

BANK SADERAT PLC
BASEL II PILLAR 3 DISCLOSURES
As At 31st December 2015

Page No.

1	Introduction
2 - 4	Risk Management Structure and Corporate Governance
5	Capital Adequacy
6	Capital Requirement and Market Risk
7	Interest Rate Risk
8	Foreign Exchange Risk
9 - 11	Credit Risk
12	Credit Risk (continued) and Operational Risk
13 - 14	Other Risks

Bank Saderat PLC

Basel II Pillar 3 Disclosures

As at 31st December 2015

Introduction

Financial institutions within the scope of Basel II are required to disclose information about their risk exposures and the risk assessment processes they have used together with explanations of their risk objectives and risk management. These disclosures form Pillar 3 of the Basel II framework.

Basel II is implemented in the European Union (EU) via the Capital Requirements Directive (CRD). The CRD brings together two existing EU directives, the Banking Consolidation Directive and the Capital Adequacy Directive. The CRD directly affects banks and building societies and certain types of investment firms.

The CRD consists of three "pillars". Pillar 1 sets out the minimum capital requirements banks are required to meet based on their credit, market and operational risk exposure. Under Pillar 2, banks and their supervisors at the Prudential Regulation Authority (PRA) have to assess whether additional capital is required to cover risks not covered in Pillar 1.

Pillar 3 complements the minimum capital requirements (Pillar 1) and the supervisory review process (Pillar 2) with the aim of developing a set of disclosure requirements which enable market participants to assess information on a bank's risks, capital and risk management procedures.

In the following pages, Bank Saderat PLC ("the Bank") explains the risks inherent in its business and the structure and procedures that its Board of Directors have established to manage those risks. It also explains the Bank's capital structure and how capital adequacy is managed.

The information contained in this disclosure has not been audited by the Bank's external auditors.

Activities of the Bank

The principal activity of the Bank is the business of banking.

Despite having been regulated by the Financial Services Authority of the United Kingdom (FSA) and prior to the formation of the FSA, by the Banking Supervision Division of the Bank of England, financial sanctions were imposed upon the Bank on 27th July 2010 by the Council of the European Union. There is no allegation that the Bank has broken any UK or EC laws or regulations and the notice states the reason for the sanctions being that Bank Saderat PLC is a 100% owned subsidiary of Bank Saderat Iran.

One of the effects of the imposition of sanctions is that Bank Saderat PLC is subject to an asset freeze. This includes a prohibition on the Bank or any other person from dealing with the Bank's funds and economic resources and a prohibition on any person from making funds or economic resources available, directly or indirectly, to or for the benefit of the Bank without a licence from HM Treasury in the United Kingdom. The Bank is not therefore in a position to take or place funds or enter into foreign exchange transactions and is not able to discount any new letters of credit or enter into any new loan transactions.

