



United Trust Bank Limited

Pillar 3 disclosures
As at 31 December 2010

Approved by the Board on
5th December 2011

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1. Introduction

This document constitutes the Pillar 3 disclosure of United Trust Bank Limited (“the Bank”) as required under the Basel II Capital Requirements Directive.

The purpose of this document is to provide information and disclosure to the Bank’s stakeholders in relation to the internal procedures and policies adopted by the Bank to manage and mitigate its key risks. The Pillar 3 disclosures also provide additional disclosures of the Bank’s assets, liabilities and capital resources over and above those shown in its financial statements.

1.1. Overview of the Basel II framework

The Basel II framework came into effect on 1 January 2007 as a means of regulating banks, and determining the level of capital that banks must hold, having regard to the individual risk profile of each bank. The purpose of a bank’s capital resources is to act as a buffer to absorb losses incurred by the bank.

The requirements of the Basel II framework are divided into three ‘pillars’ as described below.

Pillar 1 – these requirements set out the minimum capital requirements that each bank must adhere to, and the rules can be applied on a ‘standardised’ basis, or if additional permissions are granted by the Financial Services Authority (“FSA”), on an advanced basis. Advanced bases allow banks to use their own risk models to determine minimum capital requirements, as opposed to using the standardised values set out within the rules.

Pillar 2 – these rules require that each bank perform an ‘Individual Capital Adequacy Assessment Process’ (“ICAAP”) to assess its own risk profile, and determine the level of additional capital required over and above the Pillar 1 requirements having regard to those risks.

Pillar 3 – these rules are designed to promote market discipline by enhancing the level of disclosure made by banks to its stakeholders by allowing them to assess the bank’s key risk exposures and the adequacy of the bank’s risk management process to mitigate these risks.

1.2. Adoption of the Basel II framework

United Trust Bank adopted the Basel II framework on 1 January 2008, and uses the standardised approach in measuring its capital resources requirements on a Pillar 1 basis.

1.3. Basis of disclosure

The Bank's Pillar 3 disclosure document has been prepared in accordance with the requirements of Chapter 11 of the FSA BIPRU Sourcebook, and in accordance with an internal policy agreed by the Bank's Board.

All disclosures within this document have been prepared as at 31 December 2010, which is the Bank's latest financial year-end. Future disclosures will be based on year end financial information, and shall be published annually within six months of the year end.

1.4. Verification of information

The Bank's Pillar 3 disclosures are not subject to external audit or review.

2. Scope of Pillar 3 disclosure

This section of the document provides an outline of the structure of the Bank and the nature of its business. It also explains how each entity within the group has been treated within the Pillar 3 disclosures.

United Trust Bank Limited – The Company’s primary activities are the provision of short term property finance, property development finance and secured asset finance.

The Banks holding company, UTB Partners Limited, is not included in the Pillar 3 disclosures.

3. Risk management objectives and policies

3.1. Risk management objectives

Risk is inherent in all aspects of the Bank's (and every other bank's) business. Within the Bank, a risk management framework is in place to ensure that all material risks faced by the Bank have been identified and measured, and that appropriate controls are in place to ensure that each risk is mitigated to an acceptable degree.

The risk management framework is also a key input into the Bank's strategic planning processes to ensure that the future development of the Bank's business does not expose it to an excessive level of risk.

The principle methods used to manage risks identified by the Bank include:

- Board and management committees to approve initial risk limits and policies, and to monitor adherence to those policies;
- Management information packs that analyse the level of risk exposure at relevant points in time;
- Departmental policies, procedures and mandates to limit the extent to which individuals can commit the Bank to accepting additional risk;
- Independent internal audit coverage to act as a 'third line of defence' to ensure policies and procedures have been complied with.

3.2 Risk governance structures

This section describes the committee and management structures in place within the Bank in order to identify and manage risk, and ensure that the appropriate standards of corporate governance are maintained.

Significant risks faced by the Bank are reviewed by the Management of the Bank. The key duties of Management are:

- assess the risks faced by the Bank;
- to review the appropriateness of risk measurement policies and practices; and
- to review and comment on the adequacy of the Bank's controls to measure, monitor and manage risk based on information provided or obtained.

Any significant and/or material breaches of prescribed controls are reported to the Board. The Bank recognises that it is key to its future success as a financial institution to conduct its affairs with prudence and integrity and to safeguard the interests of the stakeholders.

The predominant types of risk that the Bank faces are credit risk, liquidity risk, interest rate risk and operational risk. Additional significant risks are legal risk, regulatory risk and reputational risk.

