



Amex Bank of Canada

Basel Pillar III Disclosures
December 31, 2016



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Basel Pillar III Disclosures

1 Scope of application

This document has been prepared to address the Basel Pillar 3 disclosure requirements for Amex Bank of Canada (the Bank). The Bank, incorporated under the Bank Act of Canada (the Bank Act), is a wholly owned subsidiary of American Express Travel Related Services Company, Inc. (TRS Co.). The Bank is licensed to operate as a schedule II bank in Canada (foreign bank subsidiary). The Bank's principal activities include issuing credit cards, charge cards and lines of credit and providing merchant and network services in Canada.

TRS Co. is incorporated in the United States of America (USA). The ultimate parent company of the Bank, American Express Company (AXP) is a "Bank Holding Company" under the Bank Holding Company Act of the USA and is regulated by the Federal Reserve Board in the USA.

The following disclosures have been prepared solely for the purpose of satisfying the Basel Pillar 3 disclosure requirements pertaining to capital requirements and management of certain risks. These disclosures are unaudited and are not to be considered part of the Bank's financial statements. The disclosures should not be relied upon in making any investment in the Bank's ultimate parent company, AXP.

All amounts reported in these disclosures are presented in thousands of Canadian dollars, unless otherwise noted.

Risk management framework

The Bank is exposed to the following types of risks: credit, asset liability (which includes structural interest rate and foreign exchange risk), funding & liquidity, operational, strategic and reputation risks. The objective of management and the Board of Directors of the Bank (the Board) is to minimize the Bank's exposure and to reduce business risks to acceptable levels.

Effective risk management is central to the Bank's ability to remain financially sound and the Bank has adopted an Enterprise Risk Management (ERM) Framework for the identification, measurement, monitoring and management of risks faced across the entity. The Bank's Enterprise Risk Management Policy (the ERM Policy) describes how the Bank seeks to manage key risks on an enterprise basis. The general framework for ERM has been approved by the Risk Review Committee (RRC) of the Bank's Board after recommendation by the VP & Chief Risk Officer (CRO) and the Enterprise Risk Management Committee (ERMC). It sets forth the Bank's risk appetite, assigns governance responsibilities to ensure that the Bank's risk profile aligns with that appetite, and prescribes rules for escalating risk issues between Committees, including the RRC. The ERM Policy also provides guidance to management for the development and maintenance of a framework for identifying, measuring and reporting risk concentrations throughout the Bank, and for the maintenance of risk policies addressed to particular types of risks.

Risk management structure

The details of the assignment of risk management responsibilities to the committees and key officers are detailed in the Bank's individual and committee mandates approved by the Board. The risk committees of the Bank are:

Risk Review Committee (RRC) of the Board of Directors
Enterprise Risk Management Committee (ERMC)
Operational Risk Management Committee (ORMC)
Credit Risk Committee (CRC)

Asset Liability Committee (ALCO)
Outsourcing Risk Committee (ORC)

Risk universe

The Bank's ERM framework includes the identification of the universe of risks (the "Risk Universe") inherent in the Bank's businesses. Policies, procedures, and risk limits are developed to ensure risks set out in the Risk Universe are managed within the risk appetite of the Bank. Senior management, officers and employees of the Bank are accountable for all risks inherent in their business operations. Risks are identified, assessed, managed, reported and monitored in accordance with the Bank's policies and procedures. The CRO is responsible for leading the development, maintenance and presentation of the Bank's Risk Universe. The Risk Universe is reviewed and approved by the ERM and RRC on an annual basis.

Aggregate risk

The Bank seeks to balance the aggregate amount of risk it accepts against its capital and earnings. To accomplish this, quantitative limits are established against internal risk measures and the levels of aggregate risk are monitored accordingly. The primary aggregate measure of risk used by the Bank is Economic Capital.

2 Capital structure and adequacy

The Bank follows the Capital Adequacy Requirements (CAR) Guidelines of the Office of the Superintendent of Financial Institutions (OSFI) for the measurement and reporting of its regulatory capital ratios. The guidelines are based on the capital framework issued by the Basel Committee on Banking Supervision, which includes Basel II: International Convergence of Capital Measurement and Capital Standards: A Revised Framework and Basel III: A global regulatory framework for more resilient banks and banking systems. The Bank follows the Basel III Leverage Ratio Framework for measurement and reporting of the Bank's Leverage Ratio.

Consistent with OSFI requirements pertaining to simpler approaches under Basel III, the Bank has adopted the Standardized Approach to measuring credit risk and the Basic Indicator Approach to measuring operational risk. Market risk for the Bank is immaterial and the Bank is not currently engaged in business transactions that require calculation and reporting of Market risk. The Bank is not currently required to maintain a Counter-Cyclical Capital Buffer as the same has not been activated by Office of the Superintendent of Financial Institutions.

The Bank's primary capital management objectives are to:

- ensure that the Bank's capital is of sufficient quality and quantity to comply with, at all times, external regulatory requirements;
- maintain adequate capital to act as a safeguard for the variety of risks the Bank is exposed to; and
- maintain a strong capital base to support future business growth.

