6.2 Internal capital adequacy assessment process (ICAAP)

The Bank developed a comprehensive Internal Capital Adequacy Assessment Process ("ICAAP"), as part of its 2012 plan to enhance its risk management process, in accordance with Banking Rule 12 'The Supervisory Review Process' (BR12). As part of this process, the Bank is required to assess its overall capital adequacy in relation to risk profile and a strategy for maintaining capital levels.

The purpose of the ICAAP is to formalise the process by which the Bank performs ongoing assessment of its risks, mitigates those risks and determines how much current and future capital is necessary having considered other mitigating factors.

The ICAAP has therefore been adopted by both the Board of Directors and the Bank's senior management to ensure that there is adequate identification, measurement and monitoring of the Bank's risks and that adequate internal capital is held by the Bank in relation to its risk profile. Furthermore, the Bank has utilised this ICAAP to assess its current risk management practices and to determine those practices which need to be developed further.

For this ICAAP, the Bank adopted a minimum capital requirement approach, using the audited figures as at 31 December 2014 as the benchmark year, which is based on Pillar I capital requirements together with the assessment of extra capital proportionate to Pillar II risks and supplementary stress testing to assess the impact of a possible prolonged economic recession on the Bank.

The ICAAP process was led by the Bank's Directors, and was challenged by the internal auditors. The final document was approved by the Bank's Board of Directors in June 2015 and presented to the MFSA.

The results show the Bank comfortably meeting its capital and liquidity targets over the regulatory minimum even in times of stress.

7 Remuneration Policy

The Bank's Remuneration Policy is based on the following principles:

- Clarity and transparency for all stakeholders;
- Adherence to the Bank's long-term objectives with reference to the relevant level of risk involved in attaining these goals;
- Maintaining a reasonable proportion between the fixed and variable part of remuneration package;
- The review of the annual staff remuneration considers the Bank's results, performance, as well as local market trends in the financial sector and individual performance in view of the risk level involved in the long term;
- Market data is considered and target remuneration brackets per job position are set in view to level of expertise, years in the position, attraction of talent and high performers.
- European Banking Authority Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

7 Remuneration Policy (continued)

Total remuneration payable to senior management, which includes the CEO and three other beneficiaries, in 2016 was *EUR354,638* of which *EUR322,638* was fixed and *EUR22,000* variable. No variable remuneration awarded during the year was deferred.

FCM has appointed a Remuneration Committee whose objective is to ensure that all remuneration, including benefits and variable remuneration, follows legal requirements and market rates. All members appointed on the Remuneration Committee are not management members except for the CEO, whose membership is ex-officio. The Remuneration Committee meets at least twice a year and minutes are formally kept by the Company Secretary. The Remuneration Committee undertakes periodic studies into compensation market rates, including variable rates, and other benefits. All variable compensation for senior management is submitted to be authorised by the Remuneration Committee. The Remuneration Policy is subject to the Remuneration Committee's scrutiny and authorisation.

FCM will determine the employee's remuneration and benefits by reference to market rates for specific roles and FCM's own needs at a particular time. Remuneration for senior management staff is recommended to the Remuneration Committee for authorisation. FCM incentive schemes are tied to the performance evaluation system and will always be subject to the Remuneration Committee's approval on the basis of a structured and measured approach, which must be tied to the adoption of sound operating procedures and risk practices. FCM will not implement incentive schemes which will encourage its management and employees to commit FCM to take on risks which in the view of the Board of Directors are not in line with the risk profile of FCM. FCM will also not implement incentive schemes which will constrain or endanger its financial position or capital base.

