



Butterfield

## Q4 2015

Financial Results for the Twelve Months Ended 31 December 2015  
THE BANK OF N.T. BUTTERFIELD & SON LIMITED



22 February, 2016

## **Independent Auditor's Report**

### **To the Board of Directors and Shareholders of The Bank of N.T. Butterfield & Son Limited**

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of comprehensive income, of changes in shareholders' equity and of cash flows present fairly, in all material respects, the financial position of The Bank of N.T. Butterfield & Son Limited and its subsidiaries at 31 December 2015 and 2014, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States) and in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

A handwritten signature in black ink, which appears to read "PricewaterhouseCoopers Ltd.", written in a cursive, flowing style.

**Chartered Professional Accountants**

# **The Bank of N.T. Butterfield & Son Limited**

## **Table of Contents**

## **Page**

Consolidated Balance Sheets	2
Consolidated Statements of Operations	3
Consolidated Statements of Comprehensive Income	4
Consolidated Statements of Changes in Shareholders' Equity	5
Consolidated Statements of Cash Flows	6
Notes to the Consolidated Financial Statements	
Note 1: Nature of business	7
Note 2: Significant accounting policies	7
Note 3: Cash due from banks	17
Note 4: Short-term investments	17
Note 5: Investment in securities	18
Note 6: Loans	21
Note 7: Credit risk concentrations	27
Note 8: Premises, equipment and computer software	28
Note 9: Goodwill and other intangible assets	28
Note 10: Customer deposits and deposits from banks	29
Note 11: Employee benefit plans	30
Note 12: Credit related arrangements and commitments	33
Note 13: Exit cost obligations	34
Note 14: Loan interest income	34
Note 15: Segmented information	35
Note 16: Derivative instruments and risk management	36
Note 17: Fair value measurements	39
Note 18: Interest rate risk	41
Note 19: Long-term debt	42
Note 20: Earnings per share	43
Note 21: Share-based payments	44
Note 22: Share buy-back plans	46
Note 23: Accumulated other comprehensive loss	47
Note 24: Capital structure	48
Note 25: Income taxes	49
Note 26: Business combinations	50
Note 27: Related party transactions	52
Note 28: Comparative information	52
Note 29: Subsequent events	52

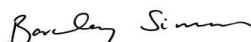
# The Bank of N.T. Butterfield & Son Limited

## Consolidated Balance Sheets

(In thousands of Bermuda dollars, except share and per share data)

	As at	
	31 December 2015	31 December 2014
<b>Assets</b>		
Cash and demand deposits with banks	489,524	482,286
Cash equivalents	1,799,366	1,581,025
Cash due from banks	2,288,890	2,063,311
Short-term investments	409,482	394,770
Investment in securities		
Trading	321,299	417,385
Available-for-sale	2,201,349	2,233,549
Held-to-maturity	701,282	338,177
Total investment in securities	3,223,930	2,989,111
Loans, net of allowance for credit losses	4,000,155	4,019,128
Premises, equipment and computer software	183,378	215,123
Accrued interest	17,460	19,241
Goodwill	23,462	24,821
Intangible assets	27,669	33,041
Equity method investments	12,786	12,838
Other real estate owned	11,206	19,300
Other assets	77,145	67,756
<b>Total assets</b>	<b>10,275,563</b>	<b>9,858,440</b>
<b>Liabilities</b>		
Customer deposits		
Non-interest bearing	1,881,745	1,558,122
Interest bearing	7,285,923	7,073,549
Total customer deposits	9,167,668	8,631,671
Bank deposits	14,478	39,906
Total deposits	9,182,146	8,671,577
Employee benefit plans	122,135	117,897
Accrued interest	2,744	4,754
Preference share dividends payable	654	655
Other liabilities	100,530	97,183
Total other liabilities	226,063	220,489
Long-term debt	117,000	117,000
<b>Total liabilities</b>	<b>9,525,209</b>	<b>9,009,066</b>
<b>Shareholders' equity</b>		
Common share capital (BMD 0.01 par; authorised shares 26,000,000,000)		
issued and outstanding: 472,932,535 (2014: 550,023,138)	4,729	5,500
Preference share capital (USD 0.01 par; USD 1,000 liquidation preference)		
issued and outstanding: 182,863 (2014: 183,046)	2	2
Contingent value convertible preference share capital (USD 0.01 par)		
issued and outstanding: nil (2014: 6,909,397)	-	69
Additional paid-in capital	1,221,088	1,348,465
Accumulated deficit	(368,618)	(405,056)
Less: treasury common shares, at cost: 9,240,317 shares (2014: 12,770,604)	(16,350)	(22,086)
Accumulated other comprehensive loss	(90,497)	(77,520)
<b>Total shareholders' equity</b>	<b>750,354</b>	<b>849,374</b>
<b>Total liabilities and shareholders' equity</b>	<b>10,275,563</b>	<b>9,858,440</b>

The accompanying notes are an integral part of these consolidated financial statements.



**Barclay Simmons**  
Chairman

# The Bank of N.T. Butterfield & Son Limited

## Consolidated Statements of Operations

(In thousands of Bermuda dollars, except per share data)

	Year ended	
	31 December 2015	31 December 2014
<b>Non-interest income</b>		
Asset management	18,910	17,728
Banking	35,221	34,280
Foreign exchange revenue	31,896	29,379
Trust	40,264	38,268
Custody and other administration services	9,522	10,166
Other non-interest income	4,359	5,009
<b>Total non-interest income</b>	<b>140,172</b>	<b>134,830</b>
<b>Interest income</b>		
Loans	186,486	191,986
Investments	69,578	67,757
Deposits with banks	6,517	5,358
<b>Total interest income</b>	<b>262,581</b>	<b>265,101</b>
<b>Interest expense</b>		
Deposits	18,446	20,903
Long-term debt	4,861	5,628
Securities sold under repurchase agreements	8	83
<b>Total interest expense</b>	<b>23,315</b>	<b>26,614</b>
<b>Net interest income before provision for credit losses</b>	<b>239,266</b>	<b>238,487</b>
Provision for credit losses	(5,741)	(8,048)
<b>Net interest income after provision for credit losses</b>	<b>233,525</b>	<b>230,439</b>
Net trading gains	(562)	10,070
Net realised gains (losses) on available-for-sale investments	(4,407)	8,680
Net realised / unrealised gains (losses) on other real estate owned	277	(1,804)
Impairment of fixed assets	(5,083)	(1,986)
Net gain on sale of equity method investments	-	277
Net other gains	338	451
<b>Total other gains (losses)</b>	<b>(9,437)</b>	<b>15,688</b>
<b>Total net revenue</b>	<b>364,260</b>	<b>380,957</b>
<b>Non-interest expense</b>		
Salaries and other employee benefits	134,917	129,761
Technology and communications	57,069	57,119
Property	21,539	24,312
Professional and outside services	27,638	24,022
Non-income taxes	13,882	14,175
Amortisation of intangible assets	4,424	4,281
Marketing	3,919	3,802
Restructuring costs	2,183	-
Other expenses	19,674	15,495
<b>Total non-interest expense</b>	<b>285,245</b>	<b>272,967</b>
<b>Net income before income taxes</b>	<b>79,015</b>	<b>107,990</b>
Income tax benefit (expense)	(1,276)	169
<b>Net income</b>	<b>77,739</b>	<b>108,159</b>
<b>Earnings per common share</b>		
Basic earnings per share	0.13	0.17
Diluted earnings per share	0.12	0.16

The accompanying notes are an integral part of these consolidated financial statements.

**The Bank of N.T. Butterfield & Son Limited**  
**Consolidated Statements of Comprehensive Income**  
*(In thousands of Bermuda dollars)*

	Year ended	
	<b>31 December 2015</b>	31 December 2014
<b>Net income</b>	<b>77,739</b>	108,159
<b>Other comprehensive income (loss), net of taxes</b>		
Net change in unrealised gains and losses on translation of net investment in foreign operations	<b>(3,139)</b>	(2,874)
Accretion of net unrealised losses on held-to-maturity investments transferred from available-for-sale investments	<b>365</b>	-
Net change in unrealised gains and losses on available-for-sale investments	<b>(11,793)</b>	40,085
Employee benefit plans adjustments	<b>1,590</b>	(47,143)
Other comprehensive (loss), net of taxes	<b>(12,977)</b>	(9,932)
<b>Total comprehensive income</b>	<b>64,762</b>	98,227

The accompanying notes are an integral part of these consolidated financial statements.

**The Bank of N.T. Butterfield & Son Limited**  
**Consolidated Statements of Changes in Shareholders' Equity**

	Year ended			
	31 December 2015		31 December 2014	
	Number of shares	In thousands of Bermuda dollars	Number of shares	In thousands of Bermuda dollars
<b>Common share capital issued and outstanding</b>				
Balance at beginning of year	550,023,138	5,500	549,803,460	5,498
Conversion of contingent value preference shares	6,909,397	69	219,678	2
Retirement of shares	(84,000,000)	(840)	-	-
<b>Balance at end of year</b>	<b>472,932,535</b>	<b>4,729</b>	<b>550,023,138</b>	<b>5,500</b>
<b>Preference shares</b>				
Balance at beginning of year	183,046	2	183,606	2
Repurchase and cancellation of preference shares	(183)	-	(560)	-
<b>Balance at end of year</b>	<b>182,863</b>	<b>2</b>	<b>183,046</b>	<b>2</b>
<b>Contingent value convertible preference shares</b>				
Balance at beginning of year	6,909,397	69	7,129,075	71
Conversion to common shares	(6,909,397)	(69)	(219,678)	(2)
<b>Balance at end of year</b>	<b>-</b>	<b>-</b>	<b>6,909,397</b>	<b>69</b>
<b>Additional paid-in capital</b>				
Balance at beginning of year		1,348,465		1,344,755
Share-based compensation		7,703		8,869
Share-based settlements		(9,749)		(4,503)
Reduction of carrying value on repurchase of preference shares		(183)		(560)
Premium paid on repurchase of preference shares		(28)		(96)
Retirement of shares		(125,120)		-
<b>Balance at end of year</b>		<b>1,221,088</b>		<b>1,348,465</b>
<b>Accumulated deficit</b>				
Balance at beginning of year		(405,056)		(460,157)
Reclassification from accumulated other comprehensive loss		-		(9,072)
Net income for year		77,739		108,159
Common share cash dividends declared and paid, \$0.05 per share (2014 \$0.05 per share)		(24,846)		(27,440)
Cash dividends declared on preference shares, \$80.00 per share (2014: \$80.00 per share)		(14,631)		(14,712)
Preference shares guarantee fee		(1,824)		(1,834)
<b>Balance at end of year</b>		<b>(368,618)</b>		<b>(405,056)</b>
<b>Treasury common shares</b>				
Balance at beginning of year	12,770,604	(22,086)	8,310,421	(10,948)
Purchase of treasury common shares	2,503,707	(4,862)	8,567,340	(17,018)
Share-based settlements	(6,033,994)	10,598	(4,107,157)	5,880
<b>Balance at end of year</b>	<b>9,240,317</b>	<b>(16,350)</b>	<b>12,770,604</b>	<b>(22,086)</b>
<b>Accumulated other comprehensive loss</b>				
Balance at beginning of year		(77,520)		(76,660)
Reclassification to accumulated deficit		-		9,072
Other comprehensive income (loss), net of taxes		(12,977)		(9,932)
<b>Balance at end of year</b>		<b>(90,497)</b>		<b>(77,520)</b>
<b>Total shareholders' equity</b>		<b>750,354</b>		<b>849,374</b>

The accompanying notes are an integral part of these consolidated financial statements.



# The Bank of N.T. Butterfield & Son Limited

## Consolidated Statements of Cash Flows

(In thousands of Bermuda dollars)

	Year ended	
	31 December 2015	31 December 2014
<b>Cash flows from operating activities</b>		
Net income	77,739	108,159
<b>Adjustments to reconcile net income from continuing operations to operating cash flows</b>		
Depreciation and amortisation	50,069	45,116
Impairment of fixed assets	5,083	1,986
Increase in carrying value of equity method investments	(980)	(834)
Share-based payments and settlements	7,913	9,049
Fair value adjustments of a contingent payment	(143)	1,070
Net realised (gains) losses on available-for-sale investments	4,407	(8,680)
Equity pick up on private equity partnership investment	(224)	(458)
Net (gains) losses on other real estate owned	(277)	1,804
Loss on sale of premises and equipment	28	-
Net gain on sales of equity method investments	-	(277)
Provision for credit losses	5,741	8,048
<b>Changes in operating assets and liabilities</b>		
Decrease in accrued interest receivable	1,417	594
(Increase) in other assets	(10,259)	(3,955)
Increase (decrease) in accrued interest payable	(1,907)	1,040
Increase (decrease) in other liabilities and employee benefit plans	16,932	(18,885)
<b>Cash provided by operating activities from operations</b>	<b>155,539</b>	<b>143,777</b>
<b>Cash flows from investing activities</b>		
Net increase in short-term investments	(28,358)	(343,773)
Net change in trading investments	96,086	134,905
Available-for-sale investments: proceeds from sale	238,756	130,453
Available-for-sale investments: proceeds from maturities and pay downs	435,827	198,311
Available-for-sale investments: purchases	(1,018,759)	(800,865)
Held-to-maturity investments: proceeds from maturities and pay downs	26,965	12,426
Held-to-maturity investments: purchases	(50,283)	(18,073)
Net (increase) decrease in loans	(36,876)	145,023
Net additions to premises, equipment and computer software	(1,477)	(6,128)
Proceeds from sale of other real estate owned	11,238	12,389
Equity method investments: net proceeds on sale, dividends received and return on capital	1,032	806
Net amounts received for assuming deposits acquired from another bank	-	310,578
Purchase of subsidiary	-	(34,757)
<b>Cash used in investing activities</b>	<b>(325,849)</b>	<b>(258,705)</b>
<b>Cash flows from financing activities</b>		
Net increase in demand and term deposit liabilities	598,578	637,705
Net decrease in securities sold under agreement to repurchase	-	(25,535)
Repayment of long-term debt	-	(90,000)
Common shares repurchased	(130,822)	(17,018)
Preference shares repurchased	(211)	(656)
Proceeds from stock option exercises	640	1,198
Cash dividends paid on common and contingent value convertible preference shares	(24,846)	(27,440)
Cash dividends paid on preference shares	(14,631)	(14,673)
Preference shares guarantee fee paid	(1,824)	(1,834)
<b>Cash provided by financing activities</b>	<b>426,884</b>	<b>461,747</b>
Net effect of exchange rates on cash due from banks	(30,995)	(13,980)
<b>Net increase in cash due from banks</b>	<b>225,579</b>	<b>332,839</b>
<b>Cash due from banks at beginning of year</b>	<b>2,063,311</b>	<b>1,730,472</b>
<b>Cash due from banks at end of year</b>	<b>2,288,890</b>	<b>2,063,311</b>
<b>Supplemental disclosure of cash flow information</b>		
Cash interest paid	21,408	27,654
Cash income tax paid	596	985
<b>Non-cash items</b>		
Transfer to other real estate owned	3,400	6,086
Transfer of available-for-sale investments to held-to-maturity investments	340,969	-

The accompanying notes are an integral part of these consolidated financial statements.



