



(Incorporated in Hong Kong)
Brunei Darussalam Branch
Registered No. RFC20001023

Branch Accounts for the year ended
31 December 2020

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Notation

AMBD Notice No. BU/N-3/2018/53 – Pillar 3 – Public Disclosure Requirements

The above documents may be obtained upon request via hard copy at Bank of China (Hong Kong) Limited, Brunei Branch located at Kiarong Jaya Komplek, Lot 56244, Spg 22, Jalan Ratna, Kampong Kiarong, Bandar Seri Begawan, BE1318, Brunei Darussalam or electronically via brunei_branch@bochk.com

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Bank of China (Hong Kong) Limited

Opinion

We have audited the financial statements of **Bank of China (Hong Kong) Limited – Brunei Branch** ("the Branch"), which comprise the statement of financial position as at 31st December 2020, and the statement of profit or loss and other comprehensive income, statement of changes in head office account and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

The Branch is a segment of **Bank of China (Hong Kong) Limited**, a company incorporated in Hong Kong, and is not a separately incorporated legal entity. The accompanying financial statements have been prepared from the records of the Branch and reflect only transactions recorded locally.

In our opinion,

- a) the accompanying financial statements give a true and fair view of the financial position of the Branch as at 31st December 2020, and of its financial performance and its cash flows for the year then ended in accordance with the provisions of the Brunei Darussalam Companies Act, Cap. 39 and International Financial Reporting Standards according to the best of our information and the explanations given to us and as shown by the books of the Branch.
- b) we have obtained all the information and explanations we required.

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 on the Branch in accordance with the *International Code of Ethics for Professional Accountants (including International Independence Standards)* ("IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in Brunei Darussalam, 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.

Other Information

Management is responsible for the other information. The other information comprises the corporate governance and regulatory disclosure set out on appendices 1 and 2 respectively.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Bank of China (Hong Kong) Limited (continued)

Other Information (continued)

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.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the provisions of the Brunei Darussalam Companies Act, Cap. 39 and International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Branch'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 Branch or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Branch'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 skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Bank of China (Hong Kong) Limited (continued)

Auditor's Responsibilities for the Audit of the Financial Statements (continued)

- 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 Branch's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Branch'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 Branch to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

ERNST & YOUNG
Public Accountants

KONG EE PIN
Registered Public Accountant

Brunei Darussalam
30th March 2021

Statement of Financial Position

As at 31 December		2020	2019
	Notes	B\$'000	B\$'000
Assets			
Cash and short-term funds	4	2,840	4,083
Balances with Autoriti Monetari Brunei Darussalam	5	47,557	47,650
Deposits with banks and other financial institutions	6	193	145
Government Sukuk	7	6,342	19,271
Group balances receivable	8	220,989	182,044
Loans and advances	9	307,454	138,985
Other assets	10	2,008	446
Property and equipment	11	1,803	2,722
Intangible assets	12	279	-
Deferred tax assets	13	47	297
Total Assets		589,512	395,643
Liabilities and Head Office Account			
Deposits from customers	14	288,473	174,055
Group balances payable	15	183,573	107,207
Other liabilities	16	17,676	56,307
Provision for taxation	17	22	-
Head Office Account		99,768	58,074
Total Liabilities and Head Office Account		589,512	395,643

The accompanying notes form an integral part of the financial statements.

Certification:

We certify that the above financial statements give a true and fair view of the financial position of the Brunei Operations of Bank of China (Hong Kong) Limited ("the Branch") as at 31 December 2020 and the financial performance and cash flows of the Branch for the year ended 31 December 2020 in accordance with the provisions of the Brunei Darussalam Companies Act, Cap 39 and International Financial Reporting Standards as issued by the International Accounting Standards Board.

Wang Xiao Lin
General Manager

Zheng Gang
Deputy General Manager

Date: 30 March 2021

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 December		2020	2019
	Notes	B\$'000	B\$'000
Income			
Interest income	19	8,862	6,736
Interest expense	19	(2,351)	(1,762)
Net interest income		6,511	4,974
Fee and commission income	20	3,402	796
Fee and commission expense	20	(284)	(30)
Net fee and commission income		3,118	766
Other operating (loss)/ income	21	(195)	1,223
Total operating income		9,434	6,963
Staff costs	22	(4,745)	(3,009)
Other expenses	23	(2,416)	(2,719)
Total operating expenses		(7,161)	(5,728)
Net impairment charges and recoveries	24	(344)	(418)
Profit from operations		1,929	817
Profit before taxation		1,929	817
Taxation	17	(272)	187
Profit for the year		1,657	1,004
Other comprehensive income			
Items that may be reclassified subsequently to income statement:			
Debt instruments at fair value through other comprehensive income:			
Change in fair value		-	40
		-	40
Total comprehensive income for the year, net of tax		1,657	1,044

The accompanying notes form an integral part of the financial statements.

Statement of Changes in Head Office Account

		Assigned capital	Statutory reserve	Fair value reserve	Accumulated losses	Total
	Notes	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000
Balance as at 1 January 2019		60,000	281	(40)	(3,211)	57,030
Fair value changes		-	-	40	-	40
Profit for the year		-	-	-	1,004	1,004
Transfer during the year	25	-	502	-	(502)	-
Balance as at 31 December 2019		60,000	783	-	(2,709)	58,074
Additional capital	26	40,037	-	-	-	40,037
Profit for the year		-	-	-	1,657	1,657
Transfer during the year	25	-	829	-	(829)	-
Balance as at 31 December 2020		100,037	1,612	-	(1,881)	99,768

The accompanying notes form an integral part of the financial statements.

Cash Flow Statement

For the year ended 31 December

	Notes	2020 B\$'000	2019 B\$'000
Cash flows from operating activities			
Profit before taxation		1,929	817
Adjustment for non-cash items:			
Depreciation of property and equipment and intangible assets		673	659
Depreciation of right-of-use assets		221	149
Interest income from Government Sukuk		(169)	(281)
Interest expense on lease liabilities		11	10
Net impairment loss on financial assets		344	418
Operating profit before change in operating assets and liabilities		3,009	1,772
Change in operating assets and liabilities			
Balances with Autoriti Monetari Brunei Darussalam		(13,571)	(6,820)
Deposits from banks and other financial institutions		(48)	(128)
Group balances receivable		(38,945)	(73,670)
Loans and advances		(168,821)	(71,233)
Other assets		(1,562)	19
Deposits from customers		114,418	64,642
Group balances payable		76,366	64,803
Other liabilities		(38,430)	53,271
Cash (used in)/ generated from operating activities		(67,584)	32,656
Income tax paid		-	-
Net cash (used in)/ generated from operating activities		(67,584)	32,656
Cash flow from investing activities			
Net investment in Government Sukuk		13,101	(7,274)
Purchase of property and equipment		(254)	(292)
Net cash flows generated from/ (used in) investing activities		12,847	(7,566)
Cash flow from financing activities			
Capital injection from Head Office		40,037	-
Interest expense on lease liabilities		(11)	(10)
Payment of principal portion of lease liabilities		(196)	(105)
Net cash flows generated from/ (used in) financing activities		39,830	(115)
Net change in cash and cash equivalents		(14,907)	24,975
Cash and cash equivalents as at beginning of the year		36,416	11,441
Cash and cash equivalents as at end of the year		21,509	36,416
Cash and cash equivalents comprises:			
Cash and short-term funds	4	2,840	4,083
Balances with Autoriti Monetari Brunei Darussalam	5	18,669	32,333
		21,509	36,416

The accompanying notes form an integral part of the financial statements.

Notes to the Financial Statements

These notes form an integral part of the financial statements.

1. Corporate Information

Bank of China (Hong Kong) Limited, incorporated in Hong Kong, has registered a branch in Brunei on 18 June 2016. The registered office of its Brunei Branch (the “Branch”) is at Kiarong Jaya Komplek, Lot No.56244, Simpang 22, Jalan Dato Ratna, Kampong Kiarong, Bandar Seri Begawan, BE1318, Brunei Darussalam.

The Branch is a segment of Bank of China (Hong Kong) Limited and is not a separately incorporated legal entity. The immediate holding company is BOC Hong Kong (Holdings) Limited incorporated in Hong Kong and the ultimate holding company is Central Huijin Investment Limited (PRC), China.

The accounts of the Branch are consolidated in that of BOC Hong Kong (Holdings) Limited. The consolidated accounts of BOC Hong Kong (Holdings) Limited are available to the public on the website.

The Branch is primarily involved in the business of banking and in the provision of financial services. There has been no significant change in the nature of this activity during the year.

2. Basis of preparation

2.1 Statement of compliance

The financial statements have been prepared in accordance with the provisions of the Companies Act, Cap 39 and International Financial Reporting Standards (“IFRS”) as issued by International Accounting Standards Board.

These financial statements were authorised for issue by the management of the Branch on 30 March 2021.

2.2 Basis of measurement

The financial statements have been prepared under the historical cost convention except as otherwise described below.

2. Basis of preparation (continued)

2.3 Functional and presentation currency

These financial statements are presented in Brunei dollars (“BND” or B\$), which is the Branch’s functional currency. All financial information presented in BND has been rounded to the nearest thousand, unless otherwise stated.

2.4 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 accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are as follows:

- (i) The Branch reviews its credit portfolios to assess impairment at least on a quarterly basis. Under IFRS 9, the measurement of impairment losses across all categories of credit asset requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Branch’s Expected Credit Loss (“ECL”) calculations are outputs of complex models. The choice of variable inputs and their interdependencies involves a series of assumptions. ECL models are developed by leveraging on existing internal rating models and loss estimates, behavioural models and forecasting factors. Elements of the ECL models that are considered accounting judgements and estimates include:

2. Basis of preparation (continued)

2.4 Use of estimates and judgements (continued)

- Internal credit rating models, which assign Probability of Defaults to the individual ratings;
- Significant credit deterioration criteria (including internal credit rating downgrade, days past due, drop in Mark-to-Market and qualitative assessment) for assessing whether the financial assets' impairment allowances should be measured on a lifetime ECL basis;
- The segmentation of financial assets according to similar risk and default characteristics when their ECL is assessed on a collective basis;
- Development of ECL models, including the determination of macroeconomic factor forecasts and the effect on Probability of Defaults, Loss Given Defaults and Exposure at Defaults; and
- Selection of forward-looking macroeconomic scenarios and their probability weightings.

It is the Branch's policy to regularly review its models in the context of actual loss experience and adjust when necessary.

- (ii) Fair valuation of financial instruments – selection of valuation models and data inputs for financial instruments with no active markets
- (iii) Provision of income taxes – interpretation of tax regulations on certain transactions and computations.

Please refer to notes 9 and 24 for estimate and judgement applied to the calculation of ECL.

3. Significant accounting policies

3.1 New amendments became effective as at 1 January 2020

The following new amendments became effective as at 1 January 2020:

- Amendments to IFRS 7, IFRS 9 and IAS 39 – *Interest Rate Benchmark Reform*
- Amendments to IAS 1 and IAS 8 – *Definition of Material*
- Amendments to References to the Conceptual Framework in IFRS Standards

The new amendments have no impacts to the accounting policies of the Branch.

3. Significant accounting policies (continued)

3.2 New accounting standards in issue but not yet effective

Amendments to IFRS 7, IFRS 9 and IAS 39 – Interest Rate Benchmark Reform – Phase 2

The amendments address issues that might affect financial reporting when an entity replaces the old interest rate benchmark with an alternative benchmark rate as a result of the Interbank Offered Rate (“IBOR”) Reform. The amendments complement those issued in 2019 and relate to:

- **Changes to contractual cash flows**

A company will not have to derecognise or adjust the carrying amount of financial instruments for changes required by the reform, but will instead update the effective interest rate to reflect the change to the alternative benchmark rate; and

- **Disclosures**

A company will be required to disclose information about new risks arising from the reform and how it manages the transition to alternative benchmark rates.