The Board has ultimate responsibility for overseeing capital adequacy and capital management. The Board reviews and approves the Bank's Capital Policy, the annual capital plan and reviews the adherence to capital limits and targets.

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The ALCO, chaired by the VP and Treasurer, establishes and maintains the capital management framework and an Internal Capital Adequacy Assessment Process (ICAAP), which it utilizes to achieve its capital goals and objectives. The Bank's ICAAP is an integrated enterprise wide process that encompasses the governance, management, and control of risk and capital functions within the Bank. It provides a framework for relating risks to capital requirements through the Bank's economic capital modeling and stress testing practices and helps determine the Bank's capital adequacy requirements.

The ALCO assesses whether the Bank's internal view of required capital is appropriate for the Bank's risks, determines the adequacy of the Bank's available capital in relation to required capital and recommends internal capital targets, over and above the minimum levels established by OSFI, which align with the Bank's risk appetite and are approved by the Board.

As at December 31, 2016, under the Basel III framework, the regulatory capital of the Bank consisted of Tier 1 capital (common shares, retained earnings and contributed surplus). As at December 31, 2016, the Bank had no Tier 2 capital.

The following table presents the Bank's regulatory capital, capital ratios and leverage ratio. As at December 31, 2016, the Bank was in compliance with the capital and leverage ratio guidelines issued by OSFI under Basel III, as well as its internal requirements.

Basel III Framework

| As at December 31: | 2016 |
|--|------------------|
| Regulatory capital | |
| Common shares | 206,000 |
| Contributed surplus | 9,155 |
| Other Comprehensive Income | (13) |
| Retained earnings | 646,321 |
| Common Equity Tier 1 capital | 861,463 |
| Regulatory adjustments to Common Equity Tier 1 capital | (4,154) |
| Tier 1 capital | 857,309 |
| Total capital | 857,309 |
| Risk weighted assets | |
| Credit risk | 2,938,334 |
| Operational risk | 1,567,450 |
| Total risk-adjusted assets | 4,505,784 |
| Capital ratios | |
| CET ratio | 19.03% |
| Tier 1 ratio | 19.03% |
| Total capital ratio | 19.03% |
| Leverage ratio | 14.30% |

The Bank is currently exceeding all minimum capital adequacy requirements under Basel III.

3 Credit risk management

One of the most significant risks to the Bank is credit risk. Credit risk is the risk of loss if a borrower or counterparty in a transaction fails to meet its agreed payment obligations resulting in the Bank incurring a financial loss.

Every loan or extension of credit by the Bank to other parties exposes the Bank to some degree of credit risk. The Bank's primary objective is to be methodical in its credit risk assessment so that it can better understand, select, and manage exposures to reduce significant fluctuations in earnings.

The Bank recognizes that its ability to accept and manage credit risk successfully depends on the sound design and implementation of business processes and risk controls.

Credit Risk Committee structure

The RRC, the President & Chief Executive Officer (CEO), the VP & Chief Risk Officer (CRO) and the ERMC have responsibility for risk management at the Bank. To support the RRC, the CEO, the CRO and the ERMC in the exercise of that responsibility, the Bank has established a management-level governance structure to oversee and direct the management of credit risks in the Bank.

The principles that are applied in the management of credit risk include, but are not limited to:

- The Bank's CRC meets monthly to review significant accounts, breach of review triggers and to review and approve changes to the Bank's credit policy. Credit triggers are escalated to the ERMC and to the RRC based on established threshold;
- Specific exposure and economic capital limits have been established for the reporting of significant credit exposures to the Board;
- Management of the Bank's overall loan portfolio to ensure broad diversification of credit risk and to limit concentrations of correlated risks (i.e. industry risks);

Credit risks in the Bank are divided into two broad categories: Individual and Institutional. The Bank defines individual credit risk as the risk of loss to the Bank due to non-payment of an amount contractually owed to the Bank by an individual, whether acting as an individual or on behalf of his or her small business or corporation. The Bank defines institutional credit risk as the risk of loss to the Bank due to non-payment of an amount contractually owed to the Bank by a business or organization; or due to a change in the credit quality of a security held in the Bank's investment or liquidity portfolios.

Individual and Institutional credit risks are measured separately and each have distinct risk management tools and metrics. Business units that create individual or institutional credit risk exposures of significant importance are supported by dedicated risk management teams reporting to the Chief Credit Officer (CCO). To preserve independence, risk officers have reporting relationships within the risk management organization and not to the business units. The CRO also has a reporting line, for functional purposes, to the RRC in addition to Bank and organizational reporting lines.

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The Bank recognizes that there is inherent credit risk associated with the Bank's assets which are presented as at December 31 in the following table:

| | 2016 |
|---|------------------|
| Deposit with regulated financial institutions | 351,319 |
| Short term marketable securities | 354,880 |
| Cardmember receivables and loans, net of allowances | 3,222,448 |
| Other receivables | 132,155 |
| | <u>4,060,802</u> |

Capital measurement of credit risk

In accordance with the Standardized Approach to measuring credit risk outlined in OSFI's CAR guideline, the Bank uses the Standard and Poor's information as the external credit assessment institution (ECAI) for claims on sovereign. For exposures to banks or deposit-taking institutions, the risk weight applied to a claim on the bank is dependent on the external credit assessment of the sovereign in the bank's country of incorporation. ECAI is not used for corporate exposures as the Bank has chosen to apply a 100% risk weight to corporate exposures.