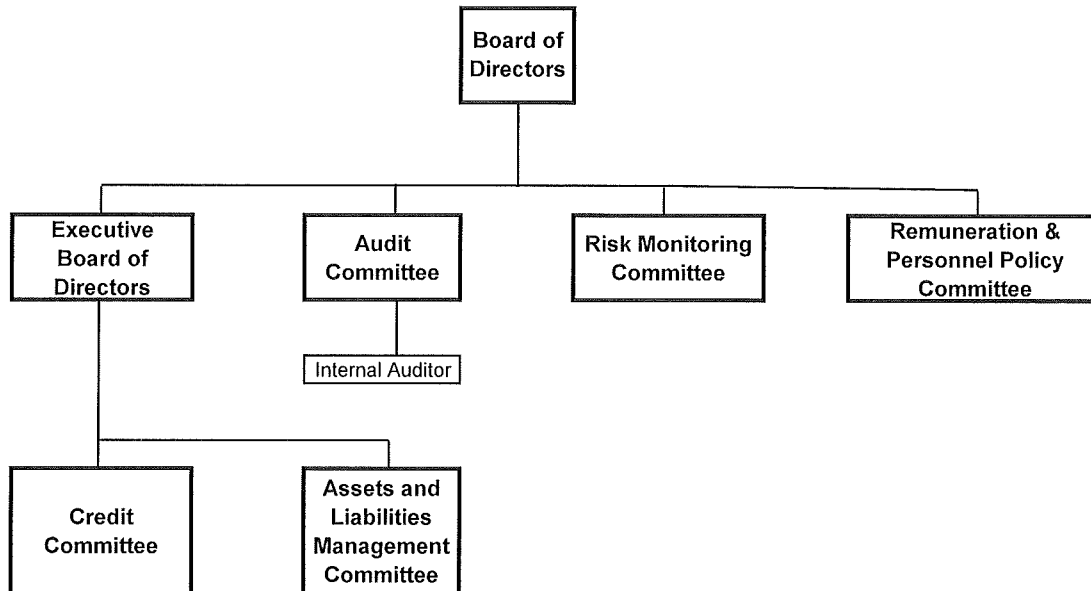
Risk management objectives

The objectives of the risk management regime within the Bank are firstly, to identify and measure all risks that the Bank is subject to and secondly, to ensure that control structures are in place to limit risks to levels that are commensurate with the level of capital held and thirdly, to identify, where appropriate, methods of mitigating risk.

Where the risk management process identifies a risk that is unacceptable to the Directors and cannot be mitigated satisfactorily, the risk is avoided if possible. If a risk cannot be avoided as it is inherent in the operations of the Bank, the Directors allocate capital to cover the risk.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Risk Management Structure and Corporate Governance



The Bank was sanctioned by the EU in July 2010 and is unable to undertake new business. Business-related risk levels are therefore, much reduced and for the duration of the sanctions, the duties and proceedings of the Risk Monitoring Committee have been incorporated into the April and October meetings (or otherwise as agreed), of the Executive Board of Directors. Quorum commitments will continue to be met.

Despite having suffered an asset freeze as a result of the imposition of sanctions, the Bank remains subject to certain risks in relation to its outstanding business entered into prior to the imposition of sanctions. These risks are measured and reported on to Senior Management even though the Bank's ability to reduce risk positions is severely curtailed by the effect of sanctions.

The principal risks facing the Bank remain liquidity risk, interest rate risk, credit risk, foreign exchange risk and operational risk. Strategic risk, including political risk and economic risk, are considered to be types of operational risk. Operational risk also includes the risk of non-compliance with regulatory and legal requirements.

The Bank's risk management focuses on these major areas of risk.

Liquidity risk is the risk that the Bank will encounter difficulty in meeting its obligations from its financial liabilities as they become due.

Interest rate risk is the risk of variability of the fair value of future cash flows arising from financial instruments due to changes in interest rates and is measured by analysing assets and liabilities into time bands according to their maturity or next interest repricing date, whichever is the earlier. Since the imposition of sanctions on the Bank by the EU on 27th July 2010 the Bank is prohibited from entering into new transactions to reduce its interest rate positions.

Credit risk is the risk that companies, financial institutions and other counterparties will be unable to meet their obligations to the Bank which may result in financial loss. Credit risk arises principally from the Bank's lending book and from holding investments.

Foreign exchange risk arises from the change in value expressed in reporting currency, of assets and liabilities held in currencies other than the reporting currency, due to fluctuations in spot or forward exchange rates. The Bank does not take speculative positions in currencies and any net open positions arise in the ordinary course of business. Since the imposition of sanctions on the Bank by the EU on 27th July 2010, the Bank is prohibited from entering into foreign exchange transactions without a specific licence from HM Treasury.

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

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Risk Management Structure and Corporate Governance (continued)

Authority flows from the Board of Directors and the above diagram shows the risk management and corporate governance structure. The main elements of risk governance are as follows:

The Board of Directors

This is the primary governing body of the Bank. It approves the level of risk to which the Bank is exposed and the framework for reporting and managing risk. The Board comprises the non-executive, Iran based Chairman representing the principal shareholder, two UK based independent non-executive Directors and the Managing Director. The Board of Directors meets four times a year.

The Board of Directors delegates authority for many of the ongoing operational decisions to:

The Executive Board of Directors

The Executive Board of Directors comprises the two UK based independent non-executive Directors and the Managing Director.

The Credit Committee and the Assets and Liabilities Management Committee report to the Executive Board of Directors. The Executive Board meets monthly, unless a full Board meeting is being held.