The amendments are applied retrospectively, except regarding designation of hedging relationships. The comparatives are not restated. Early application is permitted. The Branch is considering the financial impact of the amendments on the Branch’s financial statements.

3.3 Property and equipment

All property and equipment are stated at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditures that are directly attributable to the acquisition and installation of the items.

Subsequent costs are included in an asset’s carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Branch and the cost of the item can be measured reliably. The item is stated at cost less impairment until it begins to generate economic benefits, then the item is subsequently measured according to the measurement basis of its respective assets class. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

3. Significant accounting policies (continued)

3.3 Property and equipment (continued)

Depreciation is calculated on the straight-line method to write down the cost or revalued amount of such assets over their estimated useful lives as follows:

• Renovation	Over the period of 6 years
• Furniture, fixtures and equipment	3 to 10 years
• Motor Vehicles	5 years

The useful lives of assets are reviewed, and adjusted if appropriate, as at the end of each reporting period. At the end of each reporting period, both internal and external sources of information are considered to determine whether there is any indication that property and equipment are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such an impairment loss is recognised in the income statement except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Impairment loss is reversed through the premises revaluation reserve or the income statement as appropriate.

Gains or losses on disposals are determined as the difference between the net disposal proceeds and the carrying amount, relevant taxes and expenses. These are recognised in the income statement on the date of disposal. Any related revaluation surplus is transferred from the revaluation reserve to retained earnings and is not reclassified to the income statement.

3.4 Intangible assets

Intangible assets are reported at cost less accumulated amortisation and accumulated impairment losses. Intangible assets with finite useful lives are amortised on a straight-line basis on the following basis:

• Computer software	3 to 5 years
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The estimated useful lives and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

3. Significant accounting policies (continued)

3.4 Intangible assets (continued)

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in statement of profit or loss as incurred.

An intangible asset is derecognised on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognised in profit or loss when the asset is derecognised.

3.5 Foreign currency transactions

The functional and presentation currency of the Branch is Brunei Dollars (BND). On initial recognition, transactions in foreign currencies are recorded in the functional currency of the Branch at the exchange rate ruling at the transaction date. Subsequent to initial recognition, monetary assets and monetary liabilities denominated in foreign currencies are translated at the closing rate of exchange ruling at the reporting date. Non-monetary items that are measured at historical cost in a foreign currency are translated using the exchange rate at the date of the initial transaction. Non-monetary items measured at fair value in the foreign currency are translated using the exchange rate at the date when the fair value is determined.

Exchange differences arising on the settlement of monetary items or on translating monetary items at reporting date are recognised in the profit or loss statement.

3.6 Fair values of financial assets and liabilities

All financial instruments for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy as defined in IFRS 13, "Fair value measurement". The categorisation are determined with reference to the observability and significance of the inputs used in the valuation methods and based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: based on quoted prices (unadjusted) in active markets for identical assets or liabilities. This category includes equity securities listed on exchange, debt instruments issued by certain governments and certain exchange-traded derivative contracts.

3. Significant accounting policies (continued)

3.6 Fair values of financial assets and liabilities (continued)

- Level 2: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly. This category includes majority of the over-the-counter (“OTC”) derivative contracts, debt securities and certificates of deposit with quote from pricing services vendors, issued structured deposits and other debt instruments.
- Level 3: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable. This category includes equity investment, debt instruments and certain OTC derivative contracts with significant unobservable components.

3.7 Financial Instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Financial Assets

The Branch classifies its financial assets into one of the following measurement categories at initial recognition as subsequently measured at: fair value through profit or loss (“FVPL”), amortised cost and fair value through other comprehensive income (“FVOCI”). The classification depends on the Branch’s business model for managing its financial instruments and the contractual cash flow characteristics of the instruments, or the election of fair value option. All financial assets are recognised initially at fair value. Except for financial assets carried at FVPL, all transaction costs of financial assets are included in their initial carrying amounts.

(i) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets designated at fair value through profit or loss at inception, or financial assets mandatorily required to be measured at fair value through profit or loss, including those held for trading.

A financial asset which has been acquired or incurred principally for the purpose of selling in the short term or 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 is classified as held for trading. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments.

3. Significant accounting policies (continued)

3.7 Financial Instruments (continued)

(i) Financial assets at fair value through profit or loss (continued)

A financial asset, other than those held for trading or mandatorily measured at fair value, will be designated as a financial asset at FVPL, if it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as “an accounting mismatch”) that would otherwise arise from measuring the financial assets or recognising the gains and losses on them on different bases, and is so designated by the Management.

(ii) Financial assets at amortised cost

Financial assets are classified and subsequently measured at amortised cost if both of the following conditions are met: (i) the financial assets are held within a business model with the objective to hold financial assets in order to collect contractual cash flows (“hold-to-collect” business model), and (ii) the contractual terms of the financial asset give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding on specified dates. They are initially recognised at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses. Interest income which includes the amortisation of premium or discount is calculated using the effective interest method and is recognised in the income statement, gains or losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

(iii) Financial assets at fair value through other comprehensive income

Debt instruments are classified as subsequently measured at FVOCI if both of the following conditions are met: (i) the financial assets are held within a business model with the objective of both holding to collect contractual cash flows and selling, and (ii) the contractual terms of the financial assets give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding on specified dates.

3. Significant accounting policies (continued)

3.7 Financial instruments (continued)

Financial Liabilities

(iv) Financial liabilities designated at fair value through profit or loss

This class of instruments includes certain deposits received from customers that are embedded with derivatives. The plain vanilla contracts are valued in the similar way described in previous debt securities section. The fair value of structured deposits is derived from the fair value of the underlying deposit by using discounted cash flow analysis taking the Branch's own credit risk into account, and the fair value of the embedded derivatives determined as described in the paragraph above on derivatives.

(v) Financial liabilities held at amortised cost

Deposits from customers, group balances payable and other liabilities, other than those designated at fair value through profit or loss are carried at amortised cost. Any difference (if available) between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period using the effective interest method.

Recognition and derecognition of Financial Instruments

Loans and receivables (except investment securities without an active market) are recognised when cash is advanced to the borrowers. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Branch has transferred substantially all risks and rewards of ownership. When the Branch neither transfers nor retains substantially all the risks and rewards of ownership of the financial asset, the Branch either continues to recognise the transferred financial asset to the extent of its continuing involvement if control remains or derecognise it if there is no retained control.

Financial liabilities are derecognised from the balance sheet when and only when the obligation specified in the contract is discharged, cancelled or expires. If the Branch purchases its own debt, it is removed from the balance sheet, and the difference between the carrying amount of a liability and the consideration paid is included in net trading gain/loss.

3. Significant accounting policies (continued)

3.8 Impairment of financial assets

The Branch recognises a loss allowance for expected credit losses (ECLs) on the following items:

- Financial assets measured at amortised cost;
- Debt securities measured at FVOCI; and
- Loan commitments and financial guarantees issued, which are not measured at FVPL.

ECLs are a probability-weighted estimate of credit losses. Credit losses are measured as the present value of all expected cash shortfalls. The expected cash shortfalls are discounted where the effect of discounting is material. The maximum period considered when estimating ECLs is the maximum contractual period over which the Branch is exposed to credit risk.

In measuring ECLs, the Branch takes into account reasonable and supportable information that is available. This includes information about past events, current conditions and forecasts of future economic conditions. ECLs are measured on either of the following bases:

- 12-month ECLs: these are losses that are expected to result from possible default events within 12 months after the reporting date; or
- Lifetime ECLs: these are losses that are expected to result from all possible default events over the expected lives of the items to which the ECL model applies.

The Branch will account for expected credit losses within the next 12 months as Stage 1 when those financial instruments are initially recognised; and to recognise lifetime expected credit losses as Stage 2 when there has been significant increases in credit risk since initial recognition. Lifetime expected credit losses will be recognised for credit-impaired financial instruments as Stage 3 if one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred and interest will then be accrued net of the impairment amount of the respective Stage 3 financial assets.

In assessing whether the credit risk of a financial instrument (including a loan commitment and financial guarantee) has increased significantly since initial recognition, the Branch compares the risk of default occurring on the financial instrument assessed at the reporting date with that assessed at the date of initial recognition. In making this reassessment, the Branch considers that a default event occurs when (i) the borrower is unlikely to pay its credit obligations to the Branch in full, without recourse by the Branch to actions such as realising securities (if any is held); or (ii) the financial asset is 90 days past due. The Branch considers both quantitative and qualitative information that is reasonable and supportable, including historical experience and forward-looking information that is available without undue cost or effort.

3. Significant accounting policies (continued)

3.8 Impairment of financial assets (continued)

In particular, the following information is taken into account when assessing whether credit risk has increased significantly since initial recognition:

- failure to make payments of principal or interest on their contractually due dates;
- an actual or expected significant deterioration in a financial instrument's external or internal credit rating (if available);
- an actual or expected significant deterioration in the operating results of the debtor; and
- existing or forecast changes in the technological, market, economic or legal environment that have a significant adverse effect on the debtor's ability to meet its obligation to the Branch.

For loan commitments and financial guarantees, the date of initial recognition for the purpose of assessing ECLs is considered to be the date that the Branch becomes a party to the irrevocable commitment. In assessing whether there has been a significant increase in credit risk since initial recognition of a loan commitment or a financial guarantee, the Branch considers changes in the risk of default occurring on the loan and advances to which the loan commitment/financial guarantee relates.

Depending on the nature of the financial instruments, the assessment of a significant increase in credit risk is performed on either an individual basis or a collective basis. When the assessment is performed on a collective basis, the financial instruments are grouped based on shared credit risk characteristics, such as past due status and credit risk ratings.

ECLs are remeasured at each reporting date to reflect changes in the financial instrument's credit risk since initial recognition. Any change in the ECL amount is recognised as an impairment gain or loss in profit or loss.

The Branch recognises an impairment gain or loss for all financial instruments with a corresponding adjustment to their carrying amount through a loss allowance account, except for investments in debt securities that are measured at FVOCI, for which the loss allowance is recorded in the fair value reserve.

When a financial asset is uncollectible, it is written off against the related allowance for impairment losses. Such assets are written off after all the necessary procedures have been completed and the amount of the loss has been determined. The assets written off are still subject to enforcement activity. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses in the income statement.

3. Significant accounting policies (continued)

3.8 Impairment of financial assets (continued)

If, in a subsequent period, the amount of allowance for impairment losses decreases and the decrease can be related objectively to an event occurring after the impairment loss was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss to the extent of its decrease is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

3.9 Current and deferred income taxes

Tax expenses for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised directly in other comprehensive income. In this case, the tax is also recognised in other comprehensive income.

Income tax payable on profits, based on the applicable tax law enacted or substantively enacted at the end of the reporting period in the jurisdiction where the Branch operates and generate taxable income, is recognised as a current income tax expense in the period in which profits arise.

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantively enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from impairment allowances, depreciation of property and equipment and intangible assets and tax losses carried forward. However, the deferred income tax is not recognised if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss.

Deferred income tax liabilities are provided in full on all taxable temporary differences. Deferred income tax assets are recognised on deductible temporary differences, the carry forward of any unused tax credits and unused tax losses to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences, the carry forward of unused tax credits and unused tax losses can be utilised. Deferred income tax is charged or credited in the income statement.