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 1: Nature of business

The Bank of N.T. Butterfield & Son Limited ("Butterfield", "Bank" or the "Company") is incorporated under the laws of Bermuda and has a banking licence under the Bank and Deposit Companies Act, 1999 ("the Act"). Butterfield is regulated by the Bermuda Monetary Authority ("BMA"), which operates in accordance with Basel principles.

Butterfield is a full service community bank in Bermuda and Cayman and a provider of specialised wealth management services in all its jurisdictions. Services offered include retail, private and corporate banking, treasury, custody, asset management and personal and institutional trust services. The Bank provides such services from six jurisdictions: Bermuda, Cayman, Guernsey, Switzerland, The Bahamas and the United Kingdom. The Bank holds all applicable licences required in the jurisdictions in which it operates.

### Note 2: Significant accounting policies

#### a. Basis of Presentation and Use of Estimates and Assumptions

The accounting and financial reporting policies of the Bank and its subsidiaries conform to generally accepted accounting principles in the United States of America ("GAAP"). The preparation of consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the year, and actual results could differ from those estimates.

Critical accounting estimates are those that require management to make subjective or complex judgments about the effect of matters that are inherently uncertain and may change in subsequent periods. Changes that may be required in the underlying assumptions or estimates in these areas could have a material impact on the future financial condition and results of operations. Management believes that the most critical accounting policies upon which the financial condition depends, and which involve the most complex or subjective decisions or assessments, are as follows:

- Allowance for credit losses
- Fair value and impairment of financial instruments
- Impairment of long-lived assets
- Impairment of goodwill
- Employee benefit plans
- Share-based payments

#### b. Basis of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries (collectively the "Bank"), and those variable interest entities ("VIEs") where the Company is the primary beneficiary. Intercompany accounts and transactions have been eliminated. The Bank consolidates subsidiaries where it holds, directly or indirectly, more than 50% of the voting rights or where it exercises control. The Bank is deemed to have a controlling financial interest and is the primary beneficiary of a VIE if it has both the power to direct the activities of the VIE that most significantly impact the VIE economic performance and an obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE. The determination of whether the Bank meets the criteria to be considered the primary beneficiary of a VIE requires a periodic evaluation of all transactions (such as investments, loans and fee arrangements) with the entity. During the periods under review, the Bank had no interests in VIEs where the Bank was considered the primary beneficiary.

Entities where the Bank holds 20% to 50% of the voting rights and/or has the ability to exercise significant influence, other than investments in designated VIEs, are accounted for under the equity method, and the pro rata share of their income (loss) is included in other non-interest income.

#### c. Foreign Currency Translation

Assets, liabilities, revenues and expenses denominated in United States ("US") dollars are translated to Bermuda dollars at par. Assets and liabilities of the parent company arising from other foreign currency transactions are translated into Bermuda dollars at the rates of exchange prevailing at the balance sheet date. The resulting gains or losses are included in foreign exchange revenue in the consolidated statements of operations.

The assets and liabilities of foreign currency-based subsidiaries are translated at the rate of exchange prevailing on the balance sheet date, while associated revenues and expenses are translated to Bermuda dollars at the average rates of exchange prevailing throughout the year. Unrealised translation gains or losses on investments in foreign currency-based subsidiaries are recorded as a separate component of Shareholders' equity within accumulated other comprehensive loss ("AOCL"). Gains and losses on foreign currency based subsidiaries are recorded in the consolidated statements of operations when the Bank ceases to have a controlling financial interest in a foreign currency-based subsidiary.

#### d. Assets Held in Trust or Custody

Securities and properties (other than cash and deposits held with the Bank and its subsidiaries) held in trust, custody, agency or fiduciary capacity for customers are not included in the consolidated balance sheets because the Bank is not the beneficiary of these assets.

#### e. Cash due from banks

Cash due from banks include cash on hand, cash items in the process of collection, amounts due from correspondent banks and highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in fair value. Such investments are those with less than three months' maturity from the date of acquisition and include unrestricted term deposits, certificates of deposit and treasury bills.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **f. Short-Term Investments**

Short-term investments comprise restricted term and demand deposits and unrestricted term deposits and treasury bills with less than one year but greater than three months maturity from the date of acquisition. From August 2014, certificates of deposit with less than one year but greater than three months maturity from the date of acquisition are designated as short term investments as the investments are highly liquid and subject to an insignificant risk of change in fair value.

### **g. Investments**

Investments securities are classified as trading, available-for-sale ("AFS") or held-to-maturity ("HTM").

Investments are classified as trading when management has the intent to sell these investments either for profit or to invest the cash received by taking customer deposits in foreign currencies. Debt and equity securities classified as trading investments are carried at fair value in the consolidated balance sheets, with unrealised gains and losses included in the consolidated statements of operations as net realised / unrealised gains (losses) on trading investments. Investments are classified primarily as AFS when used to manage the Bank's exposure to interest rate and liquidity movements, as well as to make strategic longer-term investments. AFS investments are carried at fair value in the consolidated balance sheets with unrealised gains and losses reported as net increase or decrease to AOCL. Investments that the Bank has the positive intent and ability to hold to maturity are classified as HTM and are carried at amortised cost in the consolidated balance sheets. Unrecognised gains and losses on HTM securities are disclosed in the notes to the consolidated financial statements.

The specific identification method is used to determine realised gains and losses on AFS and HTM investments, which are included in net realised gains and losses on AFS and HTM investments, respectively, in the consolidated statements of operations.

Dividend and interest income, including amortisation of premiums and discounts, on securities for which cash flows are not considered uncertain are included in interest income in the consolidated statements of operations. For securities with uncertain cash flows, the investments are accounted for under the cost recovery method, whereby all principal and coupon payments received are applied as a reduction of the amortised cost and carrying amount. Accrual of income is suspended in respect of debt securities that are in default, or from which it is unlikely that future interest payments will be received as scheduled.

Contained within other assets are investments in private equity for which the Bank does not have sufficient rights or ownership interests to follow the equity method of accounting. Unquoted equity investments which are held directly by the Bank and which do not have readily determinable fair values are recorded at cost and reviewed for impairment if indicators of impairment exist.

Equity method investments which include investments whereby the Bank has the ability to influence, but not control, the financial or operating policies of such entities, are accounted for using the equity method of accounting.

### **Recognition of other-than-temporary impairments**

For debt securities, management considers a decline in fair value to be other-than-temporary when it does not expect to recover the entire amortised cost basis of the security. Investments in debt securities in unrealised loss positions are analysed as part of management's ongoing assessment of other-than-temporary impairment ("OTTI"). When management intends to sell such securities or it is more likely than not that the Bank will be required to sell the securities before recovering the amortised cost, it recognises an impairment loss equal to the full difference between the amortised cost basis and the fair value of those securities. When management does not intend to sell or it is not more likely than not that the Bank will be required to sell such securities before recovering the amortised cost, management determines whether any credit losses exist to identify any OTTI.

Under certain circumstances, management will perform a qualitative determination and consider a variety of factors, including the length of time and extent to which the fair value has been less than cost; adverse conditions specifically related to the industry, geographic area or financial condition of the issuer or underlying collateral of a security; payment structure of the security; changes to the rating of the security by a rating agency; the volatility of the fair value changes; and changes in fair value of the security after the balance sheet date. Alternatively, management estimates cash flows over the remaining lives of the underlying security to assess whether credit losses exist.

In situations where there is a credit loss, only the amount of impairment relating to credit losses on AFS and HTM investments is recognised in net income. For AFS investments, the decrease in fair value relating to factors other than credit losses are recognised in AOCL. Cash flow estimates take into account expectations of relevant market and economic data as of the end of the reporting period, including, for example, underlying loan-level data, and structural features of securitisation, such as subordination, excess spread, over collateralisation or other forms of credit enhancement. The degree of judgment involved in determining the recoverable value of an investment security is dependent upon the availability of observable market prices or observable market parameters. When observable market prices and parameters do not exist, judgment is necessary to estimate recoverable value which gives rise to added uncertainty in the assessment. The assessment takes into consideration factors such as interest rate changes, movements in credit spreads, default rate assumptions, prepayment assumptions, type and quality of collateral, and market sentiment.

With respect to the pass-through note investment ("PTN"), prior to its redemption in 2014, management compared cash flow projections to fair value and amortised cost to determine if any credit losses existed. Management's cash flow forecasts for the PTN were created in conjunction with a specialist in analytical cash flow modelling. Management also performed other analyses to support its cash flow projections to assess the reasonability.

Management's fair valuations may include inputs and assumptions that are less observable or require greater estimation, thereby resulting in values which may be greater or lower than the actual value at which the investments may be ultimately sold or the ultimate cash flows that may be recovered. If the assumptions on which management based its fair valuations change, the Bank may experience additional OTTI or realised losses or gains, and the period-to-period changes in value could vary significantly.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **h. Loans**

Loans are reported as the principal amount outstanding, net of allowance for credit losses, unearned income, fair value adjustments arising from hedge accounting and net deferred loan fees. Interest income is recognised over the term of the loan using the effective interest method, or on a basis approximating a level rate of return over the term of the loan, except for loans classified as non-accrual.

#### **Acquired loans**

Acquired loans are recorded at fair value at the date of acquisition. No allowance for credit losses is recorded on the acquisition date as the fair value of the acquired assets incorporates assumptions regarding credit risk. Acquired loans with evidence of credit quality deterioration for which it is probable that the Bank will not receive all contractually required payments receivable are accounted for as purchased credit-impaired loans. Generally, acquired loans that meet the Bank's definition for non-accrual status are considered to be credit-impaired.

The excess of the cash flows expected to be collected on purchased credit-impaired loans, measured as of the acquisition date, over the estimated fair value is referred to as the accretable yield and is recognized in interest income over the remaining life of the loan using an effective yield methodology. The difference between contractually required payments as of the acquisition date and the cash flows expected to be collected is referred to as the non-accretable difference which is included as a reduction of the carrying amount of the purchased credit-impaired loans.

The Bank evaluates at each balance sheet date the estimated cash flows and corresponding carrying value of purchased credit-impaired loans in the same manner as for the measurement of impaired loans, as is described below. The Bank evaluates at each balance sheet date whether the carrying value of its purchased credit-impaired loans has decreased and if so, recognises an allowance for credit losses in its consolidated statements of operations. For any increases in cash flows expected to be collected, the Bank adjusts any prior recorded allowance for purchased credit-impaired loans first, and then the amount of accretable yield recognized on a prospective basis over the purchased credit-impaired loan's remaining life. Purchased credit-impaired loans are not considered non-performing and continue to have an accretable yield as long as there is a reasonable expectation about the timing and amount of cash flows expected to be collected.

#### **Impaired loans**

A loan is considered to be impaired when, based on current information and events, the Bank determines that it will not be able to collect all amounts due according to the original loan contract, including scheduled interest payments. Impaired loans include all non-accruing loans and all loans modified in a troubled debt restructuring ("TDR") even if full collectability is expected following the restructuring.

When a loan is identified as impaired, the impairment is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, except when the sole (remaining) source of repayment for the loan is the operation or liquidation of the collateral. In these cases the current fair value of the collateral, less selling costs, is used instead of discounted cash flows.

If the Bank determines that the expected realisable value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortised premium or discount), impairment is recognised through an allowance estimate. If the Bank determines that part of the allowance is uncollectible, that amount is charged off.

#### **Non-accrual**

Commercial, commercial real estate and consumer loans (excluding credit card consumer loans) are placed on non-accrual status generally if:

- in the opinion of management, full payment of principal or interest is in doubt; or
- principal or interest is 90 days past due.

Residential mortgages are placed on non-accrual status immediately if:

- in the opinion of management, full payment of principal or interest is in doubt; or
- when principal or interest is 90 days past due, unless the loan is well secured and any ongoing collection efforts are reasonably expected to result in repayment of all amounts due under the contractual terms of the loan.

Interest income on non-accrual loans is recognised only to the extent it is received in cash. Cash received on non-accrual loans where there is no doubt regarding full repayment (no impairment recognised in the form of a specific allowance) is first applied as repayment of the past due principal amount of the loan and secondly to past due interest and fees.

Where there is doubt regarding the ultimate full repayment of the non-accrual loan (impairment recognised in the form of a specific allowance), all cash received is applied to reduce the principal amount of the loan. Interest income on these loans is recognised only after the entire balance receivable is recovered and interest is actually received.

Loans are returned to accrual status when:

- none of the principal or accrued interest is past due (with certain exceptions as noted below) and the Bank expects repayment of the remaining contractual obligation; or
- when the loan becomes well secured and in the process of collection.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **Loans modified in a troubled debt restructuring ("TDR")**

A modification of a loan constitutes a TDR when a borrower is experiencing financial difficulty and the modification constitutes a concession from originally agreed terms. If a restructuring is considered a TDR, the Bank is required to make certain disclosures in the notes of the consolidated financial statements and individually evaluate the restructured loan for impairment. The Bank employs various types of concessions when modifying a loan that it would not otherwise consider which may include extension of repayment periods, interest rate reductions, principal or interest forgiveness, forbearance, and other actions intended to minimise economic loss and to avoid foreclosure or repossession of collateral.

Commercial and industrial loans modified in a TDR often involve temporary interest-only payments, term extensions, and converting revolving credit lines to term loans. Additional collateral, a co-borrower, or a guarantor is often requested. Commercial mortgage and construction loans modified in a TDR often involve extending the maturity date at an interest rate lower than the current market rate for new debt with similar risk, or substituting or adding a new borrower or guarantor. Construction loans modified in a TDR may also involve extending the interest-only payment period.

Residential mortgage modifications generally involve a short-term forbearance period after which the missed payments are added to the end of the loan term, thereby extending the maturity date. Interest continues to accrue on the missed payments and as a result, the effective yield on the mortgage remains unchanged. As the forbearance period usually involves an insignificant payment delay they typically do not meet the reporting criteria for a TDR.

Automobile loans modified in a TDR are primarily comprised of loans where the Bank has lowered monthly payments by extending the term.