The following table includes the Bank's net credit risk exposures, after risk mitigation, in each risk bucket as at December 31:

| Risk buckets | 2016 |
|---------------------|-------------------------|
| 250% | 16,022 |
| 150% | 17,113 |
| 100% | 828,221 |
| 75% | 2,632,166 |
| 20% | 351,319 |
| 0% | 358,446 |
| | <u>4,203,287</u> |

Credit risk mitigation

Credit risk mitigation techniques available in the CAR Guideline include collateralized transactions, on-balance sheet netting and guarantees / credit derivatives. The Bank does not currently make use of on- and off-balance sheet netting or credit derivatives.

The Bank holds certain collateral as security in the event that cardmember receivables age past due. The collateral is in the form of guarantees (letters of credit), however these letters of credit are not used to mitigate exposures for regulatory capital purposes and the amount of exposure which is covered by letters of credit is not material as a percentage of the overall portfolio.

Additionally, the Bank has an agreement with a corporate customer whereby the customer is required to hold funds in an investment account which is hypothecated to the Bank. The Bank has opted to take the comprehensive approach for this specific collateralized transaction, where eligible financial collateral for this corporate customer is taken as a risk mitigation measure. As at December 31, 2016, there was \$43,598 owing to the Bank by the corporate customer.

Individual credit risk mitigation

General principles and the overall framework for managing individual credit risk across the Bank are defined in the Bank's Individual Credit Risk Policy and are approved by the RRC. This policy is further supported by a highly organized structure of subordinate procedures covering all facets of consumer credit extension during the customer lifecycle, new account approvals, line management, authorizations, collections, and fraud prevention. These policies and procedures ensure consistent application of credit management principles and standardized reporting of asset quality and loss recognition. Moreover, individual credit risk management is supported by sophisticated proprietary scoring and decision-making models.

Credit underwriting decisions are made based on sophisticated evaluation of product economics and customer behavior predictions. The Bank has developed unique decision logic for each customer interaction and each decision benefits from sophisticated modeling capability that uses the most up-to-date proprietary information on customers, including payment history, purchase data, as well as insights from data feeds from credit bureaus.

Institutional credit risk mitigation

General principles and the overall framework for managing institutional credit risk across the Bank are defined in the Bank's Institutional Credit Risk Policy approved by the RRC. The ERM is responsible for the implementation and enforcement of this policy and for providing guidance to the credit officers of each business unit with substantial institutional credit risk exposures, who in turn make investment decisions in core risk capabilities, ensure proper implementation of the underwriting standards and contractual rights of risk mitigation, monitor risk exposures, and determine risk mitigation actions.

The Bank has established a set of risk limits to ensure it can sustain potential losses from the credit risk it is taking without significant impediment to its ability to conduct business. These risk limits are defined in the Bank's ERM Policy. In addition, the Bank has established and maintains risk escalation thresholds for every institutional obligor to which it has credit exposure. The Bank also monitors the risk exposures to classes of institutional obligors in common industries, or with common credit ratings.

Concentrations of credit risk exist when changes in economic, industry or geographic factors similarly affect groups of counterparties whose aggregate credit exposure is material in relation to the Bank's total credit exposure. The Bank's customers generally operate in diverse industries, economic sectors and geographic regions. The Bank manages concentration risk in line with Board approved escalation triggers.

Single-name concentration, as well as other concentrations like industry segments, are thoroughly monitored as per the Institutional Credit Risk Policy of the Bank, which defines triggers for committee escalations. Actual single-name notional exposure and economic capital are monitored to ensure they are within approved escalation triggers. Trigger breaches are reviewed with Business Leaders, and a risk-return analysis is performed to justify request for trigger increase or scale-down of exposure. Report on single-name concentration, industry and rating concentration are presented to the CRC and ERM monthly, and to the Board RRC quarterly.

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The following table presents the Bank's assets which are subject to credit risk, net of allowance for credit losses, by industry and counterparty risk at December 31:

| | 2016 |
|--|------------------|
| Institutions ¹ , including cardmember receivables and loans | 1,116,942 |
| Individuals, including cardmember receivables and loans | 2,588,980 |
| Government and Agencies | 354,880 |
| | <u>4,060,802</u> |

¹ Institutions include corporations and financial institutions.

The following table represents the Bank's assets subject to a degree of credit risk by geographic distribution as at December 31, 2016:

| | Western | Central | Other within and outside of Canada | Total |
|---|----------------|------------------|--|------------------|
| Within Canada by region: | | | | |
| Deposits with regulated financial institutions | - | 351,319 | - | 351,319 |
| Short term marketable securities | - | 354,880 | - | 354,880 |
| Cardmember / other receivables and loans, net of allowances | 842,058 | 2,375,812 | 136,733 | 3,354,603 |
| | <u>842,058</u> | <u>3,082,011</u> | <u>136,733</u> | <u>4,060,802</u> |

Collective allowance

For the purposes of a collective evaluation of impairment, cardmember loans and receivables are grouped on the basis of similar risk characteristics, taking into account asset type, industry, geographical location, collateral type, past due status and other relevant factors. These characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the counterparty's ability to pay all amounts due, according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted based on current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist. These adjustments relate to events and conditions existing at statement of financial position date to ensure reflection of incurred losses only.