3. Significant accounting policies (continued)

3.10 Interest income and expense and fee and commission income and expenses

Interest income and expense are recognised in the income statement for all financial assets and financial liabilities using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Branch estimates future cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes fees, premiums or discounts and basis points paid or received between parties to the contract, and directly attributable origination fees and costs which represent an integral part of the effective yield.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised on the written down value using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Subsequent unwinding of the discount allowance is recognised as interest income.

Fee and commission income and expenses that are not an integral part of the effective yield are recognised on an accrual basis ratably over the period when the related service is provided, such as administrative fee, asset management fee and custody services fee.

3.11 Provisions

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

3. Significant accounting policies (continued)

3.12 Employee benefits

Salaries, cash bonuses, allowances, commissions and defined contributions under regulations are recognised in the income statement when incurred. Leave entitlements are recognised when they accrue to employees. Provision for leave entitlements is made based on contractual terms with adjusted for expected attrition.

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and has no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution plans are recognised as staff costs in profit or loss in the periods during which related services are rendered.

The Branch took part in the compulsory pension contribution with Tabung Amanah Pekerja (TAP) and Supplemental Contributory Pension Fund (SCP), where fund for the payment of monthly contributions are made to the TAP and SCP based on a percentage of the gross emoluments excluding certain allowances. The percentage of contributions was determined by TAP and SCP and provided for all members of the local staff.

3.13 Cash and cash equivalents

Cash and cash equivalents comprise balances with original maturity less than three months from the date of acquisition, including cash, balances with banks and other financial institutions, balances placed with Autoriti Monetari Brunei Darussalam (excluding the minimum cash reserve), short-term bills and notes classified as investment securities and certificates of deposit.

3. Significant accounting policies (continued)

3.14 Impairment of non-financial assets

At each reporting date, the Branch reviews the carrying amounts of its non-financial assets (other than deferred tax assets) to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that is largely independent of the cash inflows of other assets or CGUs.

The 'recoverable amount' of an asset or CGU is the greater of its value in use and its fair value less cost to sell. 'Value in use' is based on the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU.

An impairment loss is recognised if the carrying amount of an asset or CGU exceeds its recoverable amount.

Impairment losses are recognised in profit or loss. They are allocated to reduce the carrying amounts of the assets in the CGU on a pro rata basis.

For the assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3. Significant accounting policies (continued)

3.15 Lease

Lessees account for all leases in a similar way as the finance lease accounting under IAS 17, i.e. the lessees recognise and measure the corresponding “right-of-use” asset and lease liability at the commencement date (the date when the underlying asset is available for use by lessees) of the lease by discounting the total future lease payment. Subsequently, the lessees recognise interest expense through the unwinding of the lease liability, and the expense on the depreciation of the right-of-use asset, instead of recognising as rental expenses under operating leases before the implementation of IFRS 16.

After the commencement date, the carrying value of lease liability will be increased to reflect the unwinding of discount through interest expense and will be reduced to reflect the lease payments made. The lease liability will also be remeasured if there is any modification to the lease contracts. Right-of-use assets are depreciated by straight-line method from commencement date to the end of lease term. In case there is a purchase option that is expected to be exercised, then the right-of-use asset will be depreciated to the end of the useful life of the underlying asset.

Right-of-use assets are generally measured at the amount of the lease liabilities plus initial direct costs, estimated dismantling or restoring cost and adjusted by prepaid lease payments. Right-of-use assets are subsequently measured at cost less any accumulated depreciation and any accumulated impairment losses; and adjusted for any remeasurement of the lease liability.

Lease liabilities are the discounted present value of the future cash flows of the non-cancellable lease payments of the lease contracts, after taking into account payments to be made in optional period if the extension option is reasonably certain to be exercised, using the lessees’ incremental borrowing rates at the commencement date of leases as discount rate.

Short-term leases are those leases that have a lease term of 12 months or less which are not capitalised. When the Branch enters into a lease in respect of a low-value asset, the Branch decides whether to capitalise the lease on a lease-by-lease basis. The lease payments associated with those leases which are not capitalised are recognised as an expense on a systematic basis over the lease term.

4. Cash and short-term funds

	2020 B\$'000	2019 B\$'000
Cash in hand	2,840	4,083

5. Balances with Autoriti Monetari Brunei Darussalam

	2020 B\$'000	2019 B\$'000
Balances placed with AMBD	18,669	32,333
Minimum cash reserve	28,888	15,317
	47,557	47,650

The minimum cash reserve is maintained as required by the provisions of Section 45 of the Brunei Darussalam Banking Order 2006. This is not available for use in the Branch's day to day operations. At present the minimum cash reserve requirement is 6% of the deposit liabilities and does not earn interest.

6. Deposits with banks and other financial institutions

	2020 B\$'000	2019 B\$'000
At amortised cost	193	145

7. Government Sukuk

	2020 B\$'000	2019 B\$'000
Debt instrument at fair value through other comprehensive income:		
<u>Government Sukuk held</u>		
Original maturity less than one year	6,343	19,275
Less: Impairment allowances	(1)	(4)
	6,342	19,271

8. Group balances receivable

	2020 B\$'000	2019 B\$'000
<u>Name of the company</u>		
Bank of China (Hong Kong) Limited, Hong Kong	220,989	182,044

The group balances receivable at the year-end are unsecured and interest bearing and repayable on demand.

9. Loans and advances

	2020 B\$'000	2019 B\$'000
Loans and advances analysed by type:		
Term loans		
- Property loans	7,096	7,658
- Other term loans	15,026	25,630
Syndicated loans	81,471	88,846
Overdrafts	2,325	2,404
Trade finance	202,732	15,291
Gross loan and advances	308,650	139,829
Less: Impairment allowances		
- Stage 1 (Note 24)	(1,196)	(844)
Net loan and advances	307,454	138,985

10. Other assets

	2020 B\$'000	2019 B\$'000
Accrued interest receivable	1,449	209
Prepayments	331	103
Sundry debtors	229	135
Less: Impairment allowances	(1)	(1)
	2,008	446

11. Property and equipment

	Right-of-Use Assets	Renovation	Furniture, fixtures & equipment	Motor vehicles	Total
	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000
<u>Cost/ valuation</u>					
As at 1 January 2019	-	1,368	1,905	215	3,488
Initial adoption of IFRS 16	130	-	-	-	130
Additions	691	167	125	-	983
Modification of lease	(130)	-	-	-	(130)
As at 31 December 2019	691	1,535	2,030	215	4,471
Reclassification to intangible assets	-	-	(1,283)	-	(1,283)
Additions	-	43	119	92	254
As at 31 December 2020	691	1,578	866	307	3,442
<u>Accumulated depreciation and impairment</u>					
As at 1 January 2019	-	(323)	(607)	(48)	(978)
Depreciation charge for the year	(149)	(228)	(388)	(43)	(808)
Modification of lease	37	-	-	-	37
As at 31 December 2019	(112)	(551)	(995)	(91)	(1,749)
Reclassification to intangible assets	-	-	744	-	744
Depreciation charge for the year	(221)	(235)	(124)	(54)	(634)
As at 31 December 2020	(333)	(786)	(375)	(145)	(1,639)
Net book value as at 31 December 2020	358	792	491	162	1,803
Net book value as at 31 December 2019	579	984	1,035	124	2,722

The right-of-use assets is related to the leases of premises as its principal place of business, operations and staff accommodation.

12. Intangible assets

	Computer software B\$'000
<u>Cost/ valuation</u>	
As at 1 January 2020	-
Reclassification from property and equipment	1,283
As at 31 December 2020	1,283
<u>Accumulated depreciation and impairment</u>	
As at 1 January 2020	-
Reclassification from property and equipment	(744)
Depreciation charge for the year	(260)
As at 31 December 2020	(1,004)
Net book value as at 31 December 2020	279
Net book value as at 31 December 2019	-

13. Deferred tax assets

	Impairment allowances	Accelerated depreciation for tax purposes	Right-of- use asset and liabilities under IFRS 16	Losses available for offsetting against future taxable income	Total
	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000
1 January 2019	55	(195)	-	250	110
Credited/ (charged) to income statement (Note 17)	77	(64)	-	174	187
31 December 2019	132	(259)	-	424	297
(Charged)/ credited to income statement (Note 17)	93	68	13	(424)	(250)
31 December 2020	225	(191)	13	-	47

14. Deposits from customers

	2020 B\$'000	2019 B\$'000
<u>Analysed by type of deposit:</u>		
Demand deposits	52,019	14,264
Savings deposits	204,223	66,027
Fixed deposits	32,231	93,764
	288,473	174,055
<u>Analysed by type of customer:</u>		
Business enterprises	279,953	157,446
Individuals	8,520	7,527
Central government	-	9,082
	288,473	174,055

15. Group balances payable

	2020 B\$'000	2019 B\$'000
<u>Name of the company</u>		
Bank of China (Hong Kong) Limited, Hong Kong	183,573	107,207

The group balances payable at the year-end are interest bearing and repayable on demand.

16. Other liabilities

	2020 B\$'000	2019 B\$'000
Creditors and accruals	1,422	1,012
Other	15,811	54,651
Lease liabilities	427	623
Impairment allowances on loan commitments and financial guarantees:		
- Stage 1 (Note 24)	16	21
	17,676	56,307

The carrying amount of lease liabilities and the movements during the year are as follows:

	2020 B\$'000	2019 B\$'000
As at 1 January	623	-
Initial adoption of IFRS 16	-	130
Additions	-	641
Accretion of interest	11	10
Dismantling provision	-	50
Modifications	-	(93)
Payments	(207)	(115)
As at 31 December	427	623
Current	238	203
Non-current	189	420
	427	623

The total cash outflow for leases is **B\$ 500 thousands** (2019: B\$ 457 thousands).

17. Taxation

	2020 B\$'000	2019 B\$'000
<u>The tax charge recognised in the profit or loss comprises of the following:</u>		
<i>Current tax expense/ (benefit)</i>		
- Current year	22	-
- Deferred tax (Note 13)	250	(187)
	<u>272</u>	<u>(187)</u>

Provision for taxation:

Balance as at 1 January	-	-
Payment	-	-
Current year tax expense	22	-
Balance as at 31 December	<u>22</u>	<u>-</u>

The tax expense on the results of the Branch differs from the amount that would arise using the Brunei Darussalam statutory rate of income tax due to the following:

	2020 B\$'000	2019 B\$'000
<u>Reconciliation of effective tax rate:</u>		
Profit before income tax	1,929	817
Tax calculated at a tax rate of 18.5%	357	151
Tax effect of non-deductible expenses (net of non-taxable revenue)	9	21
Tax effect of further deduction	(17)	(10)
Threshold exemption	(28)	-
Tax incentives	(18)	-
Origination and reversal of temporary differences	(31)	(349)
Total	<u>272</u>	<u>(187)</u>

18. Commitments and contingencies

In the normal course of business, the Branch makes various commitments and incurs certain contingent liabilities with legal recourse to its customers. No material losses are anticipated as a result of these transactions. As the Contingencies and Commitments may expire without being drawn upon, the notional amounts do not necessarily reflect future cash requirements.