The Audit Committee

The Audit Committee comprises the non-executive Chairman representing the principal shareholder and the two UK based independent non-executive Directors. It is chaired by an independent non-executive Director. It may be attended by the Managing Director, the Assistant Managing Director, the Financial Controller, the Internal Auditor and the External Auditor. The Committee meets four times a year and reports directly to the Board of Directors. There is an opportunity at each meeting for members to discuss any matter without members of the executive being present.

The Committee is responsible for the assessment of the effectiveness of controls that are in place to mitigate risk and determines the risks to be assessed. It also oversees the Internal Audit function, receives internal audit reports and is responsible for approving the detailed audit plan and timetable. The Committee also receives an annual report which is used to assure the Board of Directors that controls are adequate and appropriate.

The Risk Monitoring Committee

The Risk Monitoring Committee comprises the two UK based independent non-executive Directors, the Managing Director, the Assistant Managing Director and the Financial Controller. It reports to the Board of Directors.

The Risk Monitoring Committee is charged with the responsibility of advising the Directors on the nature and relative scale of the risks confronting the Bank, the appropriateness of the controls intended to manage those risks and whether the residual risk is within the parameters approved by the Board.

The Risk Monitoring Committee oversees the production of a Risk Register whereby each department of the Bank analyses the risks to which it is subject, the mitigants and how the residual risk is managed. These departmental Risk Registers are then consolidated into a Bank Risk Register. The Risk Committee also ensures that contingency plans are in place to achieve business continuity in the event of serious disruption to business operations.

The Remuneration and Personnel Policy Committee

The Remuneration and Personnel Policy Committee comprises the two UK based independent Non-executive Directors, the Managing Director, the Assistant Managing Director and up to two departmental managers. It is charged with the responsibility of advising the Board of Directors on matters related to remuneration, including the Bank's bonus and salary review policy. It also considers matters related to employment legislation, terms and conditions of employment, the staff handbook, disciplinary matters, staff complaints and the appeals process.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Risk Management Structure and Corporate Governance (continued)

The Credit Committee

The Credit Committee comprises the Managing Director, the Assistant Managing Director, the Financial Controller and the Operations Manager. Meetings are held as and when necessary. The Committee reports to the Executive Board of Directors. The Credit Committee receives annual reviews of outstanding borrowers.

The Internal Credit Rating System

The Board of Directors has approved an in-house developed internal credit rating system which before the imposition of sanctions on the Bank was used to determine whether or not the Credit Committee was able to approve a loan or advance, or whether higher level approval would need to have been sought from either the Executive Board or full Board of Directors. The system is currently used in conducting annual reviews of borrowers to assess their on-going credit standing and to consider whether a loan or advance should be placed on a "watch list" due to a deteriorating assessment of the borrower. The system is based upon a points scoring method with points awarded against various criteria from an analysis of accounts provided by borrowers. The sum of the points awarded determines the classification of each borrower from A (the highest rating) to D (the lowest). It is likely that any D rated borrowers would be in default resulting in the raising of a provision against the debt unless adequate security renders a provision unnecessary.

The Assets and Liabilities Management Committee

The Assets and Liabilities Management Committee comprises the Managing Director, The Assistant Managing Director and the Financial Controller. Other heads of department are invited to attend from time-to-time. It meets once a month and reports to the Executive Board of Directors.

The Assets and Liabilities Committee monitors best practice management of the Bank's financial resources operating within the Bank's policy guidelines and the applicable regulatory framework.

The committee receives financial and statistical reports related to exposures, liquidity and capital adequacy.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Capital Adequacy

The Bank's capital resources include share capital, a general banking risk reserve and retained earnings (Tier 1 Capital) together with subordinated loan notes (Tier 2 Capital). The Bank does not hold any Tier 3 Capital.

At 31st December 2015, Tier 1 Capital comprised:

	€ 000s
Share Capital	
162,392,300 Ordinary shares of €1 each	162,392
General Banking Risk Reserve	6,000
Retained Earnings	413
Total Tier 1 Capital	<u><u>168,806</u></u>

and Tier 2 Capital comprised:

Shareholder's subordinated term loan notes	20,828
Total Tier 2 Capital	<u><u>20,828</u></u>
Total Capital	<u><u>189,633</u></u>

The majority of Tier 1 Capital is issued and fully paid-up ordinary shares of €1 each. Audited retained earnings to 31st December 2015 and a general banking risk reserve, which was raised to maintain the regulatory capital base and is not available for distribution, are also included in Tier 1 capital.