1. Variable remuneration will not encourage excessive risk-taking beyond the tolerated risk level of FCM;
2. Variable remuneration will be in line with business strategy, long-term bank objectives and the avoidance of conflicts of interest.
3. The implementation of basic remuneration policy (salaries) is subject to the Remuneration Committee's authorisation both at contracting stage and at periodic increase stage. The implementation of the variable remuneration policy is subject to the Remuneration Committee's scrutiny and authorisation both at initial stages, when drawing up performance targets and measures, and at recommendation stage, prior to decisions made on variable remuneration levels.
4. Staff in control functions are independent from the business units they oversee and are remunerated according to independent market rates and according to the targets and measures included in their performance evaluation forms.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

7 Remuneration Policy (continued)

Variable remuneration shall be subject to FCM's overall performance, to the achievement of targets previously established, which targets include behavioural objectives and to the following considerations:

1. FCM does not offer guaranteed variable remuneration unless the latter is part of the initial contracting process, which would only happen as a one-off factor during the first year of employment.
2. The total variable remuneration value shall not in any manner constrain FCM's capital base.
3. The total level of variable remuneration shall not exceed 25% of the level of basic salary, unless specifically authorised by the Board of Directors in exceptional circumstances. In the case of the latter, such a decision would not constrain FCM's capital base and would not be higher than 50% of basic salary.
4. Variable remuneration of the most senior Bank officers may be set in a multi-year framework which will take into consideration FCM's longer-term performance and its underlying business cycle. This may include variable remuneration being settled over a period of years corresponding to FCM's business cycle.

8 Recruitment policy

FCM is an equal opportunity employer and will not discriminate between candidates on grounds of race, religion, sex, status and disability. FCM will strive to identify candidates who are best suited to the post on the basis of their academic achievements, work experience and career history.

9 Internal audit

The Bank outsources its Internal Audit function to an independent professional services firm. The Internal Auditors support the Board of Directors by independently assessing the effectiveness of the Bank's system of internal controls and compliance of the Bank with statutory, legal and regulatory requirements. All key issues raised by Internal Audit are communicated to the management responsible via formal audit reports. The Audit Committee and Board of Directors are informed of findings and actions being taken to implement improvements.

The Internal Auditors have unrestricted access to all accounts, books and records and are provided with all information and data needed to fulfil their duties. Coordination and close cooperation with the external auditors plays an important role to enhance the efficiency of Internal Audit's work.

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

10 Encumbered and unencumbered assets

| | Carrying amount of encumbered assets EUR | Fair value of encumbered assets EUR | Carrying amount of unencumbered assets EUR | Fair value of unencumbered assets EUR |
|---------------------|---|--|---|--|
| At 31 December 2016 | | | | |
| Equity | - | - | 29,044,268 | 29,044,268 |
| Debt securities | - | - | 25,596,657 | 25,997,799 |
| Other assets | 460,823 | 460,823 | 9,363,233 | 9,363,233 |
| | <u>460,823</u> | <u>460,823</u> | <u>64,004,158</u> | <u>64,405,300</u> |

11 Return on assets

The return on assets as at 31 December 2016 is -1.82%. This is calculated as loss after tax divided by total assets.

12 Leverage

| | |
|----------------------------------|------------|
| | EUR |
| Total Assets | 65,752,174 |
| Leverage ratio exposure | 65,752,174 |
| Tier 1 Capital | 7,106,305 |
| Total on-balance sheet exposures | 65,752,174 |
| Total Exposures | 65,752,174 |
| Leverage ratio | 10.89% |