	2020 B\$'000	2019 B\$'000
<u>Contingencies:</u>		
Letters of credit	30,372	2,163
Guarantees, bonds	17	14
Acceptances	-	606
	30,389	2,783
<u>Commitments:</u>		
Undrawn credit lines	61,515	10,304
Total contingencies and commitments	91,904	13,087

19. Net interest income and interest expense

	2020 B\$'000	2019 B\$'000
<u>Interest income</u>		
Group balances receivable	2,298	1,921
Loans and advances	6,395	4,534
Government Sukuk	169	281
Total interest income	8,862	6,736
<u>Interest expense</u>		
Deposits from customers	(1,106)	(358)
Group balances payable	(1,245)	(1,404)
Total interest expense	(2,351)	(1,762)
Net interest income	6,511	4,974

20. Net fee and commission income

	2020 B\$'000	2019 B\$'000
Account services	7	412
Loan commissions	2,860	104
Currency exchange	198	4
Payment services	270	163
Others	67	113
Fee and commission income	3,402	796
Fee and commission expense	(284)	(30)
Net fee and commission income	3,118	766

21. Other operating (loss)/ income

	2020 B\$'000	2019 B\$'000
(Loss)/ gain on foreign currency exchange	(195)	1,223

22. Staff costs

	2020 B\$'000	2019 B\$'000
Wages and salaries	2,889	2,029
Allowance and bonuses	1,763	895
Local contribution plan	93	82
Others	-	3
	4,745	3,009

23. Other expenses

	2020 B\$'000	2019 B\$'000
Administration and general expenses	284	456
Advertising and publicity	89	201
Auditor's fees	41	41
Depreciation of property and equipment and intangible assets	673	659
Depreciation of right-of-use assets	221	149
EDP Expenses	464	531
Expenses relating to short-term leases	290	301
Interest expense on lease liabilities	11	10
Others	195	257
Premises and equipment expenses	67	40
Professional fees	81	74
	2,416	2,719

24. Net impairment charges and recoveries

	2020 B\$'000	2019 B\$'000
Stage 1	(344)	(418)
Stage 2	-	-
Stage 3	-	-
Total	(344)	(418)

Movement in impairment allowances

	2020			
	Stage 1 B\$'000	Stage 2 B\$'000	Stage 3 B\$'000	Total B\$'000
At 1 January	870	-	-	870
Additions	344	-	-	344
At 31 December	1,214	-	-	1,214

24. Net impairment charges and recoveries (continued)**Movement in impairment allowances**

	2019			
	Stage 1 B\$'000	Stage 2 B\$'000	Stage 3 B\$'000	Total B\$'000
At 1 January	452	-	-	452
Additions	418	-	-	418
At 31 December	870	-	-	870

	2020				
	Balance as at 1 January B\$'000	Stage 1 B\$'000	Stage 2 B\$'000	Stage 3 B\$'000	Balance as at 31 December B\$'000
Loans and advances	844	352	-	-	1,196
Government Sukuk	4	(3)	-	-	1
Other assets	1	-	-	-	1
Financial guarantees	1	6	-	-	7
Other commitments	20	(11)	-	-	9
	870	344	-	-	1,214

	2019				
	Balance as at 1 January B\$'000	Stage 1 B\$'000	Stage 2 B\$'000	Stage 3 B\$'000	Balance as at 31 December B\$'000
Loans and advances	449	395	-	-	844
Government Sukuk	-	4	-	-	4
Other assets	-	1	-	-	1
Financial guarantees	2	(1)	-	-	1
Other commitments	1	19	-	-	20
	452	418	-	-	870

25. Statutory reserve

The statutory reserve is maintained in accordance with Section 24 of the Banking Order, 2006. The Branch shall transfer a minimum of 50% of the profit for the financial year to the statutory reserve. The statutory reserve is not distributable as repatriation to the Head Office.

26. Assigned capital

On December 16, 2020, the assigned capital was increased to B\$ 100,037 thousands by capital injection of US\$ 30,000 thousands (equivalent to B\$ 40,037 thousands), which was fully contributed by the Head Office.

27. Accounting classifications and fair values

The Branch's classification of its financial assets and liabilities is summarised in the table below:

As at 31 December 2020

	Carrying Amount			Total
	Amortised cost	Fair value through other comprehensive income	Financial liabilities at amortised cost	
	B\$'000	B\$'000	B\$'000	B\$'000
<u>Assets</u>				
Cash and short-term funds	2,840	-	-	2,840
Balances with Autoriti Monetari				
Brunei Darussalam	47,557	-	-	47,557
Deposits with banks and other financial institutions	193	-	-	193
Government Sukuk	-	6,342	-	6,342
Group balances receivables	220,989	-	-	220,989
Loans and advances	307,454	-	-	307,454
Other assets (excluding prepayments)	1,678	-	-	1,678
	580,711	6,342	-	587,053
<u>Liabilities</u>				
Deposits from customers	-	-	288,473	288,473
Group balances payable	-	-	183,573	183,573
Other liabilities	-	-	17,676	17,676
	-	-	489,722	489,722

27. Accounting classifications and fair values (continued)**As at 31 December 2019**

	Carrying Amount			Total
	Amortised cost	Fair value through other comprehensive income	Financial liabilities at amortised cost	
	B\$'000	B\$'000	B\$'000	B\$'000
<u>Assets</u>				
Cash and short-term funds	4,083	-	-	4,083
Balances with Autoriti Monetari				
Brunei Darussalam	47,650	-	-	47,650
Deposits with banks and other financial institutions	145	-	-	145
Government Sukuk	-	19,271	-	19,271
Group balances receivables	182,044	-	-	182,044
Loans and advances	138,985	-	-	138,985
Other assets (excluding prepayments)	344	-	-	344
	373,251	19,271	-	392,522
<u>Liabilities</u>				
Deposits from customers	-	-	174,055	174,055
Group balances payable	-	-	107,207	107,207
Other liabilities	-	-	56,307	56,307
	-	-	337,569	337,569

27. Accounting classifications and fair values (continued)

Determination of fair value

The methodologies and assumptions used in estimating fair value depend on the terms and risk characteristics of the various instruments and include the following:

Loans and advances

Fair value of loans and advances is estimated by discounting anticipated cash flows (including interest at contractual rates). Performing loans are grouped, to the extent possible, into homogenous pools segregated by maturity and the coupon rates of the loans within each pool. In general, cash flows are discounted using current market rates for instruments with similar maturity, repricing and credit risk characteristics.

For non-performing uncollateralised loans and advances, an estimate is made of the time period to realise these cash flows and the fair value is estimated by discounting these cash flows at the effective interest rate. For non-performing loans and advances where collateral exists, the fair value is the lesser of the carrying value of the loans and advances, net of specific allowances, or the fair value of the collateral, discounted as appropriate.

Based on the methodology described above, the Branch has determined that the carrying values of loans and advances approximate fair values.

Government Sukuk

The carrying value of the Government Sukuk approximate its fair value because of the short periods to maturity.

Deposits by customers

Deposit by customer is calculated using discounted cash flow models, based on the deposit type and its related maturity, applying either market rates, where applicable or current rates offered for deposits of similar remaining maturities.

Based on the methodology described above, the Branch has determined that the carrying value of deposits by customers approximate fair values.

27. Accounting classifications and fair values (continued)**Determination of fair value (continued)****Other financial assets and liabilities**

At the reporting date, the carrying amounts of the other financial assets and liabilities (including cash and short-term funds, balances with Autoriti Monetari Brunei Darussalam, group balances receivable, other assets, deposits with banks and other financial institutions, group balances payable and other liabilities) approximate their fair value because of the short periods to maturity.

28. Related party transactions

(i) Related party shall include Key Management Personnel (KMP), close relatives and other entities. Close relative of a KMP shall include that person's children and spouse. Other related entities shall include entities which are controlled and/or significantly influenced by the KMP or their close relatives.

For the purpose of these financial statements, parties are considered to be related to the Branch if the Branch or its Head Office has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Branch and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

Key management personnel compensation

	2020 B\$'000	2019 B\$'000
Short term employee benefits	1,064	998
Post-employment benefits	-	-
	1,064	998

28. Related party transactions (continued)

	2020		
	KMP	Close relatives	Other related entities
	B\$'000	B\$'000	B\$'000
Income statement			
<u>Income</u>			
Interest income	-	-	-
Other income	-	-	-
Total	-	-	-
<u>Expense</u>			
Interest expense	-	-	-
Other expenses	-	-	-
Total	-	-	-
Balance sheet			
<u>Assets</u>			
Loans and advances	-	-	-
Credit cards	-	-	-
Other assets	-	-	-
Total	-	-	-
<u>Liabilities</u>			
Deposits	734	-	-
Total	734	-	-
<u>Off balance sheet items</u>			
Other commitments and contingencies	-	-	-
Total	-	-	-

28. Related party transactions (continued)

	2019		
	KMP	Close relatives	Other related entities
	B\$'000	B\$'000	B\$'000
Income statement			
<u>Income</u>			
Interest income	-	-	-
Other income	-	-	-
Total	-	-	-
<u>Expense</u>			
Interest expense	-	-	-
Other expenses	-	-	-
Total	-	-	-
Balance sheet			
<u>Assets</u>			
Loans and advances	-	-	-
Credit cards	-	-	-
Other assets	-	-	-
Total	-	-	-
<u>Liabilities</u>			
Deposits	669	-	-
Total	669	-	-
<u>Off balance sheet items</u>			
Other commitments and contingencies	-	-	-
Total	-	-	-

28. Related party transactions (continued)

	2020 B\$'000	2019 B\$'000
Balance sheet		
Group balances receivable	220,989	182,044
Other assets	209	-
Total assets	221,198	182,044
Group balances payable	(183,573)	(107,207)
Other liabilities	(111)	-
Total liabilities	(183,684)	(107,207)
Other commitments and contingencies	-	-
Total off-balance sheet items	-	-
Income statement		
Interest income	2,298	1,921
Total income	2,298	1,921
Interest expense	(1,245)	(1,404)
Fees and commission expense	(240)	-
Other expenses	(111)	-
Total expenses	(1,596)	(1,404)

Terms and conditions of transactions with related parties

The other assets with and borrowings from related parties as at year end are made on terms equivalent to those that prevail in arm's length transactions. The balances at the year-end are unsecured and interest bearing and settlement occurs in cash.

The other liabilities from related parties as at year end are made on terms equivalent to those that prevail in arm's length transactions. Outstanding balances at the year-end are charged with interest bearing and repayable on demand.

There have been no guarantees provided or received for any related party receivables or payables. For the year ended 31 December 2020, the Branch has not recorded any impairment of receivables and payables relating to amounts owed by related parties. This assessment is undertaken each financial year through examining the financial position of the related party and the market in which the related party operates.

29. Capital management

The Branch's approach to capital management is to ensure that the Branch maintains adequate level of capital necessary to support its business and growth, to meet regulatory capital requirements at all times and to maintain a good credit rating.

Head Office Committees oversee the Branch's capital planning and assessment process. Any capital management plans, the contingency capital plans, and any capital management actions are submitted to Head Office senior management team and/or Head Office board for approval.

As a branch of a foreign entity, Head Office is the primary equity capital provider to the Branch, and this is done via Head Office's own retained earnings and capital issuance. Capital generated by the Branch in excess of planned requirements is returned to Head Office by way of repatriations.

The Branch is required to maintain sufficient Capital Funds by the local regulator, Autoriti Monetari Brunei Darussalam (AMBD), to ensure that the relevant regulatory limits as set out in the Brunei Banking Order are complied with. Capital Funds, as defined under by AMBD, is used for the purpose of the above compliance. Besides the Capital Funds requirements, the Branch is also required to set aside the minimum level of eligible assets in Brunei in proportion to its protected deposit liabilities pursuant to the local regulatory requirements. The Branch has complied with the abovementioned regulatory requirements during the period.

The Branch has complied with the minimum capital adequacy ratio for the Bank to meet as required under the Banking Order, 2006 and the methodology for calculating these ratios under the Basel II, Pillar I Framework.