The Board

The Board of Directors are responsible for establishing risk appetite and approve policy statements defining credit risk and liquidity risk. These policy statements establish the Bank's overall capacity for risk and set out the parameters within which it operates. Implementation of these policies is the responsibility of the Executive Committee who report to the Board.

The main committees of the Bank are:

Audit committee

A non-executive director chairs this committee. It reviews and sets the internal audit programme and examines completed internal and external audit reports. It considers the major findings and ensures, via the Management, that recommendations are implemented where necessary. It also reviews the annual financial statements. The Audit Committee meets at least four times per year.

Remuneration Committee

The role of this committee is to consider remuneration policy and specifically to determine the remuneration and other terms of service of executive directors and senior managers. The executive directors decide fees payable to non-executive directors. The committee meets as required.

Executive Committee

This committee comprises the Executive Directors of the Bank and meets monthly to discuss and formulate the strategic direction of the Bank.

Operations Committee

The operations committee meets monthly to discuss matters relating to the Banks day-to-day operations. It comprises the Executive Directors and Departmental Managers.

Credit committee

This forum sanctions all counterparty limits. It regularly reviews loan performance, large exposures and adequacy of provisions. Its role is to ensure that credit policy is prudent, taking into account changing market trends.

Asset and liability committee

This committee recommends the policy for liquidity and interest rate risk. It regularly reviews the Bank's balance sheet to ensure that it is positioned prudently and meets the agreed policies taking into account prevailing markets, and projections of business growth.

Day-to-day control and monitoring of policies, procedures and limits is the responsibility of the Management.

Regular reports and information are provided to the Management and the Board, to ensure they fully understand the risk and to demonstrate proper and prudent measurement, monitoring and management of risk.

It is important that all the Bank's risks are regularly considered. Any change to business objectives can cause a change to the risk profile of the business. Consequently, under the guidance of the Management, the business regularly reviews its objectives, assesses the risks to prevent these objectives being achieved, and ensures there is defined ownership of the risks and defined ownership of the corresponding controls.

The likelihood and impact of any risk is assessed and appropriate controls are designed to be effective, taking into account the severity of the risk faced. The output from these processes is provided to Internal Audit, to enable them to give assurance as part of the audit plan that controls are working properly and all risks have been properly identified.

Major risks

The major risks associated with the Bank's business are:

- Credit risk;
- Liquidity risk;
- Interest rate risk;
- Operational risk;
- Legal risk;
- Regulatory & Compliance risk; and,
- Reputational risk.

Credit risk

This is the risk that counterparties will be unable or unwilling to meet their obligations to the Bank as they fall due. It arises from lending transactions.

The Bank's Credit Committee includes Executive Directors and Business Development Managers. The Credit Committee has to reach a unanimous consensus before authorising a credit exposure and each approval is signed by a valid quorum. Additionally exposures beyond a certain threshold require additional authorisations. Credit limits on all lending, including treasury and interbank lines are reviewed regularly.

The Bank has a focused business strategy and has considerable expertise in its chosen sectors. The vast majority of the Bank's lending, excluding interbank placements, which are predominantly with UK banks, is secured on assets. On a geographical basis, at least 95% of the credit exposure of the Bank, including contingent liabilities and commitments, is to the UK.

Liquidity risk

This risk arises from the inability of the Bank to meet its obligations as they fall due. It can arise from the withdrawal of customer deposits, the drawdown of existing customer facilities and asset growth.

The Bank's liquidity policy ensures prudent management of liquidity and adherence to FSA regulatory guidelines. This policy is developed and implemented by the Asset and Liability committee. The Bank's Treasury function has responsibility for day-to-day liquidity management.

Limits on potential cash flow mismatches over defined time horizons form the principal basis of liquidity control. Limits are also placed upon the value of deposits taken from a single source, both monthly and in aggregate. A dedicated system is used to monitor and stress test the Bank's liquidity position against different scenarios.

Interest rate risk

Interest rate risk is the risk that the value of the Bank's assets and liabilities will fluctuate because of changes in market rate.

The Bank finances its loan book and money market deposits primarily through customer deposits. The Asset and Liability Committee meets regularly to review the rates offered on the various deposit products. The deposits are spread between variable and fixed rate deposits.

The Bank's lending to customers is at rates linked to the interest rates currently prevailing in the market. The money market deposits are placed at the best rates available in the market. In common with other banks, the Bank earns part of its return by controlled mismatching of the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rates or, if earlier, the dates on which the assets and liabilities mature.