Tier 2 capital consists of capital instruments that combine the features of debt and equity in that they are structured as debt instruments, but exhibit some of the loss absorption and funding flexibility features of equity. It comprises shareholders subordinated term loan notes maturing in 2022.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Capital Requirement

The Bank's capital requirement at 31st December 2015, under the Basel II convention was:-

	€'000
Pillar 1 Credit risk capital requirement	17,772
Pillar 1 Foreign Exchange risk requirement	222
Pillar 1 Operational risk requirement	889
Total Pillar 1 Capital Requirement	18,883
Pillar 2 Additional Credit risk capital requirement	2,776
Pillar 2 Concentration risk requirement	2,115
Pillar 2 Residual risk requirement	142
Pillar 2 Market risk requirement	9,822
Total Pillar 2 Capital Requirement	14,854
Total Capital Requirement	33,737
Total Capital held at 31.12.15 under Basel II	189,633
Capital cover under Basel II at 31.12.15	562.10%
Risk Asset Ratio at 31.12.15	44.97%

The PRA has decided to apply an Internal Capital Guidance (ICG) figure of 225% of Pillar 1 capital but have not conducted a SREP. This results in Pillar 2 capital of 125% of Pillar 1 capital and a total capital requirement of € 41,010,573 at 31st December 2015 compared with a requirement of € 33,080,928 as analysed above. The higher capital requirement is being reported to the PRA each quarter, at their request. Applying this higher requirement results in capital of 462.40% of the minimum capital requirement which equates to a risk asset ratio of 36.99%.

Capital Planning Buffer

The PRA also requires the Bank to hold a Capital Planning Buffer, which is an amount of capital to be held in excess of the Bank's ICG of 225% of Pillar 1 Capital. This Capital Planning Buffer should be available to use in times of stress to ensure that the Bank does not breach its capital guideline and has been set at € 3,830,000.

Market Risk

Market risk is the risk that changes in interest rates, foreign exchange rates or other prices and volatilities will have an adverse effect on the Bank's financial conditions or results. The Bank does not have a trading book, however any currency risk arising from the Bank's commercial banking and lending activities in the banking book is treated as though it was a trading book item and managed accordingly.

It is the objective of the Bank to manage and control market risk exposures in order to optimise risk and return.

Market risk is reported to the Asset and Liability committee, which in turn reports to the Executive Board of Directors and through them, to the full Board of Directors.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Interest Rate Risk

Interest rate risk is the risk of variability of the fair value of future cash flows arising from financial instruments due to changes in interest rates.

The Bank is exposed to interest rate risk in the banking book due to mismatches between the repricing dates of assets and liabilities. This risk is monitored by the Assets and Liabilities Management Committee, reporting to the Executive Board of Directors and through them, to the full Board of Directors.

Pillar 2 Capital

Residual interest rate mismatches at 31st December 2015 exist in Euros, Sterling, US Dollars and United Arab Emirates Dirhams for periods up to one year. Consolidated interest rate mismatches at 31st December 2015 were:

	Less than three months €'000	More than three months but less than six months €'000	More than six months but less than one year €'000	Undated - Non- interest bearing €'000	Total €'000
Assets					
Cash, loans and advances to banks and customers	111,348	95,546	15,264	-	222,158
Tangible fixed assets				12,900	12,900
Other assets				258	258
Prepayments and accrued income				1,046	1,046
Total assets	<u>111,348</u>	<u>95,546</u>	<u>15,264</u>	<u>14,204</u>	<u>236,362</u>
Liabilities					
Deposits by banks & customer accounts	44,842				44,842
Other liabilities				1,886	1,886
Shareholders' funds				168,806	168,806
Subordinated loan		20,828			20,828
Total liabilities	<u>44,842</u>	<u>20,828</u>	<u>-</u>	<u>170,693</u>	<u>236,362</u>
Interest rate sensitivity gap	<u>66,506</u>	<u>74,718</u>	<u>15,264</u>	<u>(156,488)</u>	<u>0</u>

The Bank does not have interest rate gaps in excess of one year since all interest earning assets and interest bearing liabilities, have their interest rates re-set within one year.