When a loan undergoes a TDR, the determination of the loan's accrual versus non-accrual status following the modification depends on several factors. As with the risk rating process, the accrual status decision for such a loan is a separate and distinct process from the loan's TDR analysis and determination. Management considers the following in determining the accrual status of restructured loans:

- If the loan was appropriately on accrual status prior to the restructuring, the borrower has demonstrated performance under the previous terms, and the bank's credit evaluation shows the borrower's capacity to continue to perform under the restructured terms (both principal and interest payments), it is likely that the appropriate conclusion is for the loan to remain on accrual at the time of the restructuring. This evaluation must include consideration of the borrower's sustained historical repayment performance for a reasonable period prior to the date on which the loan was restructured. A sustained period of repayment performance generally would be a minimum of six months and would involve payments of cash or cash equivalents; or
- If the loan was on non-accrual status before the restructuring, but the bank's credit evaluation shows the borrower's capacity to meet the restructured terms, the loan would likely remain as non-accrual until the borrower has demonstrated a reasonable period of sustained repayment performance. As noted above, this period generally would be at least six months (thereby providing reasonable assurance as to the ultimate collection of principal and interest in full under the modified terms). Sustained performance before the restructuring may be taken into account.

Loans that have been modified in a TDR are restored to accrual status only when interest and principal payments are brought current for a continuous period of six months under the modified terms. However, performance prior to the modification, or significant events that coincide with the modification, are included in assessing whether the borrower can meet the new terms and may result in the loan being returned to accrual status at the time of loan modification or after a shorter performance period. If the borrower's ability to meet the revised payment schedule is uncertain, the loan remains on non-accrual status.

A loan that is modified in a TDR prior to becoming impaired will be left on accrual status if full collectability in accordance with the restructured terms is expected. The Bank works with its customers in these difficult economic times and may enter into a TDR for loans that are in default, or at risk of defaulting, even if the loan is not impaired.

A loan that had previously been modified in a TDR and is subsequently refinanced under current underwriting standards at a market rate with no concessionary terms is accounted for as a new loan and is no longer reported as a TDR.

### **Delinquencies**

The entire balance of an account is contractually delinquent if the minimum payment of principal or interest is not received by the specified due date. Delinquency is reported on loans that are more than 30 days past due.

### **Charge-offs**

The Bank recognises charge-offs when it determines that loans are uncollectible, and this generally occurs when all commercially reasonable means of recovering the loan balance have been exhausted.

Commercial and consumer loans are either fully or partially charged-off down to the fair value of collateral securing the loans when:

- management judges the loan to be uncollectible;
- repayment is expected to be protracted beyond reasonable time frames;
- the asset has been classified as a loss by either the Bank's internal loan review process or external examiners; or
- the customer has filed bankruptcy and the loss becomes evident owing to a lack of assets or cash flow.

The outstanding balance of commercial and consumer real estate secured loans and residential mortgages that are in excess of the estimated property value, less costs to sell, is charged-off once there is reasonable assurance that such excess outstanding balance is not recoverable.

Credit card consumer loans that are contractually 180 days past due and other consumer loans with an outstanding balance under \$100,000 that are contractually 180 days past due are generally written off and reported as charge-offs.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **i. Allowance for Credit Losses**

The Bank maintains an allowance for credit losses, which in management's opinion is adequate to absorb all estimated credit-related losses in its lending and off-balance sheet credit-related arrangements at the balance sheet date. The allowance for credit losses consists of specific allowances and a general allowance as follows:

#### **Specific allowances**

Specific allowances are determined on an exposure-by-exposure basis and reflect the associated estimated credit loss. The specific allowance for credit loss is computed as the difference between the recorded investment in the loan and the present value of expected future cash flows from the loan. The effective rate of return on the loan is used for discounting the cash flows. However, when foreclosure of a collateral-dependent loan is probable, the Bank measures impairment based on the fair value of the collateral. The Bank considers estimated costs to sell, on a discounted basis, in the measurement of impairment if those costs are expected to reduce the cash flows available to repay or otherwise satisfy the loan. If the measurement of an impaired loan is less than the recorded investment in the loan, then the Bank recognises impairment by creating an allowance with a corresponding charge to provision for credit losses.

#### **General allowances**

The allowance for credit losses attributed to the remaining portfolio is established through various analyses that estimate the incurred loss at the balance sheet date inherent in the lending and off-balance sheet credit-related arrangements portfolios. These analyses consider historical default rates and loss severities, geographic, industry, and other environmental factors. Management also considers overall portfolio indicators including trends in internally risk rated exposures, cash-basis loans, historical and forecasted write-offs, and a review of industry, geographic and portfolio concentrations, including current developments within those segments. In addition, management considers the current business strategy and credit process, including limit setting and compliance, credit approvals, loan underwriting criteria and loan workout procedures.

Each portfolio of smaller balance, homogeneous loans, including consumer instalment, revolving credit, and most other consumer loans, is collectively evaluated for impairment. The allowance for credit losses attributed to these loans is established via a process that estimates the probable losses inherent and incurred in the portfolio, based upon various analyses. Management considers overall portfolio indicators including historical credit losses; delinquent (defined as loans that are more than 30 days past due), non-performing, and classified loans; trends in volumes and terms of loans; an evaluation of overall credit quality; the credit process, including lending policies and procedures; and economic, geographical, product, and other environmental factors.

### **j. Business Combinations, Goodwill and Intangible Assets**

All business combinations are accounted for using the acquisition method. Identifiable intangible assets (mostly customer relationships) are recognised separately from goodwill and are initially valued at fair value using discounted cash flow calculations and other recognised valuation techniques. Goodwill represents the excess of the fair value of the consideration paid for the acquisition of a business over the fair value of the net assets acquired. Contingent purchase consideration was measured at its fair value and recorded on the purchase date. Any subsequent changes in the fair value of a contingent consideration liability will be recorded through the consolidated statements of operations.

Goodwill is tested annually for impairment at the reporting unit level, or more frequently if events or circumstances indicate there may be impairment. If the carrying amount of a reporting unit, including the allocated goodwill, exceeds its fair value, goodwill impairment is measured as the excess of the carrying amount of the reporting unit's allocated goodwill over the implied fair value of the goodwill. Other acquired intangible assets with finite lives are amortised on a straight-line basis over their estimated useful lives, not exceeding 15 years. Intangible assets' estimated lives are re-evaluated annually and an impairment test is carried out if certain indicators of impairment exist.

### **k. Premises, Equipment and Computer Software**

Land is carried at cost. Buildings, equipment and computer software, including leasehold improvements, are carried at cost less accumulated depreciation. The Bank generally computes depreciation using the straight-line method over the estimated useful life of an asset, which is 50 years for buildings, and three to 10 years for other equipment. For leasehold improvements the Bank uses the straight-line method over the lesser of the remaining term of the leased facility or the estimated economic life of the improvement. The Bank capitalises certain costs, including interest cost incurred during the development phase, associated with the acquisition or development of internal use software. Once the software is ready for its intended use, these costs are amortised on a straight-line basis over the software's expected useful life, which is between five and 10 years.

Management reviews the recoverability of the carrying amount of premises, equipment and computer software when indicators of impairment exist and an impairment charge is recorded when the carrying amount of the reviewed asset is deemed not recoverable by future expected cash flows to be derived from the use and disposition of the asset.

### **l. Other Real Estate Owned**

Other real estate owned ("OREO") is comprised of real estate property held for sale and commercial and residential real estate properties acquired in partial or total satisfaction of loans acquired through foreclosure proceedings, acceptance of a deed-in-lieu of foreclosure or by taking possession of assets that were used as loan collateral. These properties are initially recorded at fair value less estimated costs to sell the property. If the recorded investment in the loan exceeds the property's fair value at the time of acquisition, a charge-off is recorded against the specific allowance. If the carrying value of the real estate exceeds the property's fair value at the time of reclassification, an impairment charge is recorded in the consolidated statements of operations. Subsequent decreases in the property's fair value below the new cost basis are recorded through the use of a valuation allowance. Subsequent increases in the fair value of a property may be used to reduce the allowance but not below zero. Any operating expenses of the property are recognised through charges to non-interest expense.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **m. Derivatives**

All derivatives are recognised on the consolidated balance sheets at their fair value. On the date that the Bank enters into a derivative contract, it designates the derivative as: a hedge of the fair value of a recognised asset or liability (a fair value hedge); a hedge of a forecasted transaction or the variability of cash flows that are to be received or paid in connection with a recognised asset or liability (a cash flow hedge); a hedge of an exposure to foreign currency risk of a net investment in a foreign operation (a net investment hedge); or, an instrument that is held for trading or non-hedging purposes (a trading or non-hedging derivative instrument).

The changes in the fair value of a derivative that is designated and qualifies as a fair value hedge, along with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk, are recorded in current year earnings.

The changes in the fair value of a derivative that is designated and qualifies as a cash flow hedge, to the extent that the hedge is effective, are recorded in other comprehensive loss ("OCL") and the ineffective portion is recorded in current year earnings. That is, ineffectiveness from a derivative that overcompensates for changes in the hedged cash flows is recorded in earnings. However, the ineffectiveness from a derivative that under compensates is not recorded in earnings.

The changes in the fair value of a derivative that is designated and qualifies as a foreign currency hedge is recorded in either current year earnings or OCL, depends on whether the hedging relationship satisfies the criteria for a fair value or cash flow hedge. If, however, a derivative is used as a hedge of a net investment in a foreign operation, the changes in the derivative's fair value, to the extent that the derivative is effective as a hedge, are recorded in the cumulative translation adjustment ("CTA") account within OCL.

Changes in the fair value of trading and non-hedging derivative instruments are reported in current year earnings.

The Bank formally documents all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategies for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair value, cash flow, or foreign currency hedges to specific assets and liabilities on the consolidated balance sheets or specific firm commitments or forecasted transactions.

The Bank also formally assesses whether the derivatives that are used in hedging transactions have been highly effective in offsetting changes in the fair value or cash flows of hedged items and whether those derivatives may be expected to remain highly effective in future periods.

For those hedge relationships that are terminated, hedge designations that are elected to be removed, forecasted transactions that are no longer expected to occur, or the hedge relationship ceases to be highly effective, the hedge accounting treatment described in the paragraphs above is no longer applied and the end-user derivative is terminated or transferred to the trading designation. For fair value hedges, any changes to the carrying value of the hedged item prior to the discontinuance remain as part of the basis of the asset or liability. When a cash flow hedge is discontinued, the net derivative gain (loss) remains in AOCL unless it is probable that the forecasted transaction will not occur in the originally specified time period.

### **n. Securities Sold Under Agreements to Repurchase**

Securities sold under agreements to repurchase (securities financing agreements) are treated as collateralised financing transactions. The obligation to repurchase is recorded at the value of the cash received on sale adjusted for the amortisation of the difference between the sale price and the agreed repurchase price. The amortisation of this amount is recorded as an interest expense.

### **o. Collateral**

The Bank pledges assets as collateral as required for various transactions involving security repurchase agreements, deposit products and derivative financial instruments. Assets that have been pledged as collateral, including those that can be sold or repledged by the secured party, continue to be reported on the Bank's consolidated balance sheets under the same line items as non-pledged assets of the same type.

### **p. Employee Benefit Plans**

The Bank maintains trustee pension plans for substantially all employees as either non-contributory defined benefit plans or defined contribution plans. Benefits under the defined benefit plans are primarily based on the employee's years of credited service and average annual salary during the final years of employment as defined in the plans. The Bank also provides post-retirement medical benefits for certain qualifying active and retired Bermuda-based employees.

Expense for the defined benefit pension plans and the post-retirement medical benefits plan is comprised of (a) the actuarially determined benefits for the current year's service, (b) imputed interest on the actuarially determined liability of the plan, (c) in the case of the defined benefit pension plans, the expected investment return on the fair value of plan assets and (d) amortisation of certain items over the expected average remaining service life of employees in the case of the active defined benefit pension plans, estimated average remaining life expectancy of the inactive participants in the case of the inactive defined benefit pension plans and the expected average remaining service life to full eligibility age of employees covered by the plan in the case of the post-retirement medical benefits plan. The items amortised are amounts arising as a result of experience gains and losses, changes in assumptions, plan amendments and the change in the net pension asset or post-retirement medical benefits liability arising on adoption of revised accounting standards.

For each of the defined benefit pension plans and for the post-retirement medical benefits plan, the asset and liability recognised for accounting purposes are reported in other assets and employee benefit plans respectively. The actuarial gains and losses, transition obligation and prior service costs of the defined pension plans and post-retirement medical benefits plan are recognised in OCL net of tax and amortised to net income over the average service period for the active defined benefit pension plans and post-retirement medical benefits plan and average remaining life expectancy for the inactive defined benefit pension plans.

For the defined contribution pension plans, the Bank and participating employees provide an annual contribution based on each participating employee's pensionable earnings. Amounts paid are expensed in the period.



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### q. Share-Based Compensation

The Bank engages in equity settled share-based payment transactions in respect of services received from eligible employees. The fair value of the services received is measured by reference to the fair value of the shares or share options granted on the date of the grant. The cost of the employee services received in respect of the shares or share options granted is recognised in the consolidated statements of operations over the shorter of the vesting or service period.

The fair value of the options granted is determined using option pricing models, which take into account the exercise price of the option, the current share price, the risk-free interest rate, expected dividend rate, the expected volatility of the share price over the life of the option and other relevant factors. Time vesting conditions are taken into account by adjusting the number of shares or share options included in the measurement of the cost of employee services so that ultimately, the amount recognised in the consolidated statements of operations reflects the number of vested shares or share options. The Bank recognises compensation cost for awards with performance conditions if and when the Bank concludes that it is probable that the performance condition will be achieved, net of an estimate of pre-vesting forfeitures (e.g., due to termination of employment prior to vesting).

### r. Revenue Recognition

Trust, custody and other administration services fees include fees for private and institutional trust, executorship, and custody services. Asset management fees include fees for investment management, investment advice and brokerage services. Fees are recognised as revenue over the period of the relationship or when the Bank has rendered all services to the clients and is entitled to collect the fee from the client, as long as there are no contingencies associated with the fees.

Banking services fees primarily include fees for letters of credit and other financial guarantees, compensating balances, overdraft facilities and other financial services-related products as well as credit card fees. Letters of credit and other financial guarantees fees are recognised as revenue over the period in which the related guarantee is outstanding. Credit card fees are comprised of merchant discounts, late fees and membership fees, net of interchange and rewards costs. Credit card fees are recognised in the period in which the service is provided. All other fees are recognised as revenue in the period in which the service is provided.

Foreign exchange revenue includes fees earned on currency exchange transactions which are recognised when such transactions occur, as well as gains and losses recognised when translating financial instruments held or due in currencies other than the local functional currency at the rates of exchange prevailing at the balance sheet date.