A positive interest rate sensitivity gap exists where more assets than liabilities re-price during a given period. A positive gap position tends to benefit net interest income in an environment where interest rates are rising. However, the actual effect will depend on a number of factors including actual repayment dates and interest rate sensitivity within the banding period. The vast majority of the Loans and Advances dealt with in the table below benefit from interest rate floors. These cannot easily be dealt with in a gap table but the table is prepared on the basis that floors are not activated. The table may over-state the economic interest rate mis-match in some circumstances.

Operational risk

This is the exposure to financial or other damage arising through system or process failure, human error, or fraud or through inadequate controls and procedures. The Bank has a detailed procedures manual in place and ensures that all operational risks are evaluated and appropriately controlled.

Contingency plans are in place to ensure continuity in the event of any unforeseen serious disruption to business operations. These plans are reviewed and tested to ensure they can be implemented in a timely manner should events dictate.

To give further assurance, the Internal Audit function regularly reviews operational areas to ensure that risks and controls are appropriate and effective.

Legal risk

Legal and documentation risk is defined as the risk that contracts entered into by the Bank with its clients will not be enforceable, especially with respect to events of default by a client. This could lead to a situation where the documentation will not give the rights and remedies anticipated when the transaction was entered into, particularly when security arrangements have been agreed.

To mitigate legal risk, the Bank uses independent external legal advisors to ensure documentation gives the appropriate rights and remedies.

Regulatory & compliance risk

This is the risk that any part of the Bank fails to meet the requirements or expectations of the regulatory authorities. It can also arise where changes to regulations are not anticipated or managed properly. Compliance reports are reviewed regularly by the Board and Audit Committee and management regularly evaluates regulatory pronouncements.

Currency risk

Non-trading currency risk exposure arises principally from the Bank's investments in Debt Securities. The Bank entered into derivative contracts for non-trading purposes only, in order to hedge currency risk. As a consequence, the Bank currently has no material currency risk.

4. Capital resources

As at 31 December 2010, and throughout the period to 31 December 2010, the Bank maintained its capital resources at a level above the minimum Pillar 1 capital adequacy requirements as required by the FSA.

The following table shows the breakdown of the total available capital for the Bank as at 31 December 2010:

Tier 1	31/12/10	30/06/11
	£'000	£'000
Share Capital	8,000	8,000
Share Premium	5,020	5,020
Profit and Loss Account	804	804
Total Tier 1	<u>13,824</u>	<u>13,824</u>
 Tier 2		
Subordinated Loan	1,000	5,000
General Provisions	619	619
Total Capital	<u><u>15,443</u></u>	<u><u>19,443</u></u>

Profits earned since 31st December 2010 are included in the Banks profit and loss account, but are not available for inclusion in capital resources until audited.

5. Capital adequacy

On 1 January 2008, the Bank adopted the requirements of the Basel II Capital Requirements Directive, as set out within the BIPRU chapter of the FSA Handbook.

The Pillar 1 capital requirement, determine in accordance with the rules contained within BIPRU as applied to the Bank, consists of the following components;

Credit risk capital component – the Bank has adopted the standardised approach to determine its Pillar 1 credit risk capital. This involves the application of standard rules to each exposure class.

Operational risk capital requirement – the Bank has adopted the basic indicator approach to determine its Pillar 1 operational risk capital. This calculation is based on the Bank's income and expenditure for the past three years.

5.1. Pillar 1 capital requirement

The table below sets out the Pillar 1 capital requirements as at 31 December 2010 determined in accordance with the BIPRU chapter of the FSA Handbook

Exposure class	Description	Principle constituents	£000's
6	Institutions	<ul style="list-style-type: none"> Cash placed with financial institutions Hedging exposures 	346
7	Retail		446
9	Secured on real estate property	<ul style="list-style-type: none"> Mortgage 	5,917
16	Other items	<ul style="list-style-type: none"> Sundry Debtors and Fixed Assets 	156
Credit risk minimum capital requirement			6,865
Operational risk (<i>basic indicator approach</i>)			765
Pillar 1 capital requirement			7,630
Total capital resources			15,443
Excess of capital resources over Pillar 1 capital requirement			7,813

5.2. Capital management

As shown in the table above, the Bank benefits from a significant surplus of capital resources over and above its Pillar 1 regulatory capital requirement. The Bank has adopted the standardised approach to credit and the basic approach to operational risk since 1 January 2008 in order to calculate the BASEL II Pillar 1 minimum capital requirement.