The effect of a 2% movement in interest rates across all currencies and all dates at 31st December 2015 was € 1,522,056 (31st December 2014: €1,534,937). This calculation assumes that all interest rate gaps could be closed in the market by taking deposits or placing amounts at interest rates 2% above or below the actual rate applied to each gap in each currency.

The Directors also set aside € 8 million Pillar II capital within market risk to cover approximately three years of overhead expenditure to mitigate the impact of current, low market interest rates that do not allow the Bank to earn sufficient interest to cover its operating expenditure.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Foreign Exchange Risk

Foreign exchange risk arises from the change in value expressed in reporting currency, of assets and liabilities held in currencies other than the reporting currency, due to fluctuations in spot or forward exchange rates. The exposure is measured and monitored daily considering the position in terms of net exposure.

The foreign exchange position risk requirement in Pillar 1 is calculated by:

- calculating the net open position in each currency
- converting each such net position into base currency equivalent at spot rates of exchange
- calculating the total of all net short positions
- multiplying by 8%.

The Bank's foreign exchange position risk requirement at 31st December 2015 was **€141,739 (31.12.14 € 170,655)**

	US Dollar	United Arab Emirates Dirhams	Euros	Other Currencies	Sterling	Total
	€'000	€'000	€'000	€'000	€'000	€'000
Assets						
Cash, loans and advances to banks	11,943	2,261	181,287	118	11,088	206,698
Loans and advances to customers	-	-	16,153	-	-	16,153
Tangible fixed assets	-	-	12,900	-	-	12,900
Other assets	-	-	-	-	257	258
Prepayments and accrued income	-	-	-	-	352	352
Total assets	11,943	2,261	210,340	118	11,697	236,361
Liabilities						
Deposits by banks	6,914	3,234	20,988	115	7,863	39,113
Customer accounts	2,126	18	1,059	3	2,523	5,729
Other liabilities	251	-	33	-	1,602	1,886
Shareholders' funds			168,806			168,806
Subordinated loan			20,828			20,828
Total liabilities	9,291	3,252	211,714	118	11,988	236,361
Net position	2,652	(991)	(1,374)	(0)	(291)	0

There were no off-Balance Sheet positions.

Pillar 2 Capital

As foreign exchange positions are deemed to be insignificant and it is expected that they will remain so for the foreseeable future, it is not considered necessary to hold additional capital to cover these positions, in excess of the position risk requirement included under Pillar 1.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Credit Risk

Credit risk is the risk that companies, financial institutions and other counterparties will be unable to meet their obligations to the Bank which may result in financial loss. Credit risk arises principally from the Bank's remaining lending book. The Bank uses the Simplified Method of calculating its credit risk capital requirement using the standard risk weighting table.

Credit risk exposures at 31st December 2015

	Carrying Value	Weighted Under Basel II	8% of Basel II Weighted Asset
€ 000			
Cash	1,729	0	0
Lending to Bank Saderat Group companies	47,844	47,844	3,827
Lending to Other Banks	157,124	135,218	10,817
Lending to Other Non-Banks	16,153	23,984	1,919
Other Assets	13,510	15,106	1,208
	<u>236,361</u>	<u>222,151</u>	<u>17,772</u>

Under Basel II, the Pillar 1 capital required to support € 236,361,000 of weighted exposures at 31st December 2015 amounted to € 17,772,000.

Non-bank credit exposures by industrial sector at 31st December 2015.

	Outstanding	Limit	Capacity
€ 000			
Automotive	-	46,000	46,000
Transport	-	69,000	69,000
Metals	210	46,000	45,790
Construction	15,943	69,000	53,057
Food	-	46,000	46,000
Oil/gas/petroleum	-	138,000	138,000
Investment companies	-	92,000	92,000
	<u>16,153</u>	<u>506,000</u>	<u>489,847</u>

Pillar 2 Capital

From the various risks attributed to credit, one has been identified as high risk to the Bank - that of a fall in the price of shares quoted on the Tehran Stock Exchange which are held as security for loans. The mitigant for this risk is that the Bank normally demands 200% cover for secured lending.