Cardmember loans and receivables are classified as impaired when, in the opinion of management, there is reasonable doubt as to collectability, either in whole or in part, of principal and interest, which is generally determined by the number of days past due. Cardmember loans and receivables are considered past due when the cardmember has failed to make a payment when contractually due. Cardmember loans and receivables where the cardmember has filed for bankruptcy or where the cardmember has become deceased are written off upon receipt by the Bank of notification. Cardmember loans and receivables, other than bankrupt and deceased accounts, are written off if uncollected no later than 180 days past due.

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Impaired loans may include loans and receivables that have been modified for borrowers who are experiencing financial difficulties. The Bank may modify cardmember loans and receivables and such modifications may include reducing the interest rate or assessment fees on the loans and receivables and/or placing the cardmember on a fixed payment plan not exceeding 12 months. If the cardmember does not comply with these terms, then the loan or receivable agreement reverts back to its original terms.

As at December 31, 2016, the Bank had an allowance for loan losses of \$61,354, of which \$3,064 represents the allowance for institutional cardmember receivables and \$58,290 represents the allowance for individual cardmember receivables and loans.

The following table includes cardmember loans and receivables which are past due as at December 31, 2016 by counterparty type:

| | <u>1 - 90 days past due</u> |
|---|---------------------------------|
| Individual cardmember receivables and loans past due and not impaired | 62,329 |
| Institutional cardmember receivables past due and not impaired | 94,206 |

Included in the table below are the changes in the allowance for losses for the 12 months ended December 31:

| | <u>2016</u> | | |
|-----------------------------|-------------------|----------------------|--------------|
| | <u>Individual</u> | <u>Institutional</u> | <u>Total</u> |
| Balance - beginning of year | 66,919 | 3,774 | 70,693 |
| Net write-offs | (77,849) | (6,443) | (84,292) |
| Provision for credit losses | 69,220 | 5,733 | 74,953 |
| Balance - end of year | 58,290 | 3,064 | 61,354 |

As at December 31, 2016, the Bank had impaired individual card member loans of \$9,956.

Counterparty credit risk

The Bank manages its counterparty credit risk exposures by setting internal limits and escalation triggers based on total exposure and ratings of the counterparties. The CRO of the Bank monitors compliance to internal limits and reports to the CRC and ERM on a regular basis.

The Bank may use derivatives in the form of foreign exchange funding forwards. Credit risk associated with the Bank's derivatives is limited to the risk that a derivative counterparty will not perform in accordance with the terms of the contract, however credit exposure related to the Bank's foreign exchange funding forwards is minimal because the Bank's sole derivative counterparty is a related company which has high credit ratings as assigned by the major credit rating agencies of Moody's Standard & Poor's, Fitch Ratings and DBRS. As at December 31, 2016, there were no foreign exchange forward contracts outstanding.

4 Asset liability management

Asset and Liability (ALM) risk is the risk to earnings or value resulting from unfavourable movements in market prices impacting the structural balance sheet. The Bank incurs ALM risk exposures as a natural accompaniment to its business model in the regular course of offering its products and services. The Bank's Asset Liability Management Policy describes how the Bank seeks to manage ALM risk in the banking book on an enterprise-wide basis. It assigns key governance responsibilities, prescribes rules for escalating risks to the ERM and RRC, and sets forth the Bank's guidelines for measuring, assessing, and reporting ALM risk. The policy is a Board-approved policy, maintained by the VP and Treasurer and is an integral part of the Enterprise-Wide Risk Management Policy.

Structural interest rate risk in the banking book

The Bank's interest rate risk exposure is primarily generated by interest rate risk in its card businesses. Interest rate risk arises through the funding of cardmember receivables and fixed-rate loans with variable-rate borrowings.

Interest rate exposure within the Bank's charge card and lending products is managed by varying the proportion of total funding provided by variable-rate debt and deposits compared to fixed-rate debt.

The primary source of interest rate risk to which the Bank is exposed is re-pricing risk. Timing differences in the maturity and re-pricing of the Bank's assets and liabilities may lead to changes in the Bank's earnings, net interest income and economic value. The Bank may change the mix between variable-rate and fixed-rate funding based on changes in business volumes and mix, among other factors.

Other sources of interest rate risk such as yield curve risk, basis risk, and optionality risk are considered to be minimal sources of interest rate risk for the Bank.

The Bank uses a mix of fixed and floating funding to manage its exposure to movements in interest rates within Board approved limits.

The Bank's credit cards are spread products and as such, the Bank manages the interest rate risk on these assets by matching the maturity and/or pricing reset periods of the instruments to the sources used to fund the receivables. Interest rate exposure is mitigated by the fact that the Bank can raise the interest charged on its credit products within one month.