Pillar 1 capital adequacy is monitored by the Board, and is reported to the FSA on a quarterly basis. Capital forecasts are prepared on an annual basis, as part of the Bank's annual budgeting and forecasting cycle. During the year, additional re-forecasts are also reviewed by the Board to take into account the effects of events that were not reflected in the original budgets.

The Bank's Pillar 2 capital requirements are reviewed formally on a six monthly basis, and additional reviews are undertaken in the intervening periods if management become aware of a material issue or deviation.

5.3. Internal Capital Adequacy Process

On at least an annual basis, the Bank undertakes an Internal Capital Adequacy Assessment Process (ICAAP) which is an internal assessment of its capital needs. This internal process is designed to take account of other risks not covered by the minimum capital requirement.

Included within the ICAAP are capital projections covering a 3-year time horizon, which reflect not only the Bank's chosen strategy and potential growth prospects, but also the results of stress testing these plans. This process is designed to ensure that adequate capital is retained by the Bank to meet not only its current requirements, but also to cover the near future.

The ICAAP is presented to the Board for challenge and approval with the most recent review being completed in August 2010.

6. Credit risk

6.1. Summary of the Bank's credit risk exposures

The gross exposures (before any bad debt provisions) are summarised as follows:

Exposure Class	Description	Exposures at 31 December 2010 £000	Average Exposures Year to 31 December 2010 £000
6	Institutions	21,608	25,191
7	Corporates	-	723
8	Retail	7,429	7,268
10	Secured on real estate property	77,845	70,162
16	Other items	1,945	2,205
		108,827	105,548

The residual maturity of these exposures at 31 December 2010 is shown below.

Exposure Class	Description	Up to 1 year £'000	1-5 years £'000	More than 5 years £'000	Non-interest bearing £'000	Total £'000
6	Institutions	21,608	-	-	-	21,608
8	Retail	2,420	4,956	53	-	7,829
10	Secured on real estate property	76,159	1,686	-	-	77,845
16	Other items	-	-	-	1,945	1,945
		100,187	6,642	53	1,945	108,827

At 31 December 2010 the £ 1,759K of the Banks "Loans secured on Real Estate Property" was to customer in Europe. The remainder of the Banks exposure are to customers in the United Kingdom.

6.2. Overview and terminology

The underlying drivers of credit risk have been described in section 3 of this document. The purpose of this section is to provide more detail in relation to the Bank's credit risk profile and specifically those loans where there may be doubt as to whether the amount loaned will be recovered in full.

The Bank prepares its financial statements in accordance with UK Generally Accepted Accounting Principles ("UK GAAP"). Thus, it is required to make specific provisions against bad or doubtful debts such that the carrying value of each loan is no higher than the amount the Bank expects to recover.

Bad debts are defined as those accounts in default, where the client has failed to meet the terms of their loan, or where insolvency proceedings have been commenced against the client.

Doubtful debts are defined as those accounts where the full recovery of the balance is not considered probable, either as a result of a client falling behind their repayment schedule, or more likely in the case of both development and bridging finance, the value of the security is impaired. Such impairment would therefore result in a shortfall between the sale price of the security and the client's balance outstanding.

Specific provisions have been made against all bad and doubtful debts, based on the expected loss measured on a case by case basis. General provisions have been made in respect of losses inherent in the portfolio.

If the collection of future interest is also considered doubtful, it is suspended and excluded from interest income in the profit and loss account and from the customer balance. Loans and advances are written off to the extent that there is no longer any realistic prospect of recovery.

The following sections explain how these general principles are applied in relation to the Bank's asset portfolios.

6.3. Bad debt provisions

6.3.1	2010	2010	2010	2009	2009	2009
Balance Sheet	Specific	General	Total	Specific	General	Total
movement	£'000	£'000	£'000	£'000	£'000	£'000
At 1 January	6,400	512	6,912	4,135	971	5,106
Charge	1,176	107	1,283	3,792	-	3,792
Released	-	-	-	(270)	(459)	(729)
Written off	(4,704)	-	(4,704)	(1,257)	-	(1,257)
At 31 December	<u>2,872</u>	<u>619</u>	<u>3,491</u>	<u>6,400</u>	<u>512</u>	<u>6,912</u>
Property Finance	2,872	563	3,435	6,400	452	6,852
Asset Finance	-	56	56	-	60	60
	<u>2,872</u>	<u>619</u>	<u>3,491</u>	<u>6,400</u>	<u>512</u>	<u>6,912</u>
6.3.2			2010			2009
Bad and doubtful debts movement in the			£'000			£'000
Profit & Loss account						
Specific and general provision charge			1,283			3,792
Provision released			-			(729)
Write offs during the year			51			454
			<u>1,334</u>			<u>3,517</u>
6.3.3			2010			2009
Interest and fees in suspense			£'000			£'000
At 1 January			4,705			1,966
Suspended during the year			2,996			3,346
Written off			(3,737)			(607)
Released			(358)			-
At 31 December			<u>3,606</u>			<u>4,705</u>

6.4. Credit risk mitigation

For all property lending, the Bank takes security in the form of legal charges over the property against which funds are advanced. This is the primary method used by the Bank to mitigate credit risk. Each security is valued at inception by a qualified surveyor. Further valuations are also requested by the Bank if evidence comes to light that the security may have been enhanced as a result of development activity. In isolated cases, the Bank may

also hold cash collateral in relation to certain residual liabilities associated with a development scheme, and take personal guarantees from the directors/borrowers.

For Asset Finance agreements the Bank has a charge over the assets financed and where appropriate guarantees are taken from the borrower.

The Bank does not use derivatives or other financial instruments (for example insurance) as a means of mitigating credit risk.

7. Interest rate risk

Interest rate risk is described in section 3.4 of this document. Interest rate risk arises within the Bank's lending portfolios as follows:

Development Finance – the majority of the Bank's development lending is at a variable rate, which is linked base rate, and are subject to an interest rate floor.

Bridging and Asset Finance – There loans are made at rate which are fixed for the duration of the loan.

Treasury Assets – the majority of the Bank's cash deposits are for periods of no longer than three months, thus minimising any interest rate risk effects.

In order to mitigate the different risks created by these portfolios the Bank maintains a portfolio of retail deposits which are either linked to base rate or fixed for periods up to 5 years.

Interest rate risk exposures are measured weekly, and reported to ALCO. The position is also reported to the Board.

At 31 December 2010, the Bank's interest rate gap sensitivity, being the impact on the Bank's reported profit before tax over the next 12 months, resulting from a +/- 100bps parallel shift in the yield curve was £691,000 and - £776,000 respectively.

8. Operational risk

Operational risk is described in section 3.6 of this document.

The Bank has the option of using the Basic Indicator Approach or the Standardised Approach in determining the operational risk capital requirement. The Bank has elected to adopt the Basic Indicator Approach.

9. Remuneration

The Bank is a proportionality Tier 3 firm as defined by the FSA's PS10/21. These disclosures are accordingly limited to those required for a firm of this tier.

The remuneration policy of the Bank is determined by the Remuneration Committee, which comprises of two non-executive directors of the Bank, including the Chairman of the Board. The committee operates under an agreed terms of reference from the Board of Directors.

The policy provides a framework to attract, retain and motivate employees to achieve the objectives of the Bank within its stated risk appetite and risk management framework. Remuneration may comprise of base salary and annual cash bonus. Benefits may include holiday allowance, company car, pension scheme, life assurance, private medical insurance, permanent health insurance and staff loans.

Base salary is designed to align the value the individual provides to the Bank, including the skills and competencies required and the contribution to the Bank, in the context of the external market for staff. This is achieved through a job evaluation system based on the job descriptions which assess the knowledge and skills required for the job, the level of thinking and problem solving involved and the degree of accountability or decision making required. Salaries are reviewed annually by the Committee. Non-executive directors receive fees and bonus entitlement, which are set by executive directors.

The annual cash bonus (which is non-share based) is performance based remuneration, designed to drive and reward medium term results, reflecting the level and time horizon of risk. It considers financial and non-financial results and metrics at Bank, division and individual level. The Committee approves the bonus scheme rules in advance, and any proposed payment. A bonus is limited to 50% of total remuneration. The amount of the bonus is determined by the achievement of personal objectives. The Committee may also reward discretionary bonuses if it feels performance warrants it.

The Banks remuneration for the past two years is:

	2010	2009
	£'000	£'000
Total wages and salaries		
- Directors (including Non executives)	802	642
- All other	954	977
	<u>1,756</u>	<u>1,619</u>
Social security costs	193	181
Pension costs	48	54
	<u>1,997</u>	<u>1,854</u>

Remuneration for the year ended 31 December 2010 for the Bank by business area was as follows:

	Lending	Treasury and Central Services	Total
	£'000	£'000	£'000
Wages & salaries	431	1325	1,756
Society security costs	25	168	193
Pension costs	12	36	48
Total remuneration	<u>468</u>	<u>1,529</u>	<u>1,997</u>

The remuneration for the year ended 31 December 2010 in respect of Directors and others considered as Code Staff (senior staff members and risk takers including Non Executive Directors) includes variable remuneration of £74,000.