Medium risks relate to the deterioration of a counterparty's financial position, an illiquid market in the Tehran Stock Exchange, the inability to convert Iranian Rials into hard currency, a beneficiary being insolvent at the time of discounting a bill of exchange and the incorrect handling of a documentary credit.

Low risks include the inability of Iranian banks to pay; the insolvency of the borrower; the inability to enforce security claims due to defective documentation and a series of risks relating to internal procedural failures.

The Bank believes that sufficient mitigants are in place to cover the high and low credit risks but considers it to be prudent to hold additional Pillar 2 capital of 1.25% of risk weighted assets to cover the medium risk in this category. At 31st December 2015, this amounted to € 2,776,000 (2014: € 2,651,500.)

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Concentration of credit risk

Concentration risk is a measure of the Bank's exposure to an individual counterparty, group of connected counterparties, industry sector or country. The Bank does not hold any significant concentrations of exposure to counterparties or industry sectors but does have a significantly concentrated exposure to Iran.

The table below shows the Bank's geographic concentrations of credit risk as at 31st December 2015.

	Iran	Germany	United Kingdom	Other	Total
€ 000					
Cash and balances at banks	38,416	42,111	13,094	81	93,704
Loans and advances to banks	80,199	-	15,566	17,230	112,995
Loans and advances to customers	16,153	-	-	-	16,153
	<u>134,769</u>	<u>42,111</u>	<u>28,660</u>	<u>17,312</u>	<u>222,852</u>

Pillar 2 Capital

For prudence, additional capital of 1.25% of Iranian exposures has been allocated to compensate for the high concentration of assets in Iran. At 31st December 2015, this amounts to € 1,684,607 (2014: € 1,622,470.)

Average exposure to credit risk by credit class

	Outstanding at 31.12.15	Average outstanding during 2015
€ 000		
Cash and balances at banks	93,704	93,248
Loans and advances to banks	112,995	112,096
Loans and advances to customers	16,153	16,027
	<u>222,852</u>	<u>221,371</u>

Residual risk

All the identified residual risks are common to the credit risk items with the exception of a borrower failing to adhere to covenants and the inability to realise security should the borrower be unable to repay.

The Bank has a share secured portfolio of loans of € 12.3 million at 31st December 2015. The security margin of these facilities is normally 200% of the drawn amount, although replacement to that level, should the share price fall, normally only takes place when the cover has fallen to 150%. Additional Pillar 2 capital of 1.25% of the share secured loan portfolio is deemed prudent to cover these risks and amounted to € 153,611 at 31st December 2015.

In addition to those loans secured by Tehran Stock Exchange shares, the Bank has € 3.9 million of loans to customers which are guaranteed by a parent company or bank. Where collateral is provided by a third party, the third party becomes subject to the same annual credit review as the primary borrower. The Bank has the right to call on its security in the event of customer default on principal or interest repayments.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Residual maturity.

The residual maturity breakdown of all the exposures analysed by class is as follows:

	Less than three months	Between three and six months	Between six months and one year	Between one and five years	Total
€ 000					
Balances with and loans and advances to banks	91,973	95,546	15,264	-	202,783
Loans and advances to customers	16,153	-	-	-	16,153
	<u>108,127</u>	<u>95,545</u>	<u>15,264</u>	<u>-</u>	<u>218,937</u>

Past due and impaired.

A financial asset is past due when the counterparty has failed to make a payment when contractually due. Past due does not mean that a counterparty will never pay, but it can trigger various actions such as renegotiation, enforcement of covenants or legal proceedings.

	Less than one month		More than one month and less than three months		Over three months		€ 000s Total
	€ 000s Past Due Principal	€ 000s Past Due Interest	€ 000s Past Due Principal	€ 000s Past Due Interest	€ 000s Past Due Principal	€ 000s Past Due Interest	
By Industry							
Sector € 000s							
Construction	1,250	6	1,250	36	14,897	777	18,216
Metals	-	-	-	-	210	-	210
	<u>1,250</u>	<u>6</u>	<u>1,250</u>	<u>36</u>	<u>15,107</u>	<u>777</u>	<u>18,426</u>

Past due interest is fully provided against.