The following sources are available to the Bank to fund its cardmember loans and receivables:

- Long term credit arrangement with a related party;
- Short term credit arrangements with a related party;
- Internal funding, such as equity;
- External funding, such as short-term money market loans and retail deposits; or
- Selling card receivables to an affiliated company.

The Bank has established Board approved limits and internal management triggers expressed in the form of Earnings at Risk and Economic Value of Equity. The Bank measures and monitors its exposure to structural interest rate risk by performing monthly analysis to measure the Bank's repricing risk under various interest rate stress scenarios. The Bank monitors and reports compliance with its management triggers and Board limits to the ALCO, ERM and RRC.

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The table below summarizes the re-pricing profiles of the Bank's financial instruments and other assets and liabilities at their carrying value as at December 31. Items are allocated to time periods by reference to the earlier of the next contractual interest rate re-pricing date and the maturity date.

| | Floating rate | 0 – 3 months | 3 – 12 months | 1 – 5 years | Non-rate sensitive | Total |
|--|------------------|--------------|------------------|-------------|-----------------------|-----------|
| 2016 | | | | | | |
| Total assets | 44,394 | 1,143,980 | 462,658 | 113,298 | 2,425,354 | 4,189,684 |
| Total liabilities | - | 1,262,614 | 577,931 | 575,000 | 912,676 | 3,328,221 |
| Shareholder equity | - | - | - | - | 861,463 | 861,463 |
| Total liabilities and shareholders equity | - | 1,262,614 | 577,931 | 575,000 | 1,774,139 | 4,189,684 |
| Net interest rate gap | 44,394 | (118,634) | (115,273) | (461,702) | 651,216 | - |

Interest rate sensitivity

The Bank establishes and maintains processes, utilizing systems where appropriate, to model and measure Interest Rate Risk exposures. Banking book on- and off-balance sheet positions, market data, and behavioural assumptions will be utilized to model the Bank's Interest Rate Risk exposures under varying scenarios. These varying market scenarios can either be deterministic (i.e. using defined parameters) or stochastic (i.e. using random simulations such as Monte Carlo).

Earnings-at-Risk:

Earnings-at-Risk (EAR) is defined as the negative impact to the Bank's pre-tax net interest income, as a result of changes to market interest rates. This sensitivity measure calculates the impact over a rolling 12-month horizon.

The Bank utilizes a dynamic modelling process that incorporates planning information and market data and simulates earnings to give projected net interest margin and cash flows, where earnings respond to changes in corresponding market rates.

Economic Value of Equity:

Economic Value of Equity exposure (EVE) is defined as the negative impact to the Bank's economic value, as a result of changes to market interest rates. The Bank's economic value is calculated by aggregating the net present value of cash flows from assets, liabilities and off balance sheet positions.

As a necessary part of the modelling process, the Bank applies appropriate behavioural and/or market assumptions to more accurately reflect the interest rate sensitivity of the Bank's economic value of equity. The assumptions are reviewed and approved by the ALCO and ERMC at least annually or upon material change.

As at December 31, if interest rates had been 100 basis points higher/lower and all other variables were held constant, the impact on the Bank's earnings would be:

| | 2016 | |
|--------------------------------------|-----------------|-------------------|
| | Shift up | Shift down |
| Impact on income before income taxes | (10,892) | 10,781 |
| Impact on equity | 1,516 | (1,712) |

Foreign exchange risk management

Foreign exchange rate risk is the risk of financial loss to the Bank due to adverse fluctuations in foreign exchange rates. Foreign exchange risk in the banking book is generated by foreign currency denominated balance sheet exposures and various card related business transactions. The Bank's foreign exchange risk is managed primarily by entering into agreements to buy and sell currencies on a spot basis or by hedging this exposure through the use of derivative financial instruments such as foreign exchange forwards. The objective of the Bank's policy with respect to foreign exchange risk is to limit and control exposure through strict hedging requirements in the context of authorized instruments and within defined limits by maintaining a fully hedged position on its foreign currency assets and liabilities at all times in order to mitigate foreign exchange risk to the Bank.

5 Liquidity risk management

Liquidity risk is defined as the inability of the Bank to meet its ongoing financial and business obligations as they become due at a reasonable cost. The Bank's liquidity risk objective is to maintain sufficient liquidity to withstand a range of stress events including periods when regular sources of funding become impaired and to meet all regulatory requirements. The Bank incurs and accepts liquidity risk arising in the normal course of offering its products and services. The liquidity risk that the Bank is exposed to can arise from a variety of sources. As such, the liquidity risk management strategy of the Bank will include a variety of measurements, assessments and guidelines, including but is not limited to:

- The maintenance of a diversified set of on and off balance sheet funding sources that utilizes a prudent amount of short-term funding liabilities;
- The maintenance of a cushion of high quality, unencumbered liquid assets ("Liquidity Buffer") to be held against identified funding requirements under stress for a liquidity risk survival horizon of 30 Days and for regulatory purposes;
- The projection of cash inflows and outflows from a variety of sources under various stress scenarios;
- The capacity to conduct a range of hypothetical analyses of changes to funding requirements under stress scenarios;
- A framework for the ongoing identification, measurement, management and monitoring of liquidity requirements.
- Incorporating the trade-offs between liquidity risk and the Bank's profitability into the Internal Capital Adequacy Assessment Process (ICAAP).