Loan interest income includes the amortisation of deferred non-refundable loan origination and commitment fees. These fees are recognised as an adjustment of yield over the life of the related loan. Loan origination and commitment fees are offset by their related direct costs and only the net amounts are deferred and amortised into interest income.

Dividend and interest income, including amortisation of premiums and discounts, on securities for which cash flows are not considered uncertain are included in interest income in the consolidated statements of operations. Loans placed on non-accrual status and investments with uncertain cash flows are accounted for under the cost recovery method, whereby all principal, dividends, interest and coupon payments received are applied as a reduction of the amortised cost and carrying amount.

### s. Fair Values

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Bank determines the fair values of assets and liabilities based on the fair value hierarchy which requires an entity to maximise the use of observable inputs and minimise the use of unobservable inputs when measuring fair value. The relevant accounting standard describes three levels of inputs that may be used to measure fair value. Investments classified as trading and AFS, and derivative assets and liabilities are recognised in the consolidated balance sheets at fair value.

#### Level 1, 2 and 3 valuation inputs

Management classifies items that are recognised at fair value on a recurring basis based on the level of inputs used in their respective fair value determination as described below.

Fair value inputs are considered Level 1 when based on unadjusted quoted prices in active markets for identical assets.

Fair value inputs are considered Level 2 when based on internally developed models or based on prices published by independent pricing services using proprietary models. To qualify for Level 2, all significant inputs used in these models must be observable in the market place or can be corroborated by observable market data for substantially the full term of the instrument and includes, among others: interest yield curves, credit spreads, prices for similar assets and foreign exchange rates. Level 2 also includes financial instruments that are valued using quoted prices for identical assets but for which the market is not considered active due to low trading volumes.

Fair value inputs are considered Level 3 when based on internally developed models using significant unobservable assumptions involving management's estimations or non-binding bid quotes from brokers.

The following methods and assumptions were used in the determination of the fair value of financial instruments:

#### Cash due from banks

The carrying amount of cash and demand deposits with banks, being short-term in nature, is deemed to approximate fair value.

Cash equivalents include unrestricted term deposits, certificates of deposits and Treasury bills with a maturity of less than three months from the date of acquisition and the carrying value at cost is considered to approximate fair value because they are short term in nature, bear interest rates that approximate market rates, and generally have negligible credit risk.

#### Short-term investments

Short-term investments comprise restricted term and demand deposits and unrestricted term deposits, certificates of deposit and treasury bills with less than one year but greater than three months' maturity from the date of acquisition. The carrying value at cost is considered to approximate fair value because they are short term in nature, bear interest rates that approximate market rates, and generally have negligible credit risk.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **Trading investments and defined benefit pension plan equity securities and mutual funds**

Trading investments include equities, mutual funds and debt securities issued by both US and non-US governments. The fair value of listed equity securities is based upon quoted market values. Investments in actively traded mutual funds are based on their published net asset values. See "AFS and HTM investments and defined benefit pension plan fixed income securities" below for valuation techniques and inputs of fixed income securities.

### **AFS and HTM investments and defined benefit pension plan fixed income securities**

The fair values for AFS investments are generally sourced from third parties. The fair value of fixed income securities is based upon quoted market values where available, "evaluated bid" prices provided by third party pricing services ("pricing services") where quoted market values are not available, or by reference to broker or underwriter bid indications where pricing services do not provide coverage for a particular security. To the extent the Bank believes current trading conditions represent distressed transactions, the Bank may elect to utilise internally generated models. The pricing services typically use market approaches for valuations using primarily Level 2 inputs (in the vast majority of valuations), or some form of discounted cash flow analysis.

Pricing services indicate that they will only produce an estimate of fair value if there is objectively verifiable information available to produce a valuation. Standard inputs to the valuations provided by the pricing services listed in approximate order of priority for use when available include: reported trades, benchmark yields, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data. The pricing services may prioritise inputs differently on any given day for any security, and not all inputs listed are available for use in the evaluation process on any given day for each security evaluation. However, the pricing services also monitor market indicators and industry and economic events. When these inputs are not available, pricing services identify "buckets" of similar securities (allocated by asset class types, sectors, sub-sectors, contractual cash flows/structure, and credit rating characteristics) and apply some form of matrix or other modelled pricing to determine an appropriate security value which represents their best estimate as to what a buyer in the marketplace would pay for a security in a current sale.

It is common industry practice to utilise pricing services as a source for determining the fair values of investments where the pricing services are able to obtain sufficient market corroborating information to allow them to produce a valuation at a reporting date. In addition, in the majority of cases, although a value may be obtained from a particular pricing service for a security or class of similar securities, these values are corroborated against values provided by other pricing services. While the Bank receives values for the majority of the investment securities it holds from pricing services, it is ultimately management's responsibility to determine whether the values received and recorded in the financial statements are representative of appropriate fair value measurements.

Broker/dealer quotations are used to value investments with fixed maturities where prices are unavailable from pricing services due to factors specific to the security such as limited liquidity, lack of current transactions, or trades only taking place in privately negotiated transactions. These are considered Level 3 valuations, as significant inputs utilised by brokers may be difficult to corroborate with observable market data, or sufficient information regarding the specific inputs utilised by the broker was not available to support a Level 2 classification.

For disclosure purposes, investments held-to-maturity are fair valued using the same methods described above.

### **Loans**

The majority of loans are variable rate and re-price in response to changes in market rates and hence management estimates that the fair value of loans is not significantly different than their carrying amount. For significant fixed-rate loan exposures, fair value is estimated by discounting the future cash flows, using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities, of such loans.

### **Accrued interest**

The carrying amounts of accrued interest receivable and payable are assumed to approximate their fair values given their short-term nature.

### **OREO**

OREO assets are carried at the lower of cost or fair value less estimated costs to sell. The determination of fair value, which aims at estimating the realisable value of the properties, is based either on third party appraisals, when available, or on internal valuation models. Appraisals of OREO properties are updated on an annual basis.

### **Deposits**

The fair value of fixed-rate deposits has been estimated by discounting the contractual cash flows, using market interest rates offered at the balance sheet date for deposits of similar terms. The carrying amount of deposits with no stated maturity date is deemed to equate to the fair value.

### **Long-term debt**

The fair value of the long-term debt has been estimated by discounting the contractual cash flows, using current market interest rates.

### **Derivatives**

Derivative contracts can be exchange traded or over-the-counter ("OTC") derivative contracts and may include forward, swap and option contracts relating to interest rates or foreign currencies. Exchange-traded derivatives typically fall within Level 1 of the fair value hierarchy depending on whether they are deemed to be actively traded or not. OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources where an understanding of the inputs utilised in arriving at the valuations is obtained.

Where models are used, the selection of a particular model to value an OTC derivative depends upon the contractual terms and specific risks inherent in the instrument as well as the availability of pricing information in the market. The Bank generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, interest rate swaps and options, model inputs can generally be verified and model selection does not involve significant management judgment.

# **The Bank of N.T. Butterfield & Son Limited**

## **Notes to the Consolidated Financial Statements**

*(In thousands of Bermuda dollars, unless otherwise stated)*

### **Goodwill**

The fair value of reporting units for which goodwill is recognised is determined when an impairment assessment is performed by discounting estimated future cash flows using discount rates reflecting valuation-date market conditions and risks specific to the reporting unit.

### **t. Impairment or Disposal of Long-Lived Assets**

Impairment losses are recognised when the carrying amount of a long-lived asset exceeds the sum of the undiscounted cash flows expected from its use and disposal. The impairment recognised is measured as the amount by which the carrying amount of the asset exceeds its fair value. Long-lived assets that are to be disposed of other than by sale are classified and accounted for as held for use until the date of disposal or abandonment. Assets that meet certain criteria are classified as held for sale and are measured at the lower of their carrying amounts or fair value less estimated costs to sell.

### **u. Credit-Related Arrangements**

In the normal course of business, the Bank enters into various commitments to meet the credit requirements of its customers. Such commitments, which are not included in the consolidated balance sheet, include:

- commitments to extend credit, which represent undertakings to make credit available in the form of loans or other financing for specific amounts and maturities, subject to certain conditions;
- standby letters of credit, which represent irrevocable obligations to make payments to third parties in the event that the customer is unable to meet its financial obligations; and,
- documentary and commercial letters of credit, related primarily to the import of goods by customers, which represent agreements to honour drafts presented by third parties upon completion of specific activities.

These credit arrangements are subject to the Bank's normal credit standards and collateral is obtained where appropriate. The contractual amounts for these commitments set out in the table in Note 12 represent the maximum payments the Bank would have to make should the contracts be fully drawn, the counterparty default, and any collateral held prove to be of no value. As many of these arrangements will expire or terminate without being drawn upon or are fully collateralised, the contractual amounts do not necessarily represent future cash requirements. The Bank does not carry any liability for these obligations.

### **v. Income Taxes**

The Bank uses the asset and liability method of accounting for income taxes. Under this method, deferred income taxes reflect the net tax effect of temporary differences between the consolidated financial statements' carrying amounts of assets and liabilities and their respective tax bases. Accordingly, a deferred income tax asset or liability is determined for each temporary difference based on the enacted tax rates to be in effect on the expected reversal date of the temporary difference. The effect of a change in tax rates on deferred tax assets and liabilities is recognised in income in the period that includes the enactment date.

The Bank records net deferred tax assets to the extent the Bank believes these assets will more likely than not be realised. Net deferred income tax assets or liabilities accumulated as a result of temporary differences are included in other assets or other liabilities, respectively. A valuation allowance is established to reduce deferred income tax assets to the amount more likely than not to be realised. In making such a determination, the Bank considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax-planning strategies, and results of recent operations. In the event the Bank were to determine that it would be able to realise the deferred income tax assets in the future in excess of their net recorded amount, the Bank would make an adjustment to the deferred tax asset valuation allowance, which would reduce the provision for income taxes.

The Bank records uncertain tax positions on the basis of a two-step process whereby (1) the Bank determines whether it is more likely than not that the tax positions will be sustained based on the technical merits of the position and (2) where those tax positions that meet the more-likely-than-not recognition threshold, the Bank recognises the largest amount of tax benefit that is greater than 50 percent likely to be realised upon ultimate settlement with the related tax authority.

Income taxes on the consolidated statements of operations include the current and deferred portions of the income taxes. The Bank recognises accrued interest and penalties related to income taxes in operating expenses. Income taxes applicable to items charged or credited directly to shareholders' equity are included in such items.

### **w. Consolidated Statements of Cash Flows**

For the purposes of the consolidated statements of cash flows, cash due from banks include cash on hand, cash items in the process of collection, amounts due from correspondent banks and highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in fair value.

### **x. Earnings Per Share**

Earnings per share have been calculated using the weighted average number of common shares outstanding during the year (see also Note 20). Dividends declared on preference shares and related guarantee fees are deducted from net income to obtain net income available to common shareholders. In periods when basic earnings per share is positive, the dilutive effect of share-based compensation plans is calculated using the treasury stock method, whereby the proceeds received from the exercise of share-based awards are assumed to be used to repurchase outstanding common shares, using the quarterly average market price of the Bank's shares for the period.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

*(In thousands of Bermuda dollars, unless otherwise stated)*

### y. New Accounting Pronouncements

The following accounting developments were issued during the year ended 31 December 2015:

In February 2015, the Financial Accounting Standards Board ("FASB") published Accounting Standards Update No. 2015-02 Consolidation (Topic 810) which provides amendments to the current consolidation analysis which affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to re-evaluation under the revised consolidation model. Specifically, the amendments: modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities (VIEs) or voting interest entities; eliminate the presumption that a general partner should consolidate a limited partnership; affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships; and provide a scope exception for entities required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The update is effective for public business entities for annual periods, and interim periods within those fiscal years, beginning after 15 December 2015. Early adoption is permitted, including adoption in an interim period. The Bank has early adopted this guidance and has applied a full retrospective adoption approach. There has not been a material impact on the Bank's consolidated financial position or results of operations.

In April 2015, FASB published Accounting Standards Update No. 2015-03 Interest - Imputation of Interest (Subtopic 835-30) which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The update is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after 15 December 2015. Early adoption is permitted for financial statements that have not been previously issued. The Bank has assessed the adoption of this guidance based upon its current balance of debt issuance costs and determined that the adoption of this guidance is not expected to have an impact on the Bank's consolidated financial position.

In April 2015, FASB published Accounting Standards Update No. 2015-05 Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40) to provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If not, the arrangement should be accounted for as a service contract. The update is effective for public business entities for annual periods, and interim periods within those annual periods, beginning after 15 December 2015. Early adoption is permitted. The Bank is assessing the impact of the adoption of this guidance.

In April 2015, FASB published Accounting Standards Update No. 2015-07 Fair Value Measurement (Topic 820) which removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. Current US GAAP requires that investments for which fair value is measured at net asset value (or its equivalent) using the practical expedient in Topic 820 be categorized within the fair value hierarchy using criteria that differs from the criteria used to categorize other fair value measurements within the hierarchy. Under the amendments in this update, investments for which fair value is measured at net asset value per share (or its equivalent) using the practical expedient should not be categorized in the fair value hierarchy. The update is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after 15 December 2015 and should be applied retrospectively to all periods presented. Early application is permitted. The Bank is assessing the impact of the adoption of this guidance.

In July 2015, the FASB issued Accounting Standards Update (ASU) No. 2015-12, (Part I) Fully Benefit-Responsive Investment Contracts, (Part II) Plan Investment Disclosures, (Part III) Measurement Date Practical Expedient. The ASU (1) requires a pension plan to use contract value as the only measure for fully benefit-responsive investment contracts, (2) simplifies and increases the effectiveness of the investment disclosure requirements for employee benefit plans, and (3) provides benefit plans with a measurement-date practical expedient which provides guidance for when a benefit plan's fiscal year end does not coincide with the end of a calendar month. The Bank does not have a fully benefit responsive investment contract, and the Bank's benefit plans' each have a fiscal year coinciding with a month end, and accordingly the Bank has concluded that Part I and Part III are not applicable. The amendments in all three parts of this Update are effective for fiscal years beginning after 15 December 2015. Earlier application is permitted. The Bank has concluded that its current disclosures meet the requirements as directed under Part II, and therefore the adoption of this guidance is not expected to have an impact on the Bank's consolidated financial statements.

In August 2015, FASB published Accounting Standards Update No. 2015-14 Revenue from Contracts with Customers (Topic 606) which defers the effective date of Accounting Standards Update No. 2014-09 for all entities by one year. Public business entities should apply the guidance in Update 2014-09 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period.