The carrying value of loans are secured as follows:

	By Shares Listed on the TSE (Tehran Stock Exchange)	By Guarantee	Total
Construction	12,289	3,655	15,943
Metals	-	210	210
	<u>12,289</u>	<u>3,865</u>	<u>16,153</u>

The Directors are of the opinion that should it be deemed necessary to realise the security, in all the above instances sufficient funds would be realised to repay the amounts outstanding.

On-going assessment is made to determine whether there is objective evidence that a specific financial asset or group of financial assets is impaired. Evidence of impairment may include past due amounts or other indications that the borrower has defaulted, is experiencing significant financial difficulty or where a debt has been restructured to reduce the burden to the counterparty.

If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss is provided for.

The following impaired exposures and provisions against those exposures existed at 31st December 2015.

€ 000	Impaired Exposure	Provisions
	Non-performing loans and advances	
	- to customers - principal	(4,614)
	- to customers - interest	(394)
	- to banks	(4)
	Blocked funds	(2,533)
	<u>20,964</u>	<u>(7,546)</u>

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Amounts are written off when collection of the loan or advance is considered to be impossible, On secured loans, any write off would take place only after ultimate realisation of collateral value. All write offs are on a case by case basis, taking account of the exposure at the date of the write off.

Reconciliation of movements in provisions

	2015
At 1st January	6,667,477
Exchange adjustments	279,764
Increase in provisions	598,958
At 31st December	<u>7,546,198</u>
Impaired loans and advances	
- to banks	4,431
- to customers - principal	17,607,000
- to customers - interest	819,000
Blocked funds	2,533,394
	<u>20,963,826</u>

Operational Risk

Operational risk is the risk of loss to the Bank resulting from deficiencies in processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risk.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial loss through the implementation of controls, whilst avoiding procedures which inhibit efficiency and increase costs unjustifiably.

The Bank has elected to use the Basic Indicator Approach (BIA) which is considered to be the most appropriate basis given the disproportionate cost of establishing more sophisticated methods of capturing the requisite data and devising an acceptable method of calculating operational risk capital. Under this approach, the operational risk capital is calculated by mapping the Bank's three year average net interest income and net non-interest income and applying 15% thereto, as in the following table.

€ 000	2013	2014	2015
Net interest income	6,382	5,472	5,385
Fees and commissions receivable	264	24	10
Dealing profits/(losses)	(36)	140	144
	<u>6,610</u>	<u>5,636</u>	<u>5,539</u>
Average		<u>5,928</u>	
15% thereof = capital requirement		<u>889</u>	

Since its formation, Bank Saderat PLC has not suffered any material operating loss and the Directors consider that sufficiently robust operating procedures are in place to ensure that any operating loss that can reasonably be expected to occur in the foreseeable future would more than adequately be covered by the amount of capital allocated on this basis.

Operational risk is formally reviewed annually, when the Bank prepares its budget for the ensuing year. This review then encompasses the experience gained during the previous twelve months and also ensures that any risks associated with new areas of business, or changes in emphasis or scale of existing areas of business are incorporated in the risk review. The latest formal review took place in December 2015.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Other Risks

The Bank has considered the following additional risks and the mitigants in place to ameliorate those risks in the context of providing additional Pillar 2 capital against Operational Risk.

Strategic risk
Liquidity risk
Transactional risk
Settlement risk
Regulatory risk
Reputational risk
Systemic risk
Pension risk

i) Strategic risk

The following four categories of strategic risk have been identified:-

- a) Iran's inability to pay its debts due to low oil price or insufficient hard currency
- b) Difficulty in enforcing security in the Iranian courts
- c) Difficulty in keeping clearing facilities due to international pressure on other banks

In a worst case scenario, investment of the Bank's free capital, together with a sensible programme of cost reduction, would allow Bank Saderat PLC to remain solvent.