The ALCO chaired by the VP and Treasurer oversees the Bank's liquidity risk management program. General principles and the overall framework for managing liquidity risk are defined in the Bank's Funding and Liquidity Risk Policy which describes how the Bank seeks to manage Funding and Liquidity Risk on an enterprise basis. It assigns key governance responsibilities, prescribes rules for escalating risks to the ERM and RRC and provides for the ongoing identification, assessment, measurement, monitoring and reporting of liquidity requirements which are approved by the ALCO, ERM and RRC. The Policy is a Board-approved policy, maintained by the VP and Treasurer and is an integral part of the ERM Policy.

The regulatory requirements for liquidity have been established by OSFI based on the Basel III: The Principles for Sound Liquidity Risk Management and Supervision, standards issued by the Bank for International Settlements, Basel Committee of Banking Supervisors and commonly known as Basel III. This domestic guidance is based on the Basel III frameworks.

The regulatory requirements for liquidity have been established by OSFI, which include the Liquidity Coverage Ratio (LCR), Net Cumulative Cash Flow (NCCF) and other liquidity risk monitoring tools.

The Bank has a comprehensive liquidity stress testing program that considers multiple scenarios of varying degrees of stress over a range of time horizons. Stress testing is performed on a periodic basis to inform management of the level of liquidity risk that the Bank could face under a variety of scenarios. The Bank also performs prescribed regulatory stress scenarios (i.e. LCR and NCCF) which are used to inform the Bank and the regulator of the level of liquidity risk that the Bank could face in respect of its contractual balance sheet profile.

The Bank maintains a cushion of unencumbered, high quality liquid assets to meet funding requirements under the internally prescribed liquidity stress events. The stock of liquid assets includes but is not limited to cash and marketable securities that are traded in active secondary markets or are eligible at central banks for open market operations and marketability. The Bank also maintains a stock of unencumbered High Quality Liquidity Assets (HQLA) for LCR purpose. Sufficient unencumbered HQLA is required to cover the total net cash outflows over a 30-day period under a prescribed regulatory stress scenario.

In addition, the Bank maintains a contingency funding plan (CFP) in the event a material funding or liquidity crisis occurs. The Bank's CFP provides a framework for analyzing and responding to liquidity events that are both market- driven as well as institution-specific. The CFP describes the governance and protocol to be put into effect upon the occurrence of a liquidity event and details the roles and responsibilities of Senior Management and the Board.

6 Operational risk management

The Bank defines operational risk as risk of loss to earnings or capital from inadequate or failed processes, people or information systems; or Bank impacts from the external environment; or Bank impacts from relationships with third parties or affiliates; or legal liability from lawsuits; or fines, sanctions, or customer remediation from operational failures causing Compliance risk.

Operational risk is inherent in all business activities and can impact an organization through direct or indirect financial loss, brand damage, customer dissatisfaction, or legal or regulatory penalties. The Bank views its ability to accept and manage operational risk prudently and economically as an important aspect of its business model, with significant potential to generate earnings, drive profitable growth and build competitive advantage. The Bank seeks to manage and mitigate operational risk through the sound design, implementation and review of business processes, technological solutions and controls, both manual and automated.

Effective operational risk management and governance depends upon having clearly defined and understood roles and assigned responsibilities. Accordingly, the Bank appoints a Chief Operational Risk Officer (CORO), who has overall responsibility for the effective management of operational risk across the Bank on a day-to-day basis, and in compliance with applicable laws and regulations.

General principles and the overall framework for managing operational risk across the Bank are defined in the Bank's Operational Risk Policy approved by the ERM.

The Bank has established an ORMC to provide governance for the operational risk framework including related policies. The ORMC is chaired by the Chief Operational Risk Officer with member representation from business units and support groups. The business units have the responsibility for implementing the framework as well as for the day-to-day management of operational risk. Managing operational risk is an important priority for the Bank. The Bank's Operational Risk Policy and Procedures comply with the Basel Committee's "Sound Practices for the Management and Supervision of Operational Risk" and the Office of Superintendent of Financial Institutions' ("OSFI") capital adequacy guidelines.

The Bank also has a reporting process that provides business unit leaders with operational risk information on a periodic and frequent basis to help them assess the overall operational risks of their business units. These initiatives have resulted in improved operational risk intelligence and a heightened level of preparedness to manage risk events and conditions that may adversely impact the Bank's operations.

The overall effectiveness of the Bank's Operational Risk Management program is contingent upon the identification and mitigation of Operational Risk exposures and events. The Bank has developed a comprehensive program to identify, measure, monitor, and report inherent and emerging operational risks. The risk self-assessment methodology comprises three key approaches for Business Units and Staff Groups to identify and/or capture Operational Risk exposures and events: Entity Risk Self Assessment ("ERSA"), Process Risk Self Assessment ("PRSA") and the Operational Risk Event Capture process. Each of these tools provides a unique and complementary approach to identifying and capturing Operational Risk. Together, they comprise a holistic, comprehensive program for risk identification at the Bank.