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**  
*(In thousands of Bermuda dollars, unless otherwise stated)*

**Note 3: Cash due from banks**

	31 December 2015			31 December 2014		
	Bermuda	Non-Bermuda	Total	Bermuda	Non-Bermuda	Total
<b>Unrestricted</b>						
<b>Non-interest earning</b>						
Cash and demand deposits with banks	31,199	79,696	110,895	23,609	116,056	139,665
<b>Interest earning<sup>1</sup></b>						
Demand deposits with banks	130,589	248,040	378,629	203,572	139,049	342,621
Cash equivalents	691,439	1,107,927	1,799,366	469,388	1,111,637	1,581,025
<b>Sub-total - Interest earning</b>	<b>822,028</b>	<b>1,355,967</b>	<b>2,177,995</b>	<b>672,960</b>	<b>1,250,686</b>	<b>1,923,646</b>
<b>Total cash due from banks</b>	<b>853,227</b>	<b>1,435,663</b>	<b>2,288,890</b>	<b>696,569</b>	<b>1,366,742</b>	<b>2,063,311</b>

<sup>1</sup> Interest earning cash due from banks includes certain demand deposits with banks as at 31 December 2015 in the amount of \$306.9 million (31 December 2014: \$311.6 million) that are earning interest at a negligible rate.

**Note 4: Short-term investments**

	31 December 2015			31 December 2014		
	Bermuda	Non-Bermuda	Total	Bermuda	Non-Bermuda	Total
<b>Unrestricted term deposits, certificate of deposits and treasury bills</b>						
Maturing within three months	-	104,249	104,249	-	144,632	144,632
Maturing between three to six months	99,810	192,118	291,928	-	223,563	223,563
Maturing between six to twelve months	-	796	796	-	15,694	15,694
<b>Total unrestricted short-term investments</b>	<b>99,810</b>	<b>297,163</b>	<b>396,973</b>	<b>-</b>	<b>383,889</b>	<b>383,889</b>
<b>Affected by drawing restrictions related to minimum reserve and derivative margin requirements</b>						
Interest earning demand deposits	12,509	-	12,509	9,141	1,740	10,881
<b>Total short-term investments</b>	<b>112,319</b>	<b>297,163</b>	<b>409,482</b>	<b>9,141</b>	<b>385,629</b>	<b>394,770</b>

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**

(In thousands of Bermuda dollars, unless otherwise stated)

**Note 5: Investment in securities**

**Amortised Cost, Carrying Amount and Fair Value**

On the consolidated balance sheets trading and available-for-sale ("AFS") investments are carried at fair value and held-to-maturity ("HTM") investments are carried at amortised cost.

	31 December 2015				31 December 2014			
	Amortised cost	Gross unrealised gains	Gross unrealised losses	Fair value	Amortised cost	Gross unrealised gains	Gross unrealised losses	Fair value
<b>Trading</b>								
Certificates of deposit	-	-	-	-	37,724	19	-	37,743
US government and federal agencies	278,500	2,347	(1,504)	279,343	311,061	3,448	(2,002)	312,507
Debt securities issued								
by non-US governments	7,483	6	-	7,489	7,600	52	-	7,652
Asset-backed securities - Student loans	28,845	-	(560)	28,285	52,847	-	(250)	52,597
Mutual funds	5,739	903	(460)	6,182	6,793	1,037	(944)	6,886
<b>Total trading</b>	<b>320,567</b>	<b>3,256</b>	<b>(2,524)</b>	<b>321,299</b>	<b>416,025</b>	<b>4,556</b>	<b>(3,196)</b>	<b>417,385</b>
<b>Available-for-sale</b>								
US government and federal agencies	1,399,456	8,812	(3,769)	1,404,499	1,570,665	13,694	(8,996)	1,575,363
Debt securities issued								
by non-US governments	29,275	300	-	29,575	30,654	144	(125)	30,673
Corporate debt securities	505,139	3,779	(2,774)	506,144	391,059	9,393	(1,163)	399,289
Asset-backed securities - Student loans	13,291	-	(1,130)	12,161	13,290	-	(1,064)	12,226
Commercial mortgage-backed securities	153,046	9	(4,329)	148,726	154,211	33	(3,075)	151,169
Residential mortgage-backed securities - Prime	101,382	-	(1,138)	100,244	65,167	264	(602)	64,829
<b>Total available-for-sale</b>	<b>2,201,589</b>	<b>12,900</b>	<b>(13,140)</b>	<b>2,201,349</b>	<b>2,225,046</b>	<b>23,528</b>	<b>(15,025)</b>	<b>2,233,549</b>
<b>Held-to-maturity<sup>1</sup></b>								
US government and federal agencies	701,282	5,365	(5,152)	701,495	338,177	6,330	(518)	343,989
<b>Total held-to-maturity</b>	<b>701,282</b>	<b>5,365</b>	<b>(5,152)</b>	<b>701,495</b>	<b>338,177</b>	<b>6,330</b>	<b>(518)</b>	<b>343,989</b>

<sup>1</sup> For the years ended 31 December 2015 and 2014, non-credit impairments recognised in accumulated other comprehensive loss ("AOCL") for HTM investments were \$nil.



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Investments with Unrealised Loss Positions

In the following tables, debt securities with unrealised losses that are not deemed to be other-than-temporary-impairment ("OTTI") are categorised as being in a loss position for "less than 12 months" or "12 months or more" based on the point in time that the fair value most recently declined below the amortised cost basis.

	<u>Less than 12 months</u>		<u>12 months or more</u>			
	Fair	Gross	Fair	Gross	Total	Total gross
	value	unrealised	value	unrealised	fair value	unrealised
<b>31 December 2015</b>		losses		losses		losses
<b>Available-for-sale securities with unrealised losses</b>						
US government and federal agencies	364,939	(865)	177,224	(2,904)	542,163	(3,769)
Debt securities issued by non-US governments	-	-	-	-	-	-
Corporate debt securities	253,991	(1,480)	38,706	(1,294)	292,697	(2,774)
Asset-backed securities - Student loans	-	-	12,160	(1,130)	12,160	(1,130)
Commercial mortgage-backed securities	-	-	147,822	(4,329)	147,822	(4,329)
Residential mortgage-backed securities - Prime	90,220	(660)	10,024	(478)	100,244	(1,138)
<b>Total available-for-sale securities with unrealised losses</b>	<b>709,150</b>	<b>(3,005)</b>	<b>385,936</b>	<b>(10,135)</b>	<b>1,095,086</b>	<b>(13,140)</b>
<b>Held-to-maturity securities with unrealised losses</b>						
US government and federal agencies	217,768	(2,138)	241,855	(3,014)	459,623	(5,152)
<b>31 December 2014</b>						
	<u>Less than 12 months</u>		<u>12 months or more</u>			
	Fair	Gross	Fair	Gross	Total	Total gross
	value	unrealised	value	unrealised	fair value	unrealised
<b>Available-for-sale securities with unrealised losses</b>						
US government and federal agencies	281,469	(2,294)	263,586	(6,702)	545,055	(8,996)
Debt securities issued by non-US governments	22,588	(125)	-	-	22,588	(125)
Corporate debt securities	8,090	(8)	38,845	(1,155)	46,935	(1,163)
Asset-backed securities - Student loans	-	-	12,226	(1,064)	12,226	(1,064)
Commercial mortgage-backed securities	-	-	150,216	(3,075)	150,216	(3,075)
Residential mortgage-backed securities - Prime	-	-	18,116	(602)	18,116	(602)
<b>Total available-for-sale securities with unrealised losses</b>	<b>312,147</b>	<b>(2,427)</b>	<b>482,989</b>	<b>(12,598)</b>	<b>795,136</b>	<b>(15,025)</b>
<b>Held-to-maturity securities with unrealised losses</b>						
US government and federal agencies	-	-	60,556	(518)	60,556	(518)

The Bank does not believe that the investment securities that were in an unrealised loss position as of 31 December 2015, which were comprised of 99 securities representing 54% of the portfolio's fair value, represent an OTTI. Total gross unrealised losses were 1.1% of the fair value of affected securities and were attributable primarily to changes in market interest rates, relative to when the investment securities were purchased, and not due to the credit quality of the investment securities. Due to a strategic change in the investment portfolio composition during the year ended 31 December 2015, several AFS securities were sold while being in an unrealised loss position. The Bank considers this to be a one-time event, and has determined that it is more likely than not that the Bank will not be required to sell any of the remaining investment securities before recovery of the amortised cost basis.

The following describes the processes for identifying credit impairment in security types with the most significant unrealised losses as shown in the preceding tables.

Management believes that all the **US government and federal agencies** securities do not have any credit losses, given the explicit and implicit guarantees provided by the US federal government.

The unrealised losses in **Corporate debt securities** relate primarily to one debt security issued by a US government-sponsored enterprise and is implicitly backed by the US federal government. Management believes that the value of this security will recover and the current unrealised loss position is a result of interest rate movements.

Investments in **Asset-backed securities - Student loans** are composed primarily of securities collateralised by Federal Family Education Loan Program loans ("FFELP loans"). FFELP loans benefit from a US federal government guarantee of at least 97% of defaulted principal and accrued interest, with additional credit support provided in the form of over-collateralisation, subordination and excess spread, which collectively total in excess of 100%. Accordingly, the vast majority of FFELP loan-backed securities are not exposed to traditional consumer credit risk.

Investments in **Commercial mortgage-backed securities** are predominantly senior securities rated "AAA" and possess significant subordination, a form of credit enhancement expressed hereafter as the percentage of pool losses that can occur before the senior securities held by the Bank will incur its first dollar of principal loss. No credit losses were recognised on these securities as credit support and loan-to-value ratios ("LTV") range from 5% - 36% and 24% - 61%, respectively. Current credit support is significantly greater than any delinquencies experienced on the underlying mortgages.

Investments in **Residential mortgage-backed securities - Prime** are predominantly rated "AAA" and possess significant credit enhancement as described above. No credit losses were recognised on these securities as there are no delinquencies over 30 days on the underlying mortgages and the weighted average credit support and LTV ratios range from 8% - 16% and 58% - 69%, respectively.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Investments' Contractual Maturities

The following table presents the remaining contractual maturities of the Bank's securities. For mortgage-backed securities (primarily US government agencies), management presents the maturity date as the mid-point between the reporting and expected contractual maturity date which is determined assuming no future prepayments. By using the aforementioned mid-point, this date represents management's best estimate of the date by which the remaining principal balance will be repaid given future principal repayments of such securities. The actual maturities may differ due to the uncertainty of the timing when borrowers make prepayments on the underlying mortgages.

	Remaining term to average contractual maturity					No specific maturity	Carrying amount
	Within 3 months	3 to 12 months	1 to 5 years	5 to 10 years	Over 10 years		
<b>31 December 2015</b>							
<b>Trading</b>							
US government and federal agencies	-	24,874	8,497	53,248	192,724	-	279,343
Debt securities issued by non-US governments	7,489	-	-	-	-	-	7,489
Asset-backed securities - Student loans	-	-	28,285	-	-	-	28,285
Mutual funds	-	-	-	-	-	6,182	6,182
<b>Total trading</b>	<b>7,489</b>	<b>24,874</b>	<b>36,782</b>	<b>53,248</b>	<b>192,724</b>	<b>6,182</b>	<b>321,299</b>
<b>Available-for-sale</b>							
US government and federal agencies	-	-	126,163	202,385	1,075,951	-	1,404,499
Debt securities issued by non-US governments	-	1,360	5,399	22,816	-	-	29,575
Corporate debt securities	60,493	55,649	351,296	38,706	-	-	506,144
Asset-backed securities - Student loans	-	-	-	-	12,161	-	12,161
Commercial mortgage-backed securities	-	-	-	42,532	106,194	-	148,726
Residential mortgage-backed securities - Prime	-	-	-	-	100,244	-	100,244
<b>Total available-for-sale</b>	<b>60,493</b>	<b>57,009</b>	<b>482,858</b>	<b>306,439</b>	<b>1,294,550</b>	<b>-</b>	<b>2,201,349</b>
<b>Held-to-maturity</b>							
US government and federal agencies	-	-	-	45,664	655,618	-	701,282
<b>Total investments</b>	<b>67,982</b>	<b>81,883</b>	<b>519,640</b>	<b>405,351</b>	<b>2,142,892</b>	<b>6,182</b>	<b>3,223,930</b>
<b>Total by currency</b>							
US dollars	67,982	81,883	519,640	405,351	2,142,892	5,903	3,223,651
Other	-	-	-	-	-	279	279
<b>Total investments</b>	<b>67,982</b>	<b>81,883</b>	<b>519,640</b>	<b>405,351</b>	<b>2,142,892</b>	<b>6,182</b>	<b>3,223,930</b>

	Remaining term to average contractual maturity					No specific maturity	Carrying amount
	Within 3 months	3 to 12 months	1 to 5 years	5 to 10 years	Over 10 years		
<b>31 December 2014</b>							
<b>Trading</b>							
Certificates of deposit	18,246	19,497	-	-	-	-	37,743
US government and federal agencies	-	-	34,479	49,262	228,766	-	312,507
Debt securities issued by non-US governments	-	-	7,652	-	-	-	7,652
Asset-backed securities - Student loans	-	-	52,597	-	-	-	52,597
Mutual funds	-	-	-	-	-	6,886	6,886
<b>Total trading</b>	<b>18,246</b>	<b>19,497</b>	<b>94,728</b>	<b>49,262</b>	<b>228,766</b>	<b>6,886</b>	<b>417,385</b>
<b>Available-for-sale</b>							
US government and federal agencies	-	-	65,826	286,507	1,223,030	-	1,575,363
Debt securities issued by non-US governments	-	1,360	6,724	22,589	-	-	30,673
Corporate debt securities	8,090	121,930	230,424	38,845	-	-	399,289
Asset-backed securities - Student loans	-	-	-	-	12,226	-	12,226
Commercial mortgage-backed securities	-	-	-	43,128	108,041	-	151,169
Residential mortgage-backed securities - Prime	-	-	-	6,448	58,381	-	64,829
<b>Total available-for-sale</b>	<b>8,090</b>	<b>123,290</b>	<b>302,974</b>	<b>397,517</b>	<b>1,401,678</b>	<b>-</b>	<b>2,233,549</b>
<b>Held-to-maturity</b>							
US government and federal agencies	-	-	-	48,820	289,357	-	338,177
<b>Total investments</b>	<b>26,336</b>	<b>142,787</b>	<b>397,702</b>	<b>495,599</b>	<b>1,919,801</b>	<b>6,886</b>	<b>2,989,111</b>
<b>Total by currency</b>							
US dollars	13,088	123,290	397,702	495,599	1,919,801	6,037	2,955,517
Other	13,248	19,497	-	-	-	849	33,594
<b>Total investments</b>	<b>26,336</b>	<b>142,787</b>	<b>397,702</b>	<b>495,599</b>	<b>1,919,801</b>	<b>6,886</b>	<b>2,989,111</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Pledged Investments

The Bank pledges certain US government and federal agencies investment securities to further secure the Bank's issued customer deposit products. The secured party does not have the right to sell or repledge the collateral. The amounts of investments pledged are as follows:

	31 December 2015		31 December 2014	
	Amortised cost	Fair value	Amortised cost	Fair value
Classified as available-for-sale	304,493	307,513	381,434	383,665
Classified as held-to-maturity	372,546	372,868	107,837	110,175

### Sale Proceeds and Realised Gains and Losses of AFS Securities

	Year ended			31 December 2014	
	31 December 2015	31 December 2015	31 December 2015	31 December 2014	31 December 2014
	Sale proceeds	Realised gains (losses)	Transfers to HTM <sup>1</sup>	Sale proceeds	Realised gains (losses)
Certificates of deposit	-	-	-	-	-
US government and federal agencies	232,372	(4,465)	340,969	96,031	(52)
Debt securities issued by non-US governments	-	-	-	-	-
Residential mortgage-backed securities - Prime	6,056	(270)	-	-	-
Pass-through note	328	328	-	34,422	8,732
<b>Net realised gains (losses) recognised in net income</b>	<b>238,756</b>	<b>(4,407)</b>	<b>340,969</b>	<b>130,453</b>	<b>8,680</b>

<sup>1</sup> During 2015, certain investments were transferred out of the AFS categorization and into HTM. The transfers were recorded at fair value of the securities on the date of transfer. The related net unrealised losses of \$2.7 million that was recorded in AOCI will be accreted over the remaining life of the transferred investments using the effective interest rate method.