The risk of loss due to difficulty enforcing security in the Iranian courts is a type of credit risk, albeit a risk that could be triggered by political events and is therefore covered in the additional capital allocated for credit risk.

ii) Liquidity risk

Following the imposition of sanctions, the Bank is highly liquid as assets existing at the date of sanctions mature into cash. This highly liquid position will not change significantly until sanctions are removed and the Bank is able to operate normally. No additional capital is required, therefore, to support liquidity risk.

iii) Transactional risk

With the exception of the risk that a borrower may not adhere to covenants in their facility, all other transactional risks are common with credit risks. The single highest risk is that of a fall in the price of shares on the Tehran Stock Exchange when such shares are held as collateral. This risk has been dealt with as a credit risk.

iv) Settlement risk

Settlement risk may be divided into two elements: risks that relate to the failure of a payments system internally and risks of settlement failure due to sanctions, closure of correspondent accounts or the inability to access external payment system. The Bank has been living for many years with the risk that payments may be disrupted and is therefore confident that internal payment procedures and controls over systems are sufficiently robust to justify the conclusion that no additional capital is required to mitigate these risks beyond that already provided for operational risk.

The elements of settlement risk that relate to the political risk of sanctions are incorporated in the additional capital allocated for credit risk, as they arise, predominantly, from the concentration of the Bank's business in Iranian assets.

v) Regulatory risk

Regulatory risk concerns the Bank failing to comply with its statutory obligation of adhering to the financial sanctions imposed upon it and the regulatory limits on its business and reporting timetables and are considered to be in the medium to low category of risk. The Bank has minimal retail business that could be subject to consumer protection legislation.

The Board of Directors of Bank Saderat PLC has adopted a series of policies designed to ensure that the Bank operates in accordance with its statutory obligations and has created a "culture of compliance" throughout the organisation to ensure that regulatory requirements are met. The Bank does not consider that the allocation of additional capital for regulatory risk is necessary.

Bank Saderat PLC
Basel II Pillar 3 Disclosures
As at 31st December 2015

Other Risks (continued)

vi) Reputational risk

These medium to low probability risks may be analysed into two areas reflecting the underlying reason from which reputational risk may arise:-

- a) IT related risk such as data loss, internal or external hacking, defamatory e-mails or inappropriate web sites or theft of confidential data.
- b) Internal failings with regard to staff matters, e.g. loss of personal data or failure to comply with employment legislation.

Reputational risk in respect of the above, is intangible and considered to be mitigated by having in place appropriate and robust procedures together with a high degree of management overview of operations. It is not considered that the allocation of additional capital is necessary to mitigate these risks.

vii) Systemic risk

The principal systemic risk to which the Bank is vulnerable is that of changes to Iranian laws that would prevent the Bank enforcing a claim for security in the event of default by a borrower. If Iranian law was changed, for example, to disallow shares being offered as security for external borrowing or exchange controls were imposed that prevented the conversion of Rials into hard currency then the Bank could experience difficulty in recovering funds.

There are two mitigating factors in place. Firstly, regardless of any legislative changes in Iran, a primary obligation would remain on the borrower to repay its indebtedness and secondly, it has been the Bank's policy to lend only to large, reputable, publicly owned companies.

If the Bank had recovered security in Iranian Rials but was unable to convert the Rials into hard currency, the Bank's shareholder, Bank Saderat Iran, has agreed to accept any dividend payments in Rials which could then be netted against the value of the security. The shareholder would also assist the Bank to recover Rial denominated security within Iran in any way possible.

It is not deemed necessary to allocate additional capital to cover systemic risk.

viii) Pension risk

The Bank is not vulnerable to pension risk.

With effect from 31st January 2002, the Bank's defined benefit pension scheme, the Iran Overseas Investment Bank PLC Retirement Benefits Scheme (the 'Scheme'), was closed and all active members became deferred pensioners.

As at 31st December 2009 the assets of the Scheme were nil having been used to settle the liabilities in respect of individual members' benefits by the purchase of deferred annuities from Legal & General Assurance Company, or by the payment of individual transfer values to another pension scheme or personal pension plan.

The final winding up of the Scheme is now complete, the liabilities have been discharged and final accounts have been prepared and to this extent, the financial statements contain adequate disclosure of the cost of providing retirement benefits and the related gains, losses, assets and liabilities.

As the scheme has been terminated, an indemnity has been given by the Bank to each trustee against any possible action by a scheme member. The Bank has also become the sole corporate trustee of the scheme.

The costs of providing pension benefits to staff under the defined contribution scheme are charged to the profit and loss account monthly.

The Remuneration Code

The Bank is classified within proportionality tier 3 for the purpose of the Remuneration Code and is not therefore required to disclose details of Directors' and staffs' remuneration.