Key Risk Indicators ("KRIs") are tools used to provide an assessment of, and/or insight into changes in the risk and control environment that may lead to losses or exposures within the business units and staff groups. KRIs are objective and quantifiable, and provide a reasonable indication or an early warning of elevated levels of operational risk. Business units and staff groups are responsible for monitoring and reporting KRIs, with support from the Chief Operational Risk Officer's team.

The Bank measures its operational risk using the Basic Indicator Approach. The Bank's operational risk is calculated as disclosed previously in the Capital Structure and Adequacy section of this document.

7 Remuneration

The Bank adheres to the remuneration policies of its parent company, AXP, with governance and oversight of the remuneration policies and the compensation structure for senior management provided by the Human Resources Committee (HRC) of the Board and the Bank's VP, Human Resources. The HRC meets on a quarterly basis and once a year discusses and aligns on remuneration of senior management of the Bank.

The key features and objectives of the Bank's remuneration program include both business and leadership objectives and goals. Such objectives and goals include but are not limited to the revenue, earnings per share, employee engagement and diversity and specific role objectives. The HRC reviews the Bank's remuneration program on an annual basis. Based on the most recent annual review, the Bank has adopted "Risk Compensation Policy". The policy supports the Bank's compliance with the Financial Stability Board (FSB) guideline, which is intended to reduce incentives towards excessive risk taking that may arise from the structure of compensation systems. Key risks taken into consideration include, but are not limited to, both financial and reputational/brand risk. Measures to assess risk include internal Operational Risk events, dollar value thresholds and levels of media coverage and volume of cardmember impact. Annual variable compensation is the primary factor that can be affected post a qualified risk assessment.

The remuneration of risk and compliance employees is not tied to the business results of the unique lines of business they directly support, but rather to the overall success of the Bank's business and their respective risk and compliance related performance metrics. The funding for the compensation pools is separate from the business.

Remuneration is assessed and assigned during the annual performance review process. Objectives of this process are business, financial and leadership in nature. Performance metrics include, but are not limited to, financial objectives, operating expense management and leadership development. Both financial and leadership goals are measured across the entity and for the individual in assessing annual performance and remuneration. The remuneration available to the Bank's employees is tied to annual performance metrics and is assessed on an annual basis based on financial results of the Bank, the Bank's parent company, and individual Lines of Business. Allocations are then completed based on the successful accomplishment of those performance objectives to include both financial and leadership objectives.

The compensation structure of the Bank includes salaries, periodic performance based incentive plans and long-term incentive plans such as equity based payments and a deferred profit sharing plan. All full-time employees of the bank are eligible to receive the variable component of their compensation contingent upon their performance. Employee bonuses are not guaranteed. Equity based payments granted to the Bank's employees are awards offered by the Bank's ultimate parent, AXP. These awards may be in the form of restricted stock units, and portfolio grants (PGs), which take into account longer-term performance through the awards vesting schedule. In addition, a group retirement savings plan and health benefit plans are available to employees which satisfy certain eligibility criteria.

Key management compensation

Key management personnel are those persons having the authority and responsibility for planning, directing and controlling the activities of the Bank either directly or indirectly. The key management personnel of the Bank include the internal Board members of the Bank and Officers who are employees of the Bank that make critical decisions in relation to the strategic direction of the Bank.

The compensation paid or payable to key management for employee services as at December 31 is shown below:

| | 2016 |
|---|--------------|
| Salaries and other short-term employee benefits | 4,246 |
| Post-employment benefits | 221 |
| Share-based payments | 841 |
| | <u>5,308</u> |

The fixed and variable compensation paid or payable to key management for employee services as at December 31 is shown below:

| | 2016 |
|----------|--------------|
| Fixed | 2,521 |
| Variable | 2,787 |
| | <u>5,308</u> |

Amex Bank of Canada

Basel Pillar III Disclosures

| Amex Bank of Canada | | |
|--|---|--------------|
| Modified Capital Disclosures as at Dec.31, 2016 | | Transitional |
| Common Equity Tier 1 capital: instruments and reserves | | |
| 1 | Directly issued qualifying common share capital (and equivalent for non-joint stock companies) and related stock surplus (and other contributed surplus) | 215,155 |
| 2 | Retained earnings | 646,308 |
| 3 | Accumulated other comprehensive income (and other reserves) | - |
| 4 | <i>Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)</i> | N/A |
| 5 | Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1) | N/A |
| 6 | Common Equity Tier 1 capital before regulatory adjustments | 861,463 |
| Common Equity Tier 1 capital: regulatory adjustments | | |
| 28 | Total regulatory adjustments to Common Equity Tier 1 | 4,154 |
| 29 | Common Equity Tier 1 capital (CET1) | 857,309 |
| Additional Tier 1 capital: instruments | | |
| 30 | Directly issued qualifying Additional Tier 1 instruments plus related stock surplus | N/A |
| 31 | of which: classified as equity under applicable accounting standards | N/A |
| 32 | of which: classified as liabilities under applicable accounting standards | N/A |
| 33 | <i>Directly issued capital instruments subject to phase out from Additional Tier 1</i> | N/A |
| 34 | Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1) | N/A |
| 35 | <i>of which: instruments issued by subsidiaries subject to phase out</i> | N/A |
| 36 | Additional Tier 1 capital before regulatory adjustments | - |
| Additional Tier 1 capital: regulatory adjustments | | |
| 43 | Total regulatory adjustments to Additional Tier 1 capital | - |
| 44 | Additional Tier 1 capital (AT1) | - |
| 45 | Tier 1 capital (T1 = CET1 + AT1) | 857,309 |
| Tier 2 capital: instruments and allowances | | |
| 46 | Directly issued qualifying Tier 2 instruments plus related stock surplus | N/A |