### Note 6: Loans

The "Bermuda" and "Non-Bermuda" classifications purpose is to reflect management segment reporting as described in Note 15: Segmented information.

	31 December 2015			31 December 2014		
	Bermuda	Non-Bermuda	Total	Bermuda	Non-Bermuda	Total
<b>Commercial loans</b>						
Government	202,776	22,402	225,178	66,708	46,776	113,484
Commercial and industrial	121,466	221,243	342,709	137,053	251,392	388,445
Commercial overdrafts	34,997	5,736	40,733	48,107	11,194	59,301
Total gross commercial loans	359,239	249,381	608,620	251,868	309,362	561,230
Less specific allowance for credit losses on commercial loans	(590)	-	(590)	(352)	(65)	(417)
<b>Total commercial loans after specific allowance for credit losses</b>	<b>358,649</b>	<b>249,381</b>	<b>608,030</b>	<b>251,516</b>	<b>309,297</b>	<b>560,813</b>
<b>Commercial real estate loans</b>						
Commercial mortgage	415,747	249,622	665,369	415,315	281,663	696,978
Construction	5,396	8,211	13,607	-	20,617	20,617
Total gross commercial real estate loans	421,143	257,833	678,976	415,315	302,280	717,595
Less specific allowance for credit losses on commercial real estate loans	(727)	(2,224)	(2,951)	(770)	(1,052)	(1,822)
<b>Total commercial real estate loans after specific allowance for credit losses</b>	<b>420,416</b>	<b>255,609</b>	<b>676,025</b>	<b>414,545</b>	<b>301,228</b>	<b>715,773</b>
<b>Consumer loans</b>						
Automobile financing	12,308	7,556	19,864	12,639	7,716	20,355
Credit card	59,119	19,839	78,958	58,500	20,684	79,184
Overdrafts	4,750	8,165	12,915	12,935	8,208	21,143
Other consumer	32,022	84,062	116,084	43,679	113,941	157,620
Total gross consumer loans	108,199	119,622	227,821	127,753	150,549	278,302
Less specific allowance for credit losses on consumer loans	(274)	-	(274)	(355)	-	(355)
<b>Total consumer loans after specific allowance for credit losses</b>	<b>107,925</b>	<b>119,622</b>	<b>227,547</b>	<b>127,398</b>	<b>150,549</b>	<b>277,947</b>
<b>Residential mortgage loans</b>						
Less specific allowance for credit losses on residential mortgage loans	(13,411)	(1,879)	(15,290)	(14,771)	(1,446)	(16,217)
<b>Total residential mortgage loans after specific allowance for credit losses</b>	<b>1,229,810</b>	<b>1,288,940</b>	<b>2,518,750</b>	<b>1,256,096</b>	<b>1,237,170</b>	<b>2,493,266</b>
<b>Total gross loans</b>	<b>2,131,802</b>	<b>1,917,655</b>	<b>4,049,457</b>	<b>2,065,803</b>	<b>2,000,807</b>	<b>4,066,610</b>
Less specific allowance for credit losses	(15,002)	(4,103)	(19,105)	(16,248)	(2,563)	(18,811)
Less general allowance for credit losses	(20,176)	(10,021)	(30,197)	(18,992)	(9,679)	(28,671)
<b>Net loans</b>	<b>2,096,624</b>	<b>1,903,531</b>	<b>4,000,155</b>	<b>2,030,563</b>	<b>1,988,565</b>	<b>4,019,128</b>

The principal means of securing residential mortgages, personal, credit card and business loans are charges over assets and guarantees. Mortgage loans are generally repayable over periods of up to thirty years and personal, business and government loans are generally repayable over terms not exceeding five years. Amounts owing on credit cards are revolving and typically a minimum amount is due within 30 days from billing. The effective yield on total loans as at 31 December 2015 is 4.57% (31 December 2014: 4.51%).

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Age Analysis of Past Due Loans (Including Non-Accrual Loans)

The following tables summarise the past due status of the loans as at 31 December 2015 and 2014. The aging of past due amounts are determined based on the contractual delinquency status of payments under the loan and this aging may be affected by the timing of the last business day at period end.

	30 - 59 days	60 - 89 days	More than 90 days	Total past due loans	Total current <sup>1</sup>	Total loans
<b>31 December 2015</b>						
<b>Commercial loans</b>						
Government	-	-	-	-	225,178	225,178
Commercial and industrial	11	14	608	633	342,076	342,709
Commercial overdrafts	-	-	25	25	40,708	40,733
<b>Total commercial loans</b>	<b>11</b>	<b>14</b>	<b>633</b>	<b>658</b>	<b>607,962</b>	<b>608,620</b>
<b>Commercial real estate loans</b>						
Commercial mortgage	1,133	-	6,658	7,791	657,578	665,369
Construction	-	-	-	-	13,607	13,607
<b>Total commercial real estate loans</b>	<b>1,133</b>	<b>-</b>	<b>6,658</b>	<b>7,791</b>	<b>671,185</b>	<b>678,976</b>
<b>Consumer loans</b>						
Automobile financing	194	81	78	353	19,511	19,864
Credit card	1,459	337	132	1,928	77,030	78,958
Overdrafts	-	-	538	538	12,377	12,915
Other consumer	832	979	1,231	3,042	113,042	116,084
<b>Total consumer loans</b>	<b>2,485</b>	<b>1,397</b>	<b>1,979</b>	<b>5,861</b>	<b>221,960</b>	<b>227,821</b>
<b>Residential mortgage loans</b>	<b>40,793</b>	<b>8,911</b>	<b>65,343</b>	<b>115,047</b>	<b>2,418,993</b>	<b>2,534,040</b>
<b>Total gross loans</b>	<b>44,422</b>	<b>10,322</b>	<b>74,613</b>	<b>129,357</b>	<b>3,920,100</b>	<b>4,049,457</b>

<sup>1</sup> Loans less than 30 days past due are included in current loans.

	30 - 59 days	60 - 89 days	More than 90 days	Total past due loans	Total current <sup>1</sup>	Total loans
<b>31 December 2014</b>						
<b>Commercial loans</b>						
Government	-	-	-	-	113,484	113,484
Commercial and industrial	357	29	1,776	2,162	386,283	388,445
Commercial overdrafts	-	-	61	61	59,240	59,301
<b>Total commercial loans</b>	<b>357</b>	<b>29</b>	<b>1,837</b>	<b>2,223</b>	<b>559,007</b>	<b>561,230</b>
<b>Commercial real estate loans</b>						
Commercial mortgage	909	1,001	9,054	10,964	686,014	696,978
Construction	-	-	-	-	20,617	20,617
<b>Total commercial real estate loans</b>	<b>909</b>	<b>1,001</b>	<b>9,054</b>	<b>10,964</b>	<b>706,631</b>	<b>717,595</b>
<b>Consumer loans</b>						
Automobile financing	165	19	152	336	20,019	20,355
Credit card	753	384	202	1,339	77,845	79,184
Overdrafts	-	-	10	10	21,133	21,143
Other consumer	856	270	1,653	2,779	154,841	157,620
<b>Total consumer loans</b>	<b>1,774</b>	<b>673</b>	<b>2,017</b>	<b>4,464</b>	<b>273,838</b>	<b>278,302</b>
<b>Residential mortgage loans</b>	<b>29,577</b>	<b>15,889</b>	<b>80,812</b>	<b>126,278</b>	<b>2,383,205</b>	<b>2,509,483</b>
<b>Total gross loans</b>	<b>32,617</b>	<b>17,592</b>	<b>93,720</b>	<b>143,929</b>	<b>3,922,681</b>	<b>4,066,610</b>

<sup>1</sup> Loans less than 30 days past due are included in current loans.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Loans' Credit Quality

The four credit quality classifications set out in the following tables are defined below and describe the credit quality of the Bank's lending portfolio. These classifications each encompass a range of more granular, internal credit rating grades assigned.

31 December 2015	Pass	Special mention	Substandard	Non-accrual <sup>1</sup>	Total gross recorded investments
<b>Commercial loans</b>					
Government	213,928	11,250	-	-	225,178
Commercial and industrial	333,853	4,133	4,106	617	342,709
Commercial overdrafts	36,017	4,493	197	26	40,733
<b>Total commercial loans</b>	<b>583,798</b>	<b>19,876</b>	<b>4,303</b>	<b>643</b>	<b>608,620</b>
<b>Commercial real estate loans</b>					
Commercial mortgage	542,195	86,285	26,629	10,260	665,369
Construction	13,607	-	-	-	13,607
<b>Total commercial real estate loans</b>	<b>555,802</b>	<b>86,285</b>	<b>26,629</b>	<b>10,260</b>	<b>678,976</b>
<b>Consumer loans</b>					
Automobile financing	19,378	388	-	98	19,864
Credit card	78,826	-	132	-	78,958
Overdrafts	11,618	54	1,232	11	12,915
Other consumer	112,426	1,308	1,056	1,294	116,084
<b>Total consumer loans</b>	<b>222,248</b>	<b>1,750</b>	<b>2,420</b>	<b>1,403</b>	<b>227,821</b>
<b>Residential mortgage loans</b>	<b>2,391,723</b>	<b>42,578</b>	<b>46,793</b>	<b>52,946</b>	<b>2,534,040</b>
<b>Total gross recorded loans</b>	<b>3,753,571</b>	<b>150,489</b>	<b>80,145</b>	<b>65,252</b>	<b>4,049,457</b>

<sup>1</sup> Excludes purchased credit-impaired loans.

31 December 2014	Pass	Special mention	Substandard	Non-accrual <sup>1</sup>	Total gross recorded investments
<b>Commercial loans</b>					
Government	98,484	15,000	-	-	113,484
Commercial and industrial	381,560	4,254	1,898	733	388,445
Commercial overdrafts	55,439	3,452	304	106	59,301
<b>Total commercial loans</b>	<b>535,483</b>	<b>22,706</b>	<b>2,202</b>	<b>839</b>	<b>561,230</b>
<b>Commercial real estate loans</b>					
Commercial mortgage	544,832	91,500	48,373	12,273	696,978
Construction	20,617	-	-	-	20,617
<b>Total commercial real estate loans</b>	<b>565,449</b>	<b>91,500</b>	<b>48,373</b>	<b>12,273</b>	<b>717,595</b>
<b>Consumer loans</b>					
Automobile financing	19,615	564	-	176	20,355
Credit card	78,982	-	202	-	79,184
Overdrafts	20,933	167	-	43	21,143
Other consumer	153,226	1,917	714	1,763	157,620
<b>Total consumer loans</b>	<b>272,756</b>	<b>2,648</b>	<b>916</b>	<b>1,982</b>	<b>278,302</b>
<b>Residential mortgage loans</b>	<b>2,344,836</b>	<b>49,819</b>	<b>58,124</b>	<b>56,704</b>	<b>2,509,483</b>
<b>Total gross recorded loans</b>	<b>3,718,524</b>	<b>166,673</b>	<b>109,615</b>	<b>71,798</b>	<b>4,066,610</b>

<sup>1</sup> Excludes purchased credit-impaired loans.

### Quality classification definitions

A **pass loan** shall mean a loan that is expected to be repaid as agreed. A loan is classified as pass where the Bank is not expected to face repayment difficulties because the present and projected cash flows are sufficient to repay the debt and the repayment schedule as established by the agreement is being followed.

A **special mention** loan shall mean a loan under close monitoring by the Bank's management. Loans in this category are currently protected and still performing (current with respect to interest and principal payments), but are potentially weak and present an undue credit risk exposure, but not to the point of justifying a classification of substandard.

A **substandard** loan shall mean a loan whose evident unreliability makes repayment doubtful and there is a threat of loss to the Bank unless the unreliability is averted.

A **non-accrual** loan shall mean either management is of the opinion full payment of principal or interest is in doubt or when principal or interest is 90 days past due and for residential mortgage loans which are not well secured and in the process of collection.

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**  
(In thousands of Bermuda dollars, unless otherwise stated)

**Non-Performing Loans**

	31 December 2015			31 December 2014		
	Non-accrual <sup>1</sup>	Past due more than 90 days and accruing <sup>1</sup>	Total non-performing loans	Non-accrual <sup>1</sup>	Past due more than 90 days and accruing <sup>1</sup>	Total non-performing loans
<b>Commercial loans</b>						
Commercial and industrial	617	-	617	733	1,057	1,790
Commercial overdrafts	26	10	36	106	4	110
<b>Total commercial loans</b>	<b>643</b>	<b>10</b>	<b>653</b>	<b>839</b>	<b>1,061</b>	<b>1,900</b>
<b>Commercial real estate loans</b>						
Commercial mortgage	10,260	737	10,997	12,273	779	13,052
<b>Consumer loans</b>						
Automobile financing	98	-	98	176	-	176
Credit card	-	132	132	-	202	202
Overdrafts	11	527	538	43	-	43
Other consumer	1,294	85	1,379	1,763	255	2,018
<b>Total consumer loans</b>	<b>1,403</b>	<b>744</b>	<b>2,147</b>	<b>1,982</b>	<b>457</b>	<b>2,439</b>
<b>Residential mortgage loans</b>	<b>52,946</b>	<b>12,760</b>	<b>65,706</b>	<b>56,704</b>	<b>23,443</b>	<b>80,147</b>
<b>Total non-performing loans</b>	<b>65,252</b>	<b>14,251</b>	<b>79,503</b>	<b>71,798</b>	<b>25,740</b>	<b>97,538</b>

<sup>1</sup> Excludes purchased credit-impaired loans.