The statutory reserve is maintained in accordance with Section 24 of the Banking Order, 2006. The Branch shall transfer a minimum of 50% of the profit for the financial year to the statutory reserve. The statutory reserve is not distributable as repatriation to the Head Office.

30. Financial risk management

Overview of risk management

The Branch conducts risk assessment in daily operations based on its business activities, sets up risk appetite and risk adjusted return targets as well as different levels of risk limits and Key Risk Indicators (“KRIs”) under the overall risk appetite framework. The risk appetite is cascaded to business units into corresponding performance indicators, so as to supervise business units to make proper adjustments to the Branch’s operations based on current risk status.

The Branch conducts regular assessment on risk management status and risk governance based on regulatory requirements and assesses the Branch’s level of internal capital adequacy accordingly. Key types of risk inherent in the Branch include:

- Credit risk
- Market risk
- Foreign exchange risk
- Interest rate risk
- Liquidity risk
- Operational risk

The risk governance structure of Bank of China (Hong Kong) Limited covers 3 layers: the Board of Directors and its subordinate committees, the senior management and the management level committees, the three lines of defence risk management functions. However, the risk governance structure of the Branch only covers the senior management and the three lines of defence risk management functions.

- **Board of Directors:** Being an overseas branch, the Branch does not have a dedicated Board of Directors. The Board of Directors for Bank of China (Hong Kong) Limited represents the interests of shareholders, and is the highest decision-making authority and has the ultimate responsibility for the oversight of risk management. The Board with the assistance of its committees which includes a Risk Committee has the primary responsibilities for the determination of risk management strategies, risk appetite and risk culture.
- **Senior management:** The Branch’s senior management is responsible in implementing these risk management strategies and ensuring development of policies and procedures for identifying, measuring, monitoring and controlling risk arising from new businesses, products and operating environment, or in response to regulatory changes.

30. Financial risk management (continued)

Overview of risk management (continued)

- **Business unit (front office):** Acts as the first line of defence of risk management and is responsible for soliciting business in compliance with the risk management policies and procedures and within various risk limits, and for assessing and monitoring the risk of their business, and ensuring risk data is correctly entered, kept current and aligned with the data definitions.
- **Risk management unit (middle office):** Independent from the business unit, and responsible for day-to-day management of different kinds of risk. Primary responsibilities for providing an independent due diligence through identifying, measuring, monitoring and controlling risk to ensure an effective check and balance, as well as drafting various risk management policies and procedures. In addition, responsible for reporting the implementation of risk management policies and risk profiles to the Senior Management and for providing support and recommendations for their decision-making.
- **Supporting units (back office):** Responsible for providing proper day-to-day operations support to ensure that there are adequate human resources and systems to support risk management.
- **Internal audit:** Responsible for conducting independent checking, and reporting to the Board on the quality of risk management supervision, the adequacy and the compliance of internal policies and procedures.

30. Financial risk management (continued)

(i) Credit risk

Credit risk is defined as the risk of loss arising from any failure by a borrower or a counterparty to fulfill its financial obligations as and when they fall due. Credit risk exists in the trading book and banking book, as well as from on- and off-balance sheet transactions of the Branch. It arises principally from lending and trade finance.

The Branch has formulated a comprehensive set of credit risk management policies and procedures, and appropriate credit limits to manage and control credit risk that may arise. These policies, procedures and credit limits are regularly reviewed and updated to cope with changes in market conditions and business strategies.

Credit risk exposures are managed through a robust credit underwriting, structuring and monitoring process. The process includes monthly review of all non-performing and special mention loans, ensuring credit quality and the timely recognition of asset impairment. In addition, credit review and audit are performed regularly to proactively manage any delinquency, minimise undesirable concentrations, maximise recoveries, and ensure that credit policies and procedures are complied with. Past dues and credit limit excesses are tracked and analysed by business, product line and risk management units. Significant trends are reported to the Branch's Senior Management and Head Office.

To strengthen the credit risk management framework, the Branch follows the guideline which sets out the operation procedures and requirements with regard to the use of valid internal rating model and relevant approach in credit approval, credit monitoring and reporting of credit risk information. The internal master rating scale can be mapped to Standard & Poor's external credit ratings.

The credit risk from Cash and short-term funds, Balances with Autoriti Monetari Brunei Darussalam, Deposits with banks and other financial institutions, Group balances receivables and other assets are managed by dealing with approved counterparties and within the credit limits.

30. Financial risk management (continued)**(i) Credit risk (continued)**

The table that follows shows the maximum exposure to credit risk for the components of the statement of financial position.

Maximum exposure for the year ended 31 December	2020 B\$'000	2019 B\$'000
Credit exposure for on-statement of financial position		
<u>Financial assets</u>		
Cash and short-term funds	2,840	4,083
Balances with Autoriti Monetari Brunei Darussalam	47,557	47,650
Deposits with banks and other financial institutions	193	145
Government Sukuk	6,342	19,271
Group balances receivable	220,989	182,044
Loans and advances	308,650	139,829
Other assets	1,678	344
Credit exposure for off-statement of financial position		
<u>Financial assets</u>		
Letters of credit	30,372	2,163
Guarantees, bonds	17	14
Acceptances	-	606
Undrawn credit lines	61,515	10,304
Total maximum credit exposures	680,153	406,453

As a fundamental credit principle, the Branch does not grant credit facilities solely on the basis of the collateral provided. All credit facilities are granted based on the credit standing of the borrower, source of repayment and debt service ability.

Collateral is taken whenever possible to mitigate the credit risk assumed. The value of the collateral is monitored periodically. The main type of collateral taken by the Branch is residential and commercial properties, land and cash deposits. Policies and processes are in place to monitor collateral concentration.

30. Financial risk management (continued)

(i) Credit risk (continued)

- Past due and impaired credit facilities

Past due

An asset is considered to be past due when any payment under the strict contractual terms have been missed or received late. The amount included as past due is the entire contractual balance, rather than the overdue portion.

Past due but not impaired loans and advances

Past due but not impaired loans are those for which contractual interest or principal payments are past due, but the Branch believes that impairment is not appropriate on the basis of the level of security/collateral available and/ or the stage of collection of amounts owed to the Branch.

Impaired loans and advances

Advances are credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows have occurred. Credit-impaired advances are classified as Stage 3 and lifetime expected credit losses will be recognised.

The Branch identifies the advances as impaired if the exposure is past due for more than 90 days or the borrower is unlikely to pay in full for the credit obligations to the Branch. The impairment allowances were made after taking into account the value of collateral in respect of such advances.

Classified or impaired advances to customers represent advances which are either classified as “substandard”, “doubtful” or “loss” under the Branch’s classification of loan quality, or classified as stage 3/individually assessed to be impaired.

The Branch’s adopts the Head Office’s internal loans grading criteria which divide credit assets into five categories as below:

“Pass” represents loans where the borrower is current in meeting its repayment obligations and full repayment of interest and principal is not in doubt.

30. Financial risk management (continued)**(i) Credit risk (continued)**

“Special Mention” represents loans where the borrower is experiencing difficulties which may threaten the Branch’s position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.

“Substandard” represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.

“Doubtful” represents loans where collection in full is improbable and the Branch expects to sustain a loss of principal and/or interest, taking into account the net realisable value of the collateral.

“Loss” represents loans which are considered uncollectible after all collection options (such as the realisation of collateral or the institution of legal proceedings) have been exhausted.

Grading analysis of loans and advances that classified under neither past due nor impaired is summarised in the table that follows:

31 December 2020				
	Pass	Special Mention	Substandard or below	Total
	B\$’000	B\$’000	B\$’000	B\$’000
<u>Loans & advances</u>				
Corporate				
- Commercial loans - Stage 1	308,650	-	-	308,650
Less: Impairment allowances	(1,196)	-	-	(1,196)
	307,454	-	-	307,454
31 December 2019				
	Pass	Special Mention	Substandard or below	Total
	B\$’000	B\$’000	B\$’000	B\$’000
<u>Loans & advances</u>				
Corporate				
- Commercial loans - Stage 1	139,829	-	-	139,829
Less: Impairment allowances	(844)	-	-	(844)
	138,985	-	-	138,985

There are no loans and advances that classified under impaired and past due but not impaired.

30. Financial risk management (continued)**(i) Credit risk (continued)**

The following tables present an analysis of other financial assets that are neither past due nor impaired as at:

	31 December 2020		
	Unrated B\$'000	Rated B\$'000	Total B\$'000
Cash and short-term funds	2,840	-	2,840
Balances with Autoriti Monetari Brunei Darussalam	47,557	-	47,557
Deposits with banks and other financial institutions	-	193	193
Government Sukuk	6,342	-	6,342
Group balances receivable	-	220,989	220,989
Other assets	1,677	-	1,677
	58,416	221,182	279,598

	31 December 2019		
	Unrated B\$'000	Rated B\$'000	Total B\$'000
Cash and short-term funds	4,083	-	4,083
Balances with Autoriti Monetari Brunei Darussalam	47,650	-	47,650
Deposits with banks and other financial institutions	-	145	145
Government Sukuk	19,271	-	19,271
Group balances receivable	-	182,044	182,044
Other assets	343	-	343
	71,347	182,189	253,536

30. Financial risk management (continued)**(i) Credit risk (continued)**

- Credit risk mitigation**

Collateral

The Branch's credit risk mitigation policy determines the key considerations for eligibility, enforceability and effectiveness of credit risk mitigation arrangements. The policy articulates the standards to monitor and manage the collateral's security as the secondary repayment source and recovery of obligation loss.

Collateral types that are eligible for risk mitigation include: cash, bank guarantees and standby letters of credit, residential property, commercial property and industrial property, land, fixed assets such as aircraft and vessel.

Estimates of fair value are based on the value of collateral assessed at the time of borrowing. Regular valuation of collateral is required in accordance with the Branch's credit risk policy, which prescribes both the process of valuation and the frequency of valuation for different collateral types. The valuation frequency is driven by the level of price volatility of each type of collateral and the nature of the underlying product or risk exposures.

An estimate of the fair value of collateral and other credit enhancements held against loans and advances to customers and banks, after adjusting for the effect of over-collateralisation and excluding provision made for impairment losses, is shown below:

Collateral	2020	2019
	B\$'000	B\$'000
Gross bills receivable, loans and advances	308,650	139,829
Other contingencies and commitments	91,904	13,087
Less: financial effect of collateral held		
- Cash	(1,591)	(1,446)
- Other physical collateral	-	(103)
- Properties	(11,465)	(13,554)
- Guarantees	(17)	(14)
Net exposure from loans and advances and off statement of financial positions items	387,481	137,799

For other assets in the statement of financial position, the exposure to credit risk equals their carrying amount.

30. Financial risk management (continued)**(i) Credit risk (continued)**

- Concentration risk**

The Branch monitors concentrations of credit risk by sector. The Branch's maximum exposure to credit risk before taking into account any collateral held other credit enhancements and netting arrangements, is shown in the table below:

	2020	2019
	B\$'000	B\$'000
<u>Loans & advances:</u>		
Manufacturing	165,938	63,661
Traders	1,120	15,985
Services	7,283	8,721
Financial	105,019	21,061
Residential & commercial property	29,290	30,401
	308,650	139,829
Less: Impairment allowances	(1,196)	(844)
	307,454	138,985

30. Financial risk management (continued)

(ii) Market risk

Market risk refers to the risk of financial loss where the value of the Branch's assets and liabilities could be adversely affected by changes in market variables such as interest rates, securities prices and foreign exchange rates.