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

5 Year Summary

Statement of profit or loss and other comprehensive income

| | Year ended 31 December 2016 EUR | Year ended 31 December 2015 EUR | Year ended 31 December 2014 EUR | Year ended 31 December 2013 EUR | Year ended 31 December 2012 EUR |
|--|--|--|--|--|--|
| Interest income | 1,614,165 | 2,085,709 | 1,429,583 | 475,699 | 264,322 |
| Dividend income | 128,730 | - | - | - | - |
| Interest expense | (1,738,855) | (1,620,346) | (1,174,149) | (332,083) | (25,993) |
| Net interest income | 4,040 | 465,363 | 255,434 | 143,616 | 238,329 |
| Fee and commission expense | (74,003) | (23,967) | (17,696) | (14,162) | (3,053) |
| Net fair value loss on financial assets at fair value through profit or loss | (58,198) | (37,391) | 4,198 | 273,996 | 178,949 |
| Gains on financial assets not measured at fair value through profit or loss | 334,731 | - | - | - | - |
| Foreign exchange gain/(loss) | 13,892 | (349) | - | - | - |
| Other income | 76,519 | 5,566 | 17,500 | 145,628 | 76,878 |
| Impairment of assets | - | (182,587) | - | - | - |
| Operating income | 296,981 | 226,635 | 259,436 | 549,078 | 491,103 |
| Administrative expense | (919,162) | (1,009,832) | (1,041,563) | (683,511) | (429,331) |
| Employee compensation and benefits | (576,430) | (672,960) | (594,881) | (469,068) | (338,341) |
| Loss before income tax | (1,198,611) | (1,456,157) | (1,377,008) | (603,501) | (276,569) |
| Income tax credit | - | 64,747 | 471,338 | 212,003 | 96,940 |
| Loss for the year/period | (1,198,611) | (1,391,410) | (905,670) | (391,498) | (179,629) |
| Other comprehensive income | | | | | |
| Items that may be reclassified subsequently to profit or loss: | | | | | |
| Available-for-sale investments: | | | | | |
| - change in fair value | 468,625 | (319,150) | (250,477) | 52,317 | 55,223 |
| -impairment of available for sale investments | - | 182,587 | - | - | - |
| - deferred tax thereon | (163,071) | 47,797 | 87,667 | (18,311) | (19,328) |
| Other comprehensive (loss)/ income for the year/period net of tax | 305,554 | (88,766) | 162,810 | 34,006 | 35,895 |
| Total comprehensive loss for the year/period | (893,057) | (1,480,176) | (1,068,480) | (357,492) | (143,734) |

FCM Bank Limited

Additional Regulatory Disclosures

In terms of Banking Rule 07 for the year ended 31 December 2016

5 Year Summary

Statement of financial position

| | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|-------------------|-------------------|-------------------|-------------------|------------------|
| | EUR | EUR | EUR | EUR | EUR |
| Assets | | | | | |
| Cash and cash equivalents | 9,042,019 | 18,388,764 | 9,140,956 | 7,711,356 | 829,387 |
| Depositor compensation scheme with Central Bank of Valletta | 460,823 | 310,048 | 129,536 | 10,697 | - |
| Financial assets at fair value through profit or loss | 2,261,896 | 3,832,700 | 1,227,536 | 599,743 | 937,081 |
| Other investments | 52,379,029 | 32,251,768 | 37,252,418 | 15,843,386 | 7,033,367 |
| Intangible assets | 191,995 | 217,768 | 203,564 | 134,813 | 14,300 |
| Property, plant and equipment | 15,385 | 35,169 | 57,842 | 68,300 | 80,858 |
| Deferred tax | 839,974 | 1,003,045 | 888,177 | 329,315 | 135,621 |
| Other assets | 40,193 | 136,135 | 149,673 | 64,617 | 18,875 |
| Prepayments and accrued income | 520,860 | 628,532 | 585,367 | 293,492 | 215,270 |
| Total assets | 65,752,174 | 56,803,929 | 49,635,069 | 25,055,719 | 9,264,759 |
| Liabilities | | | | | |
| Amounts owed to customers | 56,849,001 | 48,906,650 | 38,430,577 | 16,206,021 | 2,487,906 |
| Other liabilities | 22,991 | 22,034 | 2,517,302 | 1,005,065 | 4,173 |
| Accruals and deferred income | 699,253 | 701,259 | 883,028 | 471,991 | 42,546 |
| Total liabilities | 57,571,245 | 49,629,943 | 41,830,907 | 17,683,077 | 2,534,625 |
| Equity | | | | | |
| Share capital | 12,250,000 | 10,350,000 | 9,500,000 | 8,000,000 | 7,000,000 |
| Investment revaluation reserve | 123,879 | (181,675) | (92,909) | 69,901 | 35,895 |
| Accumulated losses | (4,192,950) | (2,994,339) | (1,602,929) | (697,259) | (305,761) |
| Total equity | 8,180,929 | 7,173,986 | 7,804,162 | 7,372,642 | 6,730,134 |
| Total liabilities and equity | 65,752,174 | 56,803,929 | 49,635,069 | 25,055,719 | 9,264,759 |