**Gross Loans Evaluated For Impairment**

	31 December 2015		31 December 2014	
	Individually evaluated	Collectively evaluated	Individually evaluated	Collectively evaluated
Commercial	13,607	595,013	839	560,391
Commercial real estate	38,019	640,957	33,898	683,697
Consumer	1,882	225,939	2,068	276,234
Residential mortgage	116,176	2,417,864	105,777	2,403,706
<b>Total gross loans evaluated for impairment</b>	<b>169,684</b>	<b>3,879,773</b>	<b>142,582</b>	<b>3,924,028</b>

**Changes in General and Specific Allowances For Credit Losses**

	Year ended 31 December 2015				
	Commercial	Commercial real estate	Consumer	Residential mortgage	Total
Allowances at beginning of year	7,831	5,920	2,797	30,934	47,482
Provision taken (released)	440	1,027	586	3,688	5,741
Recoveries	788	182	1,455	427	2,852
Charge-offs	(318)	(513)	(2,031)	(3,701)	(6,563)
Other	(18)	(104)	(44)	(44)	(210)
<b>Allowances at end of year</b>	<b>8,723</b>	<b>6,512</b>	<b>2,763</b>	<b>31,304</b>	<b>49,302</b>
Allowances at end of year: individually evaluated for impairment	590	2,951	274	15,290	19,105
Allowances at end of year: collectively evaluated for impairment	8,133	3,561	2,489	16,014	30,197

	Year ended 31 December 2014				
	Commercial	Commercial real estate	Consumer	Residential mortgage	Total
Allowances at beginning of year	8,340	9,816	3,442	31,157	52,755
Provision taken (released)	282	2,789	(686)	5,663	8,048
Recoveries	67	-	1,983	274	2,324
Charge-offs	(838)	(6,621)	(1,895)	(6,113)	(15,467)
Other	(20)	(64)	(47)	(47)	(178)
<b>Allowances at end of year</b>	<b>7,831</b>	<b>5,920</b>	<b>2,797</b>	<b>30,934</b>	<b>47,482</b>
Allowances at end of year: individually evaluated for impairment	417	1,822	355	16,217	18,811
Allowances at end of year: collectively evaluated for impairment	7,414	4,098	2,442	14,717	28,671



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Impaired Loans

A loan is considered to be impaired when, based on current information and events, the Bank determines that it will not be able to collect all amounts due according to the original loan contract, including scheduled interest payments. Impaired loans include all non-accrual loans and all loans modified in a troubled debt restructuring ("TDR") even if full collectability is expected following the restructuring. During the year ended 31 December 2015, the amount of gross interest income that would have been recorded had impaired loans been current was \$3.1 million (31 December 2014: \$5.2 million). The tables below present information about the Bank's impaired loans:

	Impaired loans with an allowance			Gross recorded investment of impaired loans without an allowance	Total impaired loans <sup>1</sup>		
	Gross recorded investment	Specific allowance	Net loans		Gross recorded investment	Specific allowance	Net loans
<b>31 December 2015</b>							
<b>Commercial loans</b>							
Commercial and industrial	599	(590)	9	1,096	1,695	(590)	1,105
Commercial overdrafts	-	-	-	26	26	-	26
<b>Total commercial loans</b>	<b>599</b>	<b>(590)</b>	<b>9</b>	<b>1,122</b>	<b>1,721</b>	<b>(590)</b>	<b>1,131</b>
<b>Commercial real estate loans</b>							
Commercial mortgage	6,127	(2,951)	3,176	17,198	23,325	(2,951)	20,374
<b>Consumer loans</b>							
Automobile financing	-	-	-	98	98	-	98
Overdrafts	-	-	-	11	11	-	11
Other consumer	366	(274)	92	1,008	1,374	(274)	1,100
<b>Total consumer loans</b>	<b>366</b>	<b>(274)</b>	<b>92</b>	<b>1,117</b>	<b>1,483</b>	<b>(274)</b>	<b>1,209</b>
<b>Residential mortgage loans</b>	<b>42,145</b>	<b>(15,290)</b>	<b>26,855</b>	<b>39,283</b>	<b>81,428</b>	<b>(15,290)</b>	<b>66,138</b>
<b>Total impaired loans</b>	<b>49,237</b>	<b>(19,105)</b>	<b>30,132</b>	<b>58,720</b>	<b>107,957</b>	<b>(19,105)</b>	<b>88,852</b>

<sup>1</sup> Excludes purchased credit-impaired loans.

	Impaired loans with an allowance			Gross recorded investment of impaired loans without an allowance	Total impaired loans <sup>1</sup>		
	Gross recorded investment	Specific allowance	Net loans		Gross recorded investment	Specific allowance	Net loans
<b>31 December 2014</b>							
<b>Commercial loans</b>							
Commercial and industrial	575	(417)	158	158	733	(417)	316
Commercial overdrafts	-	-	-	106	106	-	106
<b>Total commercial loans</b>	<b>575</b>	<b>(417)</b>	<b>158</b>	<b>264</b>	<b>839</b>	<b>(417)</b>	<b>422</b>
<b>Commercial real estate loans</b>							
Commercial mortgage	5,854	(1,822)	4,032	28,044	33,898	(1,822)	32,076
<b>Consumer loans</b>							
Automobile financing	-	-	-	176	176	-	176
Overdrafts	-	-	-	43	43	-	43
Other consumer	515	(355)	160	1,344	1,859	(355)	1,504
<b>Total consumer loans</b>	<b>515</b>	<b>(355)</b>	<b>160</b>	<b>1,563</b>	<b>2,078</b>	<b>(355)</b>	<b>1,723</b>
<b>Residential mortgage loans</b>	<b>45,673</b>	<b>(16,217)</b>	<b>29,456</b>	<b>29,764</b>	<b>75,437</b>	<b>(16,217)</b>	<b>59,220</b>
<b>Total impaired loans</b>	<b>52,617</b>	<b>(18,811)</b>	<b>33,806</b>	<b>59,635</b>	<b>112,252</b>	<b>(18,811)</b>	<b>93,441</b>

<sup>1</sup> Excludes purchased credit-impaired loans.

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**

(In thousands of Bermuda dollars, unless otherwise stated)

**Average Impaired Loan Balances and Related Recognised Interest Income**

	31 December 2015		31 December 2014	
	Average gross recorded investment	Interest income recognised <sup>1</sup>	Average gross recorded investment	Interest income recognised <sup>1</sup>
<b>Commercial loans</b>				
Commercial and industrial	1,214	-	1,452	-
Commercial overdrafts	66	-	289	-
<b>Total commercial loans</b>	<b>1,280</b>	<b>-</b>	<b>1,741</b>	<b>-</b>
<b>Commercial real estate loans</b>				
Commercial mortgage	28,612	311	48,581	675
<b>Consumer loans</b>				
Automobile financing	137	-	307	-
Credit card	-	-	35	-
Overdrafts	27	-	132	-
Other consumer	1,617	2	1,963	5
<b>Total consumer loans</b>	<b>1,781</b>	<b>2</b>	<b>2,437</b>	<b>5</b>
<b>Residential mortgage loans</b>	<b>78,433</b>	<b>1,442</b>	<b>70,923</b>	<b>1,021</b>
<b>Total impaired loans</b>	<b>110,106</b>	<b>1,755</b>	<b>123,682</b>	<b>1,701</b>

<sup>1</sup> All interest income recognised on impaired loans relate to loans previously modified in a TDR.

**Loans Modified in a TDR**

	TDRs entered into during the year ended 31 December 2015						
	Number of contracts	Pre- modification recorded investment	Effects of modifications		Post- modification recorded investment	TDRs outstanding as at 31 December 2015	
			Amount of repayments	Interest capitalisation		Accrual	Non-accrual
Commercial loans	1	1,000	-	87	1,087	1,078	-
Commercial real estate loans	-	-	-	-	-	13,065	1,608
Consumer loans	-	-	-	-	-	80	-
Residential mortgage loans	20	13,283	-	1,081	14,364	28,482	7,175
<b>Total loans modified in a TDR</b>	<b>21</b>	<b>14,283</b>	<b>-</b>	<b>1,168</b>	<b>15,451</b>	<b>42,705</b>	<b>8,783</b>

	TDRs entered into during the year ended 31 December 2014					TDRs outstanding as at 31 December 2014	
	Number of contracts	Pre- modification recorded investment	Effects of modifications		Post- modification recorded investment		
			Amount of repayments	Interest capitalisation		Accrual	Non-accrual
Commercial real estate loans	-	-	-	-	-	21,625	4,297
Consumer loans	-	-	-	-	-	96	-
Residential mortgage loans	20	13,857	-	259	14,116	18,733	4,613
Total loans modified in a TDR	20	13,857	-	259	14,116	40,454	8,910

As at 31 December 2015, the Bank has one loan (31 December 2014: four loans) that was modified in a TDR during the preceding 12 months that subsequently defaulted (i.e. 90 days or more past due following a modification) with a recorded investment of \$0.8 million (31 December 2014: \$2.4 million).

**Purchased Credit-Impaired Loans**

	Year ended 31 December 2015				Year ended 31 December 2014			
	Contractual principal	Non-accretable difference	Carrying amount	Accretable yield <sup>1</sup>	Contractual principal	Non-accretable difference	Carrying amount	Accretable yield <sup>1</sup>
Balance at beginning of year	11,020	(3,804)	7,216	-	-	-	-	-
Purchases	-	-	-	-	11,001	(3,804)	7,197	-
Advances and increases in cash flows expected to be collected	150	631	150	(631)	19	-	19	-
Reductions resulting from repayments	(1,554)	107	(1,447)	107	-	-	-	-
Reductions resulting from charge-offs	(907)	818	(89)	-	-	-	-	-
Accretion	-	-	-	(107)	-	-	-	-
<b>Balance at end of year</b>	<b>8,709</b>	<b>(2,248)</b>	<b>5,830</b>	<b>(631)</b>	<b>11,020</b>	<b>(3,804)</b>	<b>7,216</b>	<b>-</b>

<sup>1</sup> The accretable yield represents the excess of a loan's cash flows expected to be collected over the loan's initial carrying amount.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 7: Credit risk concentrations

Concentrations of credit risk in the lending and off-balance sheet credit-related arrangements portfolios arise when a number of customers are engaged in similar business activities, are in the same geographic region, or when they have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic conditions. The Bank regularly monitors various segments of its credit risk portfolio to assess potential concentrations of risks and to obtain collateral when deemed necessary. In the Bank's commercial portfolio, risk concentrations are evaluated primarily by industry and by geographic region of loan origination. In the consumer portfolio, concentrations are evaluated primarily by products. Credit exposures include loans, guarantees and acceptances, letters of credit and commitments for undrawn lines of credit. Unconditionally cancellable credit cards and overdraft lines of credit are excluded from the tables below.

The following table summarises the credit exposure of the Bank by business sector. The on-balance sheet exposure amounts disclosed are net of specific allowances and the off-balance sheet exposure amounts disclosed are gross of collateral held.

Business sector	31 December 2015			31 December 2014		
	Loans	Off-balance sheet	Total credit exposure	Loans	Off-balance sheet	Total credit exposure
Banks and financial services	243,776	320,934	564,710	307,835	299,934	607,769
Commercial and merchandising	230,376	107,545	337,921	248,129	113,432	361,561
Governments	223,699	102,782	326,481	113,484	-	113,484
Individuals	2,532,209	95,956	2,628,165	2,483,275	75,224	2,558,499
Primary industry and manufacturing	36,299	978	37,277	70,298	570	70,868
Real estate	632,548	15,891	648,439	710,905	5,703	716,608
Hospitality industry	125,471	14,854	140,325	107,538	275	107,813
Transport and communication	5,974	-	5,974	6,335	-	6,335
Sub-total	4,030,352	658,940	4,689,292	4,047,799	495,138	4,542,937
General allowance	(30,197)	-	(30,197)	(28,671)	-	(28,671)
<b>Total</b>	<b>4,000,155</b>	<b>658,940</b>	<b>4,659,095</b>	<b>4,019,128</b>	<b>495,138</b>	<b>4,514,266</b>

The following table summarises the credit exposure of the Bank by geographic region for cash due from banks, short-term investments, loans receivable and off-balance sheet exposure. The credit exposure by currency for investments is disclosed in Note 5: Investments.

Geographic region	31 December 2015				31 December 2014			
	Cash and cash equivalents and short-term investments	Loans	Off-balance sheet	Total credit exposure	Cash and cash equivalents and short-term investments	Loans	Off-balance sheet	Total credit exposure
Australia	14,187	-	-	14,187	7,521	-	-	7,521
Barbados	-	11,250	-	11,250	-	15,000	-	15,000
Belgium	3,352	-	-	3,352	-	-	-	-
Bermuda	22,009	2,269,635	371,687	2,663,331	18,486	2,269,748	263,407	2,551,641
Canada	340,037	-	-	340,037	16,648	-	-	16,648
Cayman	19,086	713,468	207,139	939,693	196,746	692,496	145,796	1,035,038
Guernsey	1	434,531	53,750	488,282	1,741	527,560	70,976	600,277
Japan	23,424	-	-	23,424	32,464	-	-	32,464
New Zealand	999	-	-	999	3,384	-	-	3,384
Saint Lucia	-	65,285	-	65,285	-	55,883	-	55,883
Sweden	3,659	-	-	3,659	2,419	-	-	2,419
Switzerland	3,905	-	-	3,905	7,954	-	-	7,954
The Bahamas	3,196	28,736	-	31,932	4,423	31,809	-	36,232
United Kingdom	1,103,088	507,447	26,364	1,636,899	1,300,686	455,303	14,959	1,770,948
United States	1,161,106	-	-	1,161,106	864,361	-	-	864,361
Other	323	-	-	323	1,248	-	-	1,248
Sub-total	2,698,372	4,030,352	658,940	7,387,664	2,458,081	4,047,799	495,138	7,001,018
General allowance	-	(30,197)	-	(30,197)	-	(28,671)	-	(28,671)
<b>Total</b>	<b>2,698,372</b>	<b>4,000,155</b>	<b>658,940</b>	<b>7,357,467</b>	<b>2,458,081</b>	<b>4,019,128</b>	<b>495,138</b>	<b>6,972,347</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 8: Premises, equipment and computer software

Category	31 December 2015			31 December 2014		
	Cost	Accumulated depreciation	Net carrying value	Cost	Accumulated depreciation	Net carrying value
Land	9,008	-	9,008	11,569	-	11,569
Buildings	135,684	(55,030)	80,654	147,421	(58,141)	89,280
Equipment	31,108	(27,620)	3,488	36,956	(32,678)	4,278
Computer hardware and software in use	174,162	(88,582)	85,580	166,896	(63,138)	103,758
Computer software in development	4,648	-	4,648	6,238	-	6,238
<b>Total</b>	<b>354,610</b>	<b>(171,232)</b>	<b>183,378</b>	<b>369,080</b>	<b>(153,957)</b>	<b>215,123</b>

	Year ended	
	31 December 2015	31 December 2014
<b>Depreciation charged to operating expenses</b>		
Buildings (included in Property expense)	4,183	4,434
Equipment (included in Property expense)	1,605	1,728
Computer hardware and software (included in Technology and communication expense)	19,076	18,588
<b>Total depreciation charged to operating expenses</b>	<b>24,864</b>	<b>24,750</b>
<b>Impairment of buildings' carrying value (included in Impairment of fixed assets)</b>	<b>-</b>	<b>1,986</b>

During the year ended 31 December 2014, the Bank's intended use of three Bermuda properties changed and therefore the properties were assessed for impairment. The carrying amounts of the Bermuda segment's buildings were impaired by \$1.2 million during 2014 because their respective fair values were lower than the carrying amounts.