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Basel Pillar III Disclosures

| | | | |
|--|--|-----------|-----------|
| 47 | <i>Directly issued capital instruments subject to phase out from Tier 2</i> | N/A | |
| 48 | Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2) | N/A | |
| 49 | <i>of which: instruments issued by subsidiaries subject to phase out</i> | N/A | |
| 50 | Collective allowances | N/A | |
| 51 | Tier 2 capital before regulatory adjustments | - | |
| Tier 2 capital: regulatory adjustments | | | |
| 57 | Total regulatory adjustments to Tier 2 capital | - | |
| 58 | Tier 2 capital (T2) | - | |
| 59 | Total capital (TC = T1 + T2) | 857,309 | 858,981 |
| 60 | Total risk-weighted assets | 4,505,784 | 4,507,446 |
| Capital ratios | | | |
| 61 | Common Equity Tier 1 (as percentage of risk-weighted assets) | 19.03% | 19.06% |
| 62 | Tier 1 (as percentage of risk-weighted assets) | 19.03% | 19.06% |
| 63 | Total capital (as percentage of risk-weighted assets) | 19.03% | 19.06% |
| OSFI all-in target | | | |
| 69 | Common Equity Tier 1 capital all-in target ratio | 7.00% | |
| 70 | Tier 1 capital all-in target ratio | 8.50% | |
| 71 | Total capital all-in target ratio | 10.50% | |
| Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022) | | | |
| 80 | <i>Current cap on CET1 instruments subject to phase out arrangements</i> | N/A | |
| 81 | <i>Amounts excluded from CET1 due to cap (excess over cap after redemptions and maturities)</i> | N/A | |
| 82 | <i>Current cap on AT1 instruments subject to phase out arrangements</i> | N/A | |
| 83 | <i>Amounts excluded from AT1 due to cap (excess over cap after redemptions and maturities)</i> | N/A | |
| 84 | <i>Current cap on T2 instruments subject to phase out arrangements</i> | N/A | |
| 85 | <i>Amounts excluded from T2 due to cap (excess over cap after redemptions and maturities)</i> | N/A | |

Amex Bank of Canada

Basel Pillar III Disclosures

| Amex Bank of Canada | | |
|---|--|------------------|
| BASEL III - Leverage Ratio as at Dec.31, 2016 | | |
| | Item | |
| | On-balance sheet exposures | |
| 1 | On-balance sheet items (excluding derivatives, SFTs and grandfathered securitization exposures but including collateral) | 4,189,684 |
| 2 | (Asset amounts deducted in determining Basel III "all-in" Tier 1 capital) | (4,154) |
| 3 | Total on-balance sheet exposures (excluding derivatives and SFTs) (sum of lines 1 and 2) | 4,185,530 |
| | Derivative exposures | |
| 4 | Replacement cost associated with all derivative transactions (i.e. net of eligible cash variation margin) | |
| 5 | Add-on amounts for PFE associated with all derivative transactions | |
| 6 | Gross up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the operative accounting framework | |
| 7 | (Deductions of receivables assets for cash variation margin provided in derivative transactions) | |
| 8 | (Exempted CCP-leg of client cleared trade exposures) | |
| 9 | Adjusted effective notional amount of written credit derivatives | |
| 10 | (Adjusted effective notional offsets and add-on deductions for written credit derivatives) | |
| 11 | Total derivative exposures (sum of lines 4 to 10) | |
| | Securities financing transaction exposures | |
| 12 | Gross SFT assets recognized for accounting purposes (with no recognition of netting), after adjusting for sale accounting transactions | |
| 13 | (Netted amounts of cash payables and cash receivables of gross SFT assets) | |
| 14 | Counterparty credit risk (CCR) exposure for SFTs | |
| 15 | Agent transaction exposures | |
| 16 | Total securities financing transaction exposures (sum of lines 12 to 15) | |
| | Other off-balance sheet exposures | |
| 17 | Off-balance sheet exposure at gross notional amount | 18,083,562 |
| 18 | (Adjustments for conversion to credit equivalent amounts) | 16,272,645 |
| 19 | Off-balance sheet items (sum of lines 17 and 18) | 1,810,917 |
| | Capital and Total Exposures | |
| 20 | Tier 1 capital | 857,309 |
| 21 | Total Exposures (sum of lines 3, 11, 16 and 19) | 5,996,448 |
| | Leverage Ratios | |
| 22 | Basel III leverage ratio | 14.30% |