Bank of China (Hong Kong) Limited's market risk management is intended to ensure proper oversight of market risk, assure market risk taking activities are consistent with its risk appetite while optimising risk and return. In accordance with the Bank of China (Hong Kong) Limited's corporate governance principles in respect of risk management, the Board and Risk Management Committee, the Branch's Senior Management and functional departments/units perform their duties and responsibilities to manage the market risk. The Risk and Compliance Department is mainly responsible for managing market risk, assisting senior management to perform their day-to-day duties, independently monitoring the market risk profile and compliance of management policies and limits and ensuring that the aggregate and individual market risks are within acceptable levels.

With reference to Bank of China Hong Kong Limited's market risk management framework, the Branch manages its market risk according to prescribed business requirements and risk tolerance level.

30. Financial risk management (continued)**(iii) Foreign exchange risk**

Foreign exchange risk is the risk to earnings and economic value of foreign currency assets, liabilities and financial derivatives caused by fluctuations in foreign exchange rates.

The following is a summary of the Branch's net exposure to major foreign currencies arising from trading and structural positions, followed by a sensitivity analysis (assuming all other risk variables remain constant):

	Assets/ (Liabilities)	Assets/ (Liabilities)
	2020	2019
	B\$'000	B\$'000
<u>Net trading position:</u>		
Chinese Yuan	(1)	14
Euro	14	4
Hong Kong Dollar	204	232
United States Dollar	(346)	269
	(129)	519
	2020	2019
	B\$'000	B\$'000
<u>Net structural position:</u>		
United States Dollar	40,037	-

A 10% strengthening of BND against the foreign currencies as at year end, would have increased/(decreased) profit or loss by the amounts shown below. The analysis assumes that all other variables, in particular interest rates, remain constant.

	Profit/ (Loss)	Profit/ (Loss)
	2020	2019
	B\$'000	B\$'000
<u>Net trading position:</u>		
Chinese Yuan	(0.1)	1.4
Euro	1.4	0.4
Hong Kong Dollar	20.4	23.2
United States Dollar	(34.6)	26.9
	(12.9)	51.9

A 10% weakening of BND against the foreign currencies as at year end would have had the equal but opposite effect on the amounts shown above, on the basis that all other variables remain constant.

30. Financial risk management (continued)

(iv) Interest rate risk in the banking book (IRRBB)

Interest rate risk means the risks to a Branch's earnings and economic value arising from movements in interest rate and term structures of the Branch's asset and liabilities positions. The Branch's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

- **Repricing risk:** mismatches in the maturity or repricing periods of assets, liabilities and off-balance sheet instruments that may affect net interest income;
- **Basis risk:** different pricing basis for different transactions resulting that the yield on assets and cost of liabilities may change by different amounts within the same repricing period;
- **Option risk:** exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cash flows of assets and liabilities.

The Bank of China (Hong Kong) Limited's risk management framework applies also to interest rate risk management. The Asset and Liability Management Committee ("ALCO") exercises its oversight of interest rate risk in accordance with the "Banking Book Interest Rate Risk Management Policy of Bank of China (Hong Kong), Brunei Branch" approved by Senior Management. Risk and Compliance Department is responsible for monitoring of the execution and management of interest rate risk. Its roles include, but are not limited to, the formulation of management policies, selection of methodologies, setting of risk indicators and limits, assessment of target balance sheet, monitoring of the compliance with policies and limits, and submission of interest rate risk management reports to the senior management and RC, etc. Finance and Accounting Department assists the Risk Management Unit to perform day-to-day interest rate risk management.

The Bank of China (Hong Kong) Limited sets out interest rate risk indicators and limits to identify, measure, monitor and control interest rate risk. The indicators and limits are classified into different levels, which are approved by the Chief Financial Officer ("CFO") and Chief Risk Officer ("CRO"), ALCO, RC accordingly.

The Branch is required to conduct their business within the boundary of the interest rate risk limits as stipulated by Bank of China (Hong Kong) Limited as well as local regulatory guidelines.

30. Financial risk management (continued)**(iv) Interest rate risk in the banking book (IRRBB) (continued)**

Net Interest Income (“NII”) and Economic Value (“EV”) assess the impact of interest rate movement on the Branch’s net interest income and capital base. They are the Branch’s key interest rate risk indicators. The former assesses the impact of interest rate movement on net interest income as a percentage to the projected net interest income for the year. The latter assesses the impact of interest rate movement on economic value (i.e. the net present value of cash flows of assets, liabilities and off-balance sheet items discounted using market interest rate) as a percentage to the latest capital base.

	Impact on net interest income over the next twelve months at 31 December		Impact on reserves at 31 December	
	2020 B\$’M	2019 B\$’M	2020 B\$’M	2019 B\$’M
Total	0.88	0.52	(0.03)	(0.11)

30. Financial risk management (continued)

(v) Liquidity risk

Liquidity risk is the risk that the Branch fails to provide sufficient funds to grow assets or pay due obligations, and need to bear an unacceptable loss. The Branch's maintains sound liquidity risk appetite to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances and stressed scenarios.

The Branch's liquidity risk management objective is to effectively manage the liquidity of on- and off-balance sheet items with reasonable cost based on the liquidity risk appetite to achieve sound operation and sustainable profitability. Deposits from customers are the Branch's primary source of funds. To ensure stable and sufficient source of funds are in place, the Branch actively attracts new deposits, keeps the core deposit and obtains supplementary funding from the interbank market. According to different term maturities and the results of funding needs estimated from stressed scenarios, the Branch adjusts its asset structure (including loans, interbank placement, etc.) to maintain sufficient liquid assets which provide adequate funds in support of normal business needs and ensure its ability to raise funds at a reasonable cost to serve external claims in case of emergency.

The following table shows cash flow analysis of the Branch's liabilities by remaining contractual maturities on an undiscounted basis. Actual maturity dates may differ from contractual maturity dates due to behavioural patterns such as early withdrawal of deposits or loans from counterparties.

30. Financial risk management (continued)**(v) Liquidity risk (continued)**

As at 31 December 2020	Carrying amount	Gross nominal outflow	Up to 1 month	1-3 months	3-12 months	1-3 years	More than 3 years
	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000
<u>Liabilities</u>							
Deposits from customers	288,473	288,492	258,274	30,135	83	-	-
Group balances payable	183,573	183,596	183,596	-	-	-	-
Other liabilities	17,249	17,249	13,117	139	3,859	126	8
Lease liabilities	427	404	24	34	155	190	1
Provision for taxation	22	22	-	22	-	-	-
	489,744	489,763	455,011	30,330	4,097	316	9

As at 31 December 2019	Carrying amount	Gross nominal outflow	Up to 1 month	1-3 months	3-12 months	1-3 years	More than 3 years
	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000	B\$'000
<u>Liabilities</u>							
Deposits from customers	174,055	174,961	93,290	44	81,627	-	-
Group balances payable	107,207	107,371	107,371	-	-	-	-
Other liabilities	55,684	55,663	54,651	97	877	-	38
Lease liabilities	623	611	20	39	155	380	17
Provision for taxation	-	-	-	-	-	-	-
	337,569	338,606	255,332	180	82,659	380	55

30. Financial risk management (continued)

(vi) Operational risk

Bank of China (Hong Kong) Limited – Brunei Branch (“the Branch”) as part of Bank of China (Hong Kong) Limited (“BOCHK”) Group is committed to ensure that the Branch can continuously and effectively develop its business by maintaining an effective operational risk management infrastructure by the abilities to identify, assess, monitor, report, control and mitigate its operational risk.

This is achievable through:

- (i) strengthening the structure of operational risk governance including management policy, procedures, organizational division of functions, accountability and responsibility as well as reporting system;
- (ii) promoting the operational risk management culture so as to strengthen the awareness and expertise of the management and staff towards operational risk management;
- (iii) establishing operational risk management processes, methodologies and modeling techniques so as to enhance the Branch’s operational risk management capabilities.

Operational risk is the risk of loss resulting from inadequate or failed internal process, people and systems, or from external events. This includes reputational and legal risk but excludes strategy and business risk. The risk is inherent in every aspect of business operations and confronted by BOCHK Group in its day to day operational activities. BOCHK Group has implemented the “Three Lines of Defence” for its operational risk management:

- (i) First line of defence – All departments/functional units as the first line of defence are the first parties responsible for operational risk management, and carry out the duties and functions of self-risk control in the process of business operation through self-assessment and self enhancement.

30. Financial risk management (continued)

(vi) Operational risk (continued)

- (ii) Second line of defence – The Legal & Compliance and Operational Risk Management Department (“LCO”), together with certain specialist functions units in the relation to operational risk management within BOCHK Group, including the Human Resources Department, Financial Crime Compliance Department, Information Technology Department, Corporate Services Department, Financial Management Department, Treasury and General Accounting & Accounting Policy Department (collectively known as “specialist functional units”), are the second line of defence. They are responsible for assessing and monitoring the operational risk conditions in the first line of defence, and providing them with guidance. The LCO, being independent from the business units, is responsible for assisting the Management in managing BOCHK Group’s operational risk, including the establishment and review of the operational risk management policy and framework, designing the operational risk management tools and reporting mechanism, and assessing and reporting the overall operational risk position to the Management and Risk Committee. Specialist functional units are required to carry out their managerial duties of the second line of defence with respect to some specific aspects of operational risk and its related issues. Besides taking charge of operational risk management in their own units, these units are also required to provide other units with professional advice/training in respect of certain operational risk categories and to lead the group-wide operational risk management.
- (iii) Third line of defence – Group Audit is the third line of defence which provides independent assessment to the effectiveness and adequacy of the operational risk management framework and is required to conduct periodic audit of the operational risk management activities within BOCHK Group regarding their compliance and effectiveness and to put forward recommendations for remedial actions.

All departments within the Brunei Branch are exposed to operational risk. To ensure operational risk management is effectively managed, Brunei Branch applied locally the three lines of defence in accordance to BOCHK model. Brunei Branch’s Risk & Compliance Department is the second line of defence to lead operational risk management and report operation risk situation to its management and BOCHK LCO. Senior Management of Brunei Branch has direct responsibilities for operational risk management.

BOCHK Group adopts various operational risk management tools or methodologies such as KRI, operational risk and control assessment (RACA), operational risk events reporting and review to identify, assess, monitor and control the risks inherent in business activities and products.

30. Financial risk management (continued)

(vi) Operational risk (continued)

Brunei Branch has developed and implemented the KRI and operational risk events reporting under the guidance of BOCHK LCO to assess the operational risk situations. KRIs results are reported regularly to its management and BOCHK LCO. The scope of reporting covers Operational Loss, Customer Complaints, Staff Turnover, Audit Findings, Compliance Security & Fraud Risk, New Product & Services, Technology Risks & Information Security.

BOCHK Group has established business continuity plans to support business operations in the event of an emergency or disaster. Adequate backup facilities are maintained and periodic drills are conducted. Under the guidance of BOCHK LCO, Brunei Branch continues to improve its business continuity planning, such as business impact analysis, and back-up facilities. In addition, insurance is purchased to mitigate unforeseeable operational risks.

31. Current and non-current assets and liabilities

Current assets and liabilities (expected to be settled or recovered within the next 12 months) and non-current assets and liabilities (not expected to be settled or recovered within the next 12 months) are as follows:

As at 31 December 2020	Current B\$'000	Non-current B\$'000	Total B\$'000
<u>Assets</u>			
Cash and short-term funds	2,840	-	2,840
Balances with Autoriti Monetari Brunei Darussalam	47,557	-	47,557
Deposits with banks and other financial institutions	193	-	193
Government Sukuk	6,342	-	6,342
Group balances receivable	220,989	-	220,989
Loans and advances	213,331	94,123	307,454
Other assets	1,910	98	2,008
Property and equipment	-	1,803	1,803
Intangible assets	-	279	279
Deferred tax assets	-	47	47
	493,162	96,350	589,512
<u>Liabilities and Head Office Account</u>			
Deposits from customers	288,473	-	288,473
Group balances payable	183,573	-	183,573
Other liabilities	17,353	323	17,676
Provision for taxation	22	-	22
Head Office Account	-	99,768	99,768
	489,421	100,091	589,512

31. Current and non-current assets and liabilities (continued)

As at 31 December 2019	Current B\$'000	Non-current B\$'000	Total B\$'000
<u>Assets</u>			
Cash and short-term funds	4,083	-	4,083
Balances with Autoriti Monetari Brunei Darussalam	47,650	-	47,650
Deposits with banks and other financial institutions	145	-	145
Government Sukuk	19,271	-	19,271
Group balances receivable	182,044	-	182,044
Loans and advances	44,168	94,817	138,985
Other assets	446	-	446
Property and equipment	-	2,722	2,722
Deferred tax assets	-	297	297
	<u>297,807</u>	<u>97,836</u>	<u>395,643</u>
<u>Liabilities and Head Office Account</u>			
Deposits from customers	174,055	-	174,055
Group balances payable	107,207	-	107,207
Other liabilities	55,829	478	56,307
Head Office Account	-	58,074	58,074
	<u>337,091</u>	<u>58,552</u>	<u>395,643</u>

AMBD Notice No. BU/N-1/2017/36 – Disclosure of Corporate Governance Arrangements

A copy of the Corporate Governance Policy of BOC Hong Kong (Holdings) Limited ("BOCHK (Holdings)"), the holding company of Bank of China (Hong Kong) Limited ("BOCHK"), can be found at the following website link:

<https://www.bochk.com/en/aboutus/corpgovernance/policy.html>

A copy of BOCHK parent bank's (Bank of China Limited) corporate governance disclosures can be found in the Annual Report of Bank of China Limited at the following website link:

<http://www.boc.cn/en/investor/ir3/>

Corporate Governance Framework at BOCHK Brunei Branch

In line with BOCHK, BOCHK Brunei Branch ("the Branch") is committed to maintaining and upholding high standards of corporate governance in order to safeguard the interests of shareholders, customers and employees. The Board of Directors of BOCHK ("the Board") is at the core of corporate governance framework and there is a clear division of responsibilities between the Board and the Management.

Being a Southeast Asian branch of BOCHK, the Branch does not have a locally established Board of Directors and the Board oversees the Group which includes the Branch. The Board is responsible for providing high-level guidance and effective oversight of the Management. The Board authorizes the Management (Chief Executive ("CE") or the Management Committee ("MC") chaired by CE and other decision making committees designated by CE or MC) to implement the strategies as approved by the Board. The Management is responsible for the day-to-day operations of the Group including overseas branches and reports to the Board. For this purpose, the Board has formulated clear written guidelines which stipulate the circumstances when the Management should report to and obtain prior approval from the Board before making decisions or entering into any commitments on behalf of the Group.

Roles of the Chairman and the Chief Executive

To avoid concentration of power in any single individual, the positions of the Chairman and CE of BOCHK are held by two different individuals. Their roles are distinct, clearly established and stipulated in the Board's Mandate. In short, the Chairman is responsible for ensuring that the Board properly discharges its responsibilities and conforms to good corporate governance practices and procedures. In addition, as the Chairman of the Board, he is also responsible for ensuring that all directors are properly briefed on all issues currently on hand, and that all directors receive adequate, accurate and reliable information in a timely manner.

The CE is responsible for providing leadership for the whole management and implementing important policies and development strategies as adopted by the Board. Led by the CE, the MC fulfills responsibilities including management of the Group's routine operation, implementation of business development strategies and realisation of the Group's long-term targets and strategies.

Under the South East Asia entities Governance structure, the Branch General Manager (“GM”) has direct reporting lines to BOCHK CE and BOCHK Senior Management (Deputy CE and Chief Officers). Local Risk Management and Compliance teams have dual reporting lines to both the Branch’s GM/CRO and the corresponding BOCHK Regional Management Team in Hong Kong. The Corporate Governance policy of the Branch is implemented and monitored via this governance structure but may adopt differentiation in Corporate Governance practice in accordance with local laws/regulatory requirements.

Corporate Governance Policy

BOCHK Group including the Branch recognises the importance of high standards of corporate governance and maintains an effective corporate governance framework which delivers long-term success of the Group. The Group is also strongly committed to embracing and enhancing sound corporate governance principles and practices. The established well-structured corporate governance framework of BOCHK adopted by the Branch directs and regulates the business ethical conduct of the Branch, thereby protects and upholds the interests of shareholders and stakeholders as a whole in a sustainable manner.

However, the following is a summary of deviations noted from local regulatory guidelines on Corporate Governance (“Brunei Guidelines”) with rationale and/or alternative arrangements put in place provided.

1. While the Brunei Guidelines require that the number of executive directors on the Board be kept to the very minimum and there should not be more than one executive director sitting on the Board, BOCHK is adhering to the corporate governance regulations and practice in Hong Kong which allows BOCHK to appoint such number of executive director(s) as it deems appropriate, which is currently one. The Board, which is currently composed of a majority of independent non-executive directors, maintains an appropriate level of checks and balances to ensure independence and objectivity of the decisions of the Board, as well as the impartial oversight of the Management.
2. The Brunei Guidelines require that every Bank should appoint a lead independent director and the independent directors should, under the leadership of this lead independent director, meet periodically without the presence of the other directors and the lead independent director should provide feedback to the Chairman after such meetings. Based on the corporate governance regulations and practice in Hong Kong, although BOCHK is not required to appoint such a lead independent director, the Chairman shall hold meetings with the independent non-executive directors at least annually without the presence of the other directors so as to facilitate open discussion.
3. While the Brunei Guidelines require that a director should not have more than 3 Board representations, BOCHK is adhering to Hong Kong’s regulations that the Board would disclose why it believes a proposed independent non-executive director would still be able to devote sufficient time to the Board if the individual will be holding his/her seventh (or more) listed company directorship. Currently there is no director who holds more than 3 listed company directorships (excluding BOCHK (Holdings)). Moreover, all directors have disclosed to BOCHK their significant commitments and have undertaken and confirmed that they are able to devote sufficient time to the affairs of BOCHK.

4. While the Brunei Guidelines require that a simple majority of directors should constitute a quorum for a meeting of the Board, BOCHK's Articles of Association state that the quorum necessary for the transaction of the business of the directors may be fixed by the directors and unless so fixed shall be two. According to the Mandate of the Board of Directors approved by the Board, the quorum of Board meeting is three directors. In accordance with the guideline issued by the Hong Kong Monetary Authority, independent non-executive directors should, in principle, be prepared to attend all meetings of the Board and should only miss meetings in exceptional circumstances with reasons being provided and documented. In case the independent non-executive directors are not able to attend the meeting via any means, they should submit written views on items to be discussed ahead of the Board meeting. The high attendance record and active participation has been consistently maintained by the directors of BOCHK and disclosed in BOCHK's Annual Report.
5. The Brunei Guidelines require that Banks should have a policy on payment of dividends and should communicate it to shareholders, BOCHK (Holdings) has disclosed its dividend policy in 2020 Annual Report pursuant to the relevant requirement of the Listing Rules.
6. The Brunei Guidelines require that the nomination committee determines annually, and as and when circumstances require, if a director is independent. According to the Mandate of BOCHK's Nomination and Remuneration Committee, the said Committee shall, on an ongoing basis, assess the independence of the independent non-executive directors. Besides, the independent non-executive directors are required to inform BOCHK as soon as practicable if there is any change of circumstances which may affect their independence.
7. According to the Brunei Guidelines, the Board should state in the Bank's Annual Report how the assessment of the Board, its Board Committees and each director has been conducted. If an external facilitator has been used, the Board should disclose in the Bank's Annual Report whether the external facilitator has any other connection with the Bank or any of its directors. BOCHK's Annual Report has disclosed how the assessment of the Board, its Board Committees and each director has been conducted. While there is currently no external facilitator engaged, BOCHK has engaged an external professional consultant to conduct independent review of the effectiveness of the individual directors.
8. The Brunei Guidelines require the Board should also comment in the Bank's Annual Report on whether it has received assurance from the Chief Executive Officer ("CEO") and the Chief Financial Controller ("CFO") (a) that the financial records have been properly maintained and the financial statements give a true and fair view of the Bank's operations and finances; and (b) regarding the effectiveness of the Bank's risk management and internal control systems. As disclosed in the Corporate Governance section of BOCHK's Annual Report: (i) the directors are required by the Hong Kong Companies Ordinance to prepare financial statements that give a true and fair view of the state of affairs of BOCHK, and the directors are responsible for ensuring that the accounting records kept by BOCHK at any time reasonably and accurately reflect the financial position of BOCHK; and (2) the Board oversees the Management in the design, implementation and monitoring of the risk management and internal control systems; according to the Board's scope of delegation, the Management is responsible for the day-to-day operations and risk management, and the Management needs to provide a confirmation to the Board on the effectiveness of these systems.

Risk Management & Internal controls

Refer to Appendix 2 attached to the Annual Report for further details

Internal Audit

Refer to Appendix 2 attached to the Annual Report for further details

Compliance

Refer to Appendix 2 attached to the Annual Report for further details

AMBD Notice No. BU/N-1/2018/51- Amendment No.1 – Disclosure on Risk Management, Credit Risk Management, Internal Audit Function, Compliance and Compliance Function and Internal Control Systems

Risk Management Framework and Internal Control Systems

In line with Bank of China (Hong Kong) Limited (“BOCHK”), BOCHK Brunei Branch (“the Branch”) is committed to maintaining and upholding high standards of corporate governance in order to safeguard the interests of shareholders, customers and employees. The Board is at the core of corporate governance framework and there is a clear division of responsibilities between the Board and the Management.

Being a Southeast Asian branch of BOCHK, the Branch does not have a locally established Board of Directors as BOCHK Board of Directors oversees the Group¹ which includes the Branch. BOCHK’s risk management framework and internal control systems are applicable to and adopted by the Branch. The Board of Directors for BOCHK is responsible for providing high-level guidance and effective oversight of the Management. The Board authorizes and discharges their oversight responsibilities to the Management (Chief Executive (“CE”) or the Management Committee (“MC”) chaired by CE and other decision making committees designated by CE or MC) to implement the strategies as approved by the Board. The Management is responsible for the day-to-day operations of the Group including overseas branches and reports to the Board. For this purpose, the Board has formulated clear written guidelines which stipulate the circumstances when the Management should report to and obtain prior approval from the Board before making decisions or entering into any commitments on behalf of the Group.

The Group’s risk management governance structure is designed to cover all business processes and ensures various risks are properly managed and controlled in the course of conducting business. The Group has a robust risk management organisational structure with a comprehensive set of policies and procedures to identify, measure, monitor and control various risks that may arise. These risk management policies and procedures are regularly reviewed and updated to reflect changes in markets and business strategies. Various groups of risk takers assume their respective responsibilities for risk management.

The Board of Directors, representing the interests of shareholders, is the highest decision-making authority of the Group and has the ultimate responsibility for risk management. The Board, with the assistance of its Committees, has the primary responsibility for the formulation of risk management strategies and ensuring that the Group has an effective risk management system to implement these strategies.

The Risk Management Committee (“RMC”), a standing committee established by the Board of Directors, is responsible for overseeing the Group’s various types of risks, approving risk management policies and monitoring their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it considers that any transaction should

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not proceed. The Audit Committee assists the Board in fulfilling its role in overseeing the internal control system.