At the end of 2014, the Bank changed its commitment with respect to a Bermuda property which was being used in its operations but is now contemplated for disposal and therefore the property has been reclassified as held for sale and included in OREO assets in the consolidated balance sheet. The reclassification resulted in an \$0.8 million write down during 2014 of the carrying amount to its fair value less cost to sell. The fair value was based on the discounted cash flow of a projected sale.

During the year ended 31 December 2015, the Bank sold four Bermuda properties and one Cayman property which were classified as premises, equipment and computer software as at 31 December 2014. The properties were sold for total proceeds of \$11.2 million and a gain of \$0.5 million, which is recognized on the consolidated statements of operations under net realised / unrealised gains (losses) on other real estate owned. For the Cayman property, the Bank has entered into a leaseback agreement for two floors with lease payments of \$0.4 million per year for three years.

During the year ended 31 December 2015, the Bank recognized impairment of \$5.1 million regarding the core banking system in the UK as described in Note 13: Exit cost obligations.

### Note 9: Goodwill and other intangible assets

#### Goodwill

Guernsey segment	Year ended	
	31 December 2015	31 December 2014
Balance at beginning of year	24,821	7,086
Acquisitions during the year (see Note 26)	-	19,291
Foreign exchange translation adjustment	(1,359)	(1,556)
<b>Balance at end of year</b>	<b>23,462</b>	<b>24,821</b>

#### Customer Relationship Intangible Assets

Business segment	31 December 2015			31 December 2014		
	Cost	Accumulated amortisation	Net carrying amount	Cost	Accumulated amortisation	Net carrying amount
Bermuda	8,342	(6,258)	2,084	8,342	(5,702)	2,640
Cayman	12,324	(1,960)	10,364	12,324	(1,138)	11,186
Guernsey	58,420	(43,199)	15,221	58,420	(39,205)	19,215
<b>Total</b>	<b>79,086</b>	<b>(51,417)</b>	<b>27,669</b>	<b>79,086</b>	<b>(46,045)</b>	<b>33,041</b>

Customer relationships are initially valued based on the present value of net cash flows expected to be derived solely from the recurring customer base existing as at the date of acquisition. Customer relationship intangible assets may or may not arise from contracts. See Note 26: Business Combinations for details of acquisitions of customer relationship intangible assets that occurred during the year ended 31 December 2014.

During the year ended 31 December 2015, the Bank did not acquire any new customer intangible assets (31 December 2014: \$26.6 million), the amortisation expense amounted to \$4.4 million (31 December 2014: \$4.3 million) and the foreign exchange translation adjustment decreased the net carrying amount by \$0.9 million (31 December 2014: decreased by \$1.3 million). The estimated aggregate amortisation expense for each of the succeeding five years is \$4.4 million.

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**

(In thousands of Bermuda dollars, unless otherwise stated)

**Note 10: Customer deposits and deposits from banks**

**By Maturity**

	31 December 2015			31 December 2014		
	Customers	Banks	Total	Customers	Banks	Total
<b>Demand deposits</b>						
Demand deposits - Non-interest bearing	1,881,745	403	1,882,148	1,558,122	408	1,558,530
Demand deposits - Interest bearing	5,772,898	10,176	5,783,074	5,179,522	26,512	5,206,034
<b>Total demand deposits</b>	<b>7,654,643</b>	<b>10,579</b>	<b>7,665,222</b>	<b>6,737,644</b>	<b>26,920</b>	<b>6,764,564</b>
<b>Term deposits having a denomination of less than \$100 thousand</b>						
Term deposits maturing within six months	50,251	202	50,453	57,451	82	57,533
Term deposits maturing between six to twelve months	14,273	-	14,273	18,310	-	18,310
Term deposits maturing after twelve months	16,257	-	16,257	18,492	-	18,492
<b>Total term deposits having a denomination of less than \$100 thousand</b>	<b>80,781</b>	<b>202</b>	<b>80,983</b>	<b>94,253</b>	<b>82</b>	<b>94,335</b>
<b>Term deposits having a denomination of \$100 thousand or more</b>						
Term deposits maturing within six months <sup>1</sup>	1,230,789	3,697	1,234,486	1,445,072	9,368	1,454,440
Term deposits maturing between six to twelve months	138,973	-	138,973	294,175	3,536	297,711
Term deposits maturing after twelve months	62,482	-	62,482	60,527	-	60,527
<b>Total term deposits having a denomination of \$100 thousand or more</b>	<b>1,432,244</b>	<b>3,697</b>	<b>1,435,941</b>	<b>1,799,774</b>	<b>12,904</b>	<b>1,812,678</b>
<b>Total term deposits</b>	<b>1,513,025</b>	<b>3,899</b>	<b>1,516,924</b>	<b>1,894,027</b>	<b>12,986</b>	<b>1,907,013</b>
<b>Total deposits</b>	<b>9,167,668</b>	<b>14,478</b>	<b>9,182,146</b>	<b>8,631,671</b>	<b>39,906</b>	<b>8,671,577</b>

<sup>1</sup> As at 31 December 2015, \$192 million (2014: \$nil) of the term deposits having a denomination of \$100 thousand or more, bear a special interest rate of 0%.

The weighted-average interest rate on interest-bearing demand deposits as at 31 December 2015 is 0.10% (31 December 2014: 0.16%).

**By Type and Segment**

	31 December 2015			31 December 2014		
	Payable on demand	Payable on a fixed date	Total	Payable on demand	Payable on a fixed date	Total
<b>Bermuda</b>						
Customers	3,739,829	531,877	4,271,706	2,914,440	955,683	3,870,123
Banks	403	-	403	9,508	-	9,508
<b>Cayman</b>						
Customers	2,596,642	416,489	3,013,131	2,153,500	437,259	2,590,759
Banks	9,365	3,899	13,264	15,797	12,986	28,783
<b>Guernsey</b>						
Customers	996,343	248,866	1,245,209	1,350,377	145,132	1,495,509
Banks	669	-	669	1,307	-	1,307
<b>The Bahamas</b>						
Customers	36,078	3,602	39,680	53,317	7,514	60,831
<b>United Kingdom</b>						
Customers	285,751	312,191	597,942	266,010	348,439	614,449
Banks	142	-	142	308	-	308
<b>Total Customers</b>	<b>7,654,643</b>	<b>1,513,025</b>	<b>9,167,668</b>	<b>6,737,644</b>	<b>1,894,027</b>	<b>8,631,671</b>
<b>Total Banks</b>	<b>10,579</b>	<b>3,899</b>	<b>14,478</b>	<b>26,920</b>	<b>12,986</b>	<b>39,906</b>
<b>Total deposits</b>	<b>7,665,222</b>	<b>1,516,924</b>	<b>9,182,146</b>	<b>6,764,564</b>	<b>1,907,013</b>	<b>8,671,577</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 11: Employee benefit plans

The Bank maintains trustee pension plans including non-contributory defined benefit plans and a number of defined contribution plans, and provides post-retirement medical benefits to its qualifying retirees. The defined benefit provisions under the pension plans are generally based upon years of service and average salary during the relevant years of employment. The defined benefit and post-retirement medical plans are not open to new participants and are non-contributory and the funding required is provided by the Bank, based upon the advice of independent actuaries.

#### Bermuda Defined Benefit Post Retirement Healthcare Plan

For the year ended 31 December 2014 numerous changes in the plan provisions were made to align the plan provisions with the administrative practices of the Bank resulting in a further increase in the Bermuda defined benefit post-retirement healthcare plan liability of \$7.9 million.

The Bank amortises prior service credit resulting from plan amendments that occurred when plan members were active employees, on a linear basis over the expected average remaining service period (to full eligibility) of active members expected to receive benefits under the plan. Such remaining service periods are as follow: 3.1 years for the 2010 plan amendments and 4.6 years for the 2011 plan amendments. Plan amendments occurring in 2014 resulted in the recognition of new prior service cost on 31 December 2014 on a plan for which substantially all members are now inactive and, in accordance with US GAAP, the Bank has elected to amortise this new prior service cost on a linear basis over 21 years, which is the average remaining life expectancy of members eligible for benefits under the plan at the time of the amendments.

#### Guernsey Defined Benefit Pension Plan

Effective 30 September 2014, the defined benefit pension benefits of the Bank's Guernsey operations were amended to freeze credited service and final average earnings for remaining active members. The benefits amendment resulted in a further reduction in the Guernsey defined benefit pension liability of \$4.59 million as at 30 September 2014.

Effective October 2014, all the participants of the Guernsey defined benefit pension plan are inactive and in accordance with US GAAP, the net actuarial loss of the Guernsey defined benefit pension plan will be amortised over the then estimated average remaining life expectancy of the inactive participants of 39 years. Prior to all of the Guernsey participants being inactive, the net actuarial loss of the Guernsey defined benefit pension plan was amortised to net income over the estimated average remaining service period for active members of 15 years.

The following table presents the financial position of the Bank's defined benefit pension plans and the Bank's post-retirement medical benefits, which is unfunded. The Bank measures the benefit obligations and plan assets annually on each 31 December and therefore, the most recent measurement date is 31 December 2015.

	31 December 2015		31 December 2014	
	Pension plans	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
<b>Accumulated benefit obligation at end of year</b>	<b>166,815</b>	<b>-</b>	<b>188,890</b>	<b>-</b>
<b>Change in projected benefit obligation</b>				
Projected benefit obligation at beginning of year	188,890	114,640	167,469	89,109
Service cost	-	341	1,203	825
Employee contributions	-	-	99	-
Interest cost	6,958	4,745	7,760	4,503
Benefits paid	(7,573)	(2,871)	(8,771)	(3,590)
Plan amendment	-	-	-	7,901
Settlement and curtailment of liability	(2,509)	-	(4,662)	-
Actuarial (gain) loss	(14,157)	2,252	31,604	15,892
Foreign exchange translation adjustment	(4,794)	-	(5,812)	-
<b>Projected benefit obligation at end of year</b>	<b>166,815</b>	<b>119,107</b>	<b>188,890</b>	<b>114,640</b>
<b>Change in plan assets</b>				
Fair value of plan assets at beginning of year	194,007	-	186,412	-
Actual return on plan assets	687	-	18,451	-
Employer contribution	808	2,871	4,172	3,590
Employee contributions	-	-	99	-
Plan settlement	(2,424)	-	-	-
Benefits paid	(7,573)	(2,871)	(8,771)	(3,590)
Foreign exchange translation adjustment	(5,544)	-	(6,356)	-
<b>Fair value of plan assets at end of year</b>	<b>179,961</b>	<b>-</b>	<b>194,007</b>	<b>-</b>
<b>Amounts recognised in the consolidated balance sheets consist of:</b>				
Prepaid benefit cost included in other assets	16,174	-	8,374	-
Accrued pension benefit cost included in employee benefit plans liability	(3,028)	(119,107)	(3,257)	(114,640)
<b>Surplus (deficit) of plan assets over projected benefit obligation at measurement date</b>	<b>13,146</b>	<b>(119,107)</b>	<b>5,117</b>	<b>(114,640)</b>



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

As at 31 December 2015, the pension plans of the Guernsey and United Kingdom subsidiaries were in a surplus position (i.e. net surplus presented in other assets in the consolidated balance sheets) while the pension plan of the Bermuda operations was in a deficit position with projected benefit obligations of \$88.0 million and plan assets of \$85.0 million.

	Year ended		31 December 2014	
	31 December 2015	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
<b>Amounts recognised in accumulated other comprehensive loss consist of:</b>				
Net actuarial loss, excluding deferred taxes	(46,696)	(28,779)	(53,970)	(29,874)
Prior service credit, net of prior service cost	-	665	-	7,008
Deferred income taxes assets	365	-	801	-
<b>Net amount recognised in accumulated other comprehensive loss</b>	<b>(46,331)</b>	<b>(28,114)</b>	<b>(53,169)</b>	<b>(22,866)</b>

### Annual Benefit Expense

Expense component	31 December 2015	Post-retirement medical benefit plan	31 December 2014	Post-retirement medical benefit plan
Service cost	-	341	1,203	825
Interest cost	6,958	4,745	7,760	4,503
Expected return on plan assets	(9,585)	-	(10,653)	-
Amortisation of prior service credit	-	(6,343)	-	(6,719)
Amortisation of net actuarial losses	1,607	3,347	1,058	922
Loss on settlement	101	-	-	-
Defined benefit expense (income)	(919)	2,090	(632)	(469)
Defined contribution expense	6,907	-	6,892	-
<b>Total benefit expense (income)</b>	<b>5,988</b>	<b>2,090</b>	<b>6,260</b>	<b>(469)</b>

### Other Changes Recognised in Other Comprehensive (Loss) Income

Net gain (loss) arising during the year	5,096	(2,252)	(18,947)	(15,892)
Prior service cost arising during the year	-	-	-	(7,901)
Amortisation of prior service credit	-	(6,343)	-	(6,719)
Amortisation of net actuarial losses	1,703	3,347	1,058	922
Change in deferred taxes	(391)	-	83	-
Foreign exchange adjustment	430	-	253	-
<b>Total changes recognised in other comprehensive (loss) income</b>	<b>6,838</b>	<b>(5,248)</b>	<b>(17,553)</b>	<b>(29,590)</b>

The estimated portion of the net actuarial loss for the pