LIST OF DEFINITIONS

INTERNAL GOVERNANCE

In these guidelines, the term ‘internal governance’ is used, as opposed to the term ‘corporate governance.’ While corporate governance has a wider scope and includes issues that concern the shareholders and other stakeholders of a credit institution, internal governance focuses on the responsibility of the Board of Directors and senior management. It is mainly concerned with setting the credit institution’s business objectives and its appetite for risk, how the business of the credit institution is organised, how responsibilities and authority are allocated, how reporting lines are set up and what information they convey, and how internal control (including risk control, compliance, and internal audit) is organised.

INTERNAL CONTROL

The Board of Directors is responsible for ensuring that the credit institution has in place the three independent functions that constitute an efficient system of internal control. These functions are risk control, compliance and internal audit. The risk control function ensures that risk policies are complied with. The compliance function identifies and assesses compliance risk. The internal audit function is an instrument for the Board of Directors to ensure that the quality of the risk control function and the compliance function is adequate. Internal control also includes, for example, accounting organisation, treatment of information, risk assessment and measurement systems.

RISKS

For the purposes of this Rule, the risks faced by credit institutions are defined as follows:

Business risks: consists amongst others of credit risk, market risk, interest rate risk, liquidity risk, operational risk, strategic risk and reputation risk.

Concentration risk: as part of credit risk, concentration risk includes (i) large (connected) individual exposures and (ii) significant exposures to groups of counterparts whose likelihood of default is driven by common underlying factors, e.g. sector, economy, geographical location, instrument type.

Credit risk: the current or prospective risk to earnings and capital arising from an obligor’s failure to meet the terms of any contract with the credit institution or its failure to perform as agreed. This risk includes residual risk, the credit risk in securitisation and cross-border (or transfer) risk.

Interest rate risk: the current or prospective risk to earnings and capital arising from adverse movements in interest rates.

IT risk (subcategory of operational risk): the current or prospective risk to earnings and capital arising from inadequate information technology and processing in terms of manageability, exclusivity, integrity, controllability and continuity, or arising from an inadequate IT strategy and policy or from inadequate use of the credit institution's information technology.

Legal and compliance risk (subcategory of operational risk): the current or prospective risk to earnings and capital arising from violations or non-compliance with laws, rules, regulations, agreements, prescribed practices, or ethical standards.

Liquidity risk: the current or prospective risk to earnings and capital arising from a credit institution's inability to meet its liabilities when they become due.

Market risk: the current or prospective risk to earnings and capital arising from adverse movements in bond prices, security or commodity prices or foreign exchange rates in the trading book. This risk can arise from market making, dealing and position taking in bonds, securities, currencies, commodities, or derivatives (on bonds, securities, currencies, or commodities). This risk includes foreign exchange risk, defined as the current or prospective risk to earnings and capital arising from adverse movements in currency exchange rates.

Model risk: the potential loss a credit institution may incur, as a consequence of decisions that could be principally based on the output of internal models, due to errors in the development, implementation or use of such models.

Operational risk: the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This risk includes IT, legal and compliance risk.

Reputation risk: the current or prospective risk to earnings and capital arising from adverse perception of the image of the credit institution on the part of customers, counterparties, shareholders, investors or regulators.

Residual risk (subcategory of credit risk): the risk that recognised risk measurement and mitigation techniques used by the credit institution prove less effective than expected.

Settlement Risk: The risk that the credit institution will deliver the sold asset or cash to the counterparty and will not receive the purchased asset or cash as expected. As such, a settlement risk comprises credit risk and liquidity risk.

Strategic risk: the current or prospective risk to earnings and capital arising from changes in the business environment and from adverse business decisions, improper implementation of decisions, or lack of responsiveness to changes in the business environment.

OTHER DEFINITIONS

For the purpose of this Rule and the Annexes certain definitions are as follows:

Discretionary pension benefits: enhanced pension benefits granted on a discretionary basis by an institution to an employee as part of that employee's variable remuneration package, which do not include accrued benefits granted to an employee under the terms of the company pension scheme.

Securitisation special purpose entity (SPPE): a corporation trust or other entity, other than an institution, organised for carrying out a securitisation or securitisations, the activities of which are limited to those appropriate to accomplishing that objective, the structure of which is intended to isolate the obligations of the SSPE from those of the originator institution, and in which the holders of the beneficial interests have the right to pledge or exchange those interests without restriction.