The Chief Executive (“CE”) is responsible for managing the Group’s various types of risks, and approving material risk exposures or transactions within his authority delegated by the Board of Directors. The Deputy Chief Executives (“DCEs”) and the Chief Risk Officer (“CRO”) as part of the Senior Management team assist the CE in fulfilling his responsibilities on the day-to-day management of various types of risk, and are responsible for approving material risk exposures or transactions within their authorities delegated by the CE. In addition, the CRO is responsible for initiating new risk management strategies, projects and measures in response to regulatory changes that will enable the Group to better monitor and manage any risks that may arise from time to time from new businesses, products and changes in the operating environment. In accordance with the principle of setting the hierarchy of risk management policies approved by the Board, Senior Management are also responsible for approving the detailed risk management policies of their responsible areas.

Under the South East Asia entities Governance structure, the Branch General Manager (“GM”) has direct reporting lines to BOCHK CE and BOCHK Senior Management (Deputy CE and Chief Risk Officer). Local Risk Management and Compliance teams have dual reporting lines to both the Branch’s GM/CRO and the corresponding BOCHK Regional Management Team in Hong Kong. The Risk Management Framework and internal control systems of the Branch are implemented and monitored via this governance structure.

Various units of the Group have their respective risk management responsibilities. Business units act as the first line of defence while risk management units, which are independent from the business units, are responsible for the day-to-day management of different kinds of risk. Risk management units have the primary responsibilities for drafting, reviewing and updating various risk management policies and procedures.

The Group supplements the analysis of various types of risks with stress testing. Stress testing is a risk management tool for estimating risk exposures under stressed conditions arising from extreme but plausible market or macroeconomic movements. These tests are conducted on a regular basis by the Group’s various risk management units. The Asset & Liability Committee (“ALCO”) monitors the results against the key risk limits approved by the RMC. The Financial Management department reports the combined stress test results of the Group to the Board and RMC regularly.

The Group is committed to upholding good corporate governance practices and the internal control systems are reviewed regularly.

Continuous improvements on the organisation structure, segregation of duty and the risk management policy and procedure have been undertaken. Similar to 2019, the Branch is implementing the disclosure transparency requirements by Autoriti Monetari Brunei Darussalam (“AMBD”) as part of the Branch’s Annual Report to the financial statements for the operations in Brunei Darussalam for the year ended 31st December 2020.

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Credit Risk Management

Please refer to Annual Report Notes 30 for details.

Internal Audit Function

Based on the latest regulatory requirements, guidelines as well as market practices, the Board at BOCHK has established five standing Board Committees to assist in performing its responsibilities, namely the Audit Committee, the Nomination and Remuneration Committee, the Risk Committee, the Strategy and Budget Committee and the Sustainability Committee. The Audit Committee oversees the Group's internal audit function and is responsible for:

- integrity of financial statements and financial reporting process
- monitoring of risk management and internal control systems
- effectiveness of internal audit function and performance appraisal of the General Manager of BOCHK Group Audit ("Group Audit")
- appointment of external auditor and assessment of its qualification, independence and performance and, with authorisation of the Board and shareholders at general meeting, determination of its remuneration
- periodic review and annual audit of the Bank's and the Group's financial statements, financial and business review
- compliance with applicable accounting standards as well as legal and regulatory requirements on financial disclosures
- corporate governance framework of the Group and implementation thereof

Local internal audit function of the Branch has been established since November 2019, with dual reporting lines to Branch Manager administratively and Group Audit functionally. The local internal audit ("IA") team currently has one audit specialist who carries out risk information reporting and ensures audit reviews are timely performed to address major risks effectively. With the direct management approach adopted by Group Audit, the local IA team forms an integral part of Group Audit and is being supported by Group Audit which consists of high caliber professional staff with wide range of expertise that is essential to the effectiveness of the bank's internal audit function.

The Internal Audit Charter of Group Audit articulates the mission, purpose, responsibility and scope of work, accountability, independence and objectivity, authority, strategic and annual audit plan, relationship with other control functions, professional standards, quality assurance and improvement programme, and service standards of the internal audit function within the bank in a manner that promotes an effective internal audit function.

Through the three lines of defence governance structure, Group Audit under Audit Committee endeavours to provide risk-based, independent and objective assurance with a systematic and disciplined approach to assist the Board or its designated Audit Committee and the Management in the discharge of their responsibilities by ensuring all major risks are under good oversight, as well

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as the risk management systems regarding tactics, policies, procedures and internal controls are well implemented and promoted continuously.

Pursuant to a risk-based approach and in accordance with the internal audit plan approved by the Audit Committee, Group Audit conducts independent reviews on such aspects as financial activities, various business areas, various kinds of risks (8 major banking risks within the bank – Credit, Market, Operational, Legal and Compliance, Interest Rate, Liquidity, Strategic and Reputation), operations and activities. The scope of the internal audit function's activities will ensure adequate coverage including matters of local legal and regulatory provisions within the Audit plan. Reports are submitted directly to the Audit Committee and the Management. Group Audit closely follows up on the items that require attention in a systematic way and reports to the Management and the Audit Committee in a timely manner.

In accordance with the Internal Audit Charter, Group Audit shall maintain a quality assurance programme. Group Audit has a delegated quality assurance team for the general audit quality management work of the Department. In addition, every 3 to 5 years, an external consultant will be appointed to perform independent assessment of the internal audit function.

Compliance and Compliance Function

Compliance risk is the risk of legal or regulatory sanctions, financial losses or losses in reputation the Group¹ may suffer as a result of its failure to comply with applicable laws and regulations. Major functions of Compliance risk management aims at improving the overall prevention and control capability of the branch so as to ensure that the branch effectively complies with the regulatory requirements, preventing the punishment on and loss against, or negative impact on the branch due to the failure of rapid response to the changes of external regulatory environment, internal environment and compliance requirements.

The Board of Directors has the ultimate responsibility for the Group's operation and financial fitness, including legal, compliance and reputation risk management. The Board of Directors or its Risk Management Committee is also responsible for the overall supervision of the Group's legal, compliance and reputation risk management.

As documented in the Board Manual on "Matters for the approval of the Board and Matters to be noted by the Board", the Board reviews and assesses annually the effectiveness of the Group's risk management and internal control system. It would cover important monitoring aspects including compliance controls.

The Board approves the Group's high level risk management policies such as the "Legal, Compliance and Reputational Risk Management Policy" which is applicable to the Compliance Function at the Branch. The Group including the Branch should strictly follow this Policy with full commitment to implementing the values of honesty and integrity, and require managers and employees at all levels to comply with this Policy and ensure that all business activities and operations are conducted in accordance with laws and regulations in order to uphold the Group's

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reputation. Key members of the Group, including overseas subsidiary banks and branches must follow the risk management strategies and principles set out in this Policy.

BOCHK Senior Management and the Branch Senior Management have direct responsibility on legal, compliance and reputation risk management. BOCHK Senior Management has the following duties:

- To establish and implement relevant risk management policies;
- To assess and determine the factors that give rise to the above risks; establish and timely adjust the corresponding risk management mechanism, methods and procedures; and to manage the legal, compliance and reputation risks inherent in the Group's business operations;
- To approve contingency plans or crisis management plans to deal with any risk events that have occurred or will potentially occur, and oversee the implementation of remedial measures to mitigate the adverse effect;
- To ensure that the Group has effective and sufficient resources to support all units and staff in implementing this management policy, and supervise LCO or relevant functional units in their performance of risk management.
- To report any significant risk events to the Board of Directors or its authorized committee; regularly report the Group's overall risk evaluation results to the Board of Directors or its authorized committee, and seek advice or approval when necessary; and
- To foster the Group's risk management culture and promote risk awareness across the board.
- To earnestly perform its own compliance duties, set the right tone of compliance and lead by personal example, transmit the correct compliance risk management principles from top to bottom, and form a good compliance culture.

In order to ensure that each unit in the Group manages and supervises their legal, compliance and reputation risks effectively, the "Three Lines of Defence" management model is adopted and implemented across the Group.

The Branch First Line of Defence for Legal and Compliance Risk Management

In accordance with the Group's LCO policy, the Branch is the first line of defence and responsible for legal, compliance and reputation risks within its purview. The Branch's GM/CRO should bear the ultimate responsibilities of their respective legal and compliance risk management and the Branch's GM is the primary responsible person of the Branch and is responsible for the management of the Branch's legal and compliance risk.

BOCHK Second Line of Defence for Legal and Compliance Risk Management

As the designated unit for legal and compliance risk management, LCO of BOCHK is responsible for regulatory compliance; coordinating, managing, supporting, monitoring and following up on legal and compliance risk management of the bank, including the Branch. As a second line of defense, BOCHK LCO will perform on-site/off-site review periodically in order to ensure the Branch has complied with the Group's requirement as well as the related regulations issued by HKMA.

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Three Lines of Defence mechanism of the Branch

The Branch also has a developed “three lines of defence” mechanism and a comprehensive legal and compliance risk management organization structure and management system as its respective internal second line of defence. The Branch’s LCO second line of defence should maintain its independency and professionalism, and independently implement legal and compliance risk monitoring, management and reporting.

The Branch’s LCO will also ensure that the Branch has effectively implemented appropriate procedures to manage the above risks, monitor each unit’s status of implementing the procedures, supervise any corrective actions and deal with breaches, and report breaches and the progress of remedial measures to the BOCHK LCO respective team. The Branch’s LCO will conduct regular risk-based compliance testing and reviews so as to ensure that business and support units effectively execute relevant control measures in daily operations to achieve due compliance with applicable laws and regulations.

Annually, a Compliance Risk Assessment is being performed by the Branch and reported to BOCHK LCO to assess the overall risk profile at the Branch including the improvement in mechanism for legal compliance risk management.

BOCHK Third Line of Defence for Legal and Compliance Risk Management

Group Audit is the third line of defence, which provides independent assessment on the legal, compliance and reputation risk management framework, and is required to conduct periodic audit, assess the effectiveness of the internal control systems and make audit recommendations.

Legal, Compliance and Operational Risk Management Policy and Measures and Reporting Mechanism

The Group has formulated Legal, Compliance and Operational Risk Management Policy (“The Policy”) and the Administrative Measures for Legal and Compliance Risk Management (“The Measures”) to effectively manage and control the legal and compliance risks of BOCHK. The Policy together with the Measures promote and cultivate a sound compliance culture so as to develop all employees to be self-conscious in operational compliance and jointly ensure that the implementation of basic requirements of relevant laws and regulations in all aspects.

The Branch should reference to the major principles and measures of the Policy and Measures, taking its own standards, structures, businesses, existing mechanisms and local legal and regulatory requirements into consideration, formulate relevant management measures (in addition to complying with the Measures, the Branch must also comply with the relevant local regulatory requirements. Whenever there are discrepancies, the more stringent one shall prevail in principle).

The Branch LCO team is required to submit regular risk management reporting to BOCHK LCO which summarizes the legal and compliance risk management of the month. Moreover, the Branch LCO should notify the material and extremely material legal and compliance risk incidents, which

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are defined under the Policy and Measures together with the handling and rectification status to BOCHK LCO immediately.

BOCHK LCO should analyze the specific incident circumstances. BOCHK LCO should report to the Board of Directors, the Risk Committee and Senior Management and, if necessary, follow up on the handling and rectification progress of the relevant incident with the Branch to avoid the occurrence of similar incidents in the Branch. The Branch LCO should organize the compliance review on a timely basis for any material and extremely material legal and compliance risk incidents. There is also a requirement to submit risk incident reporting to BOCHK LCO as part of their oversight of the Branch's compliance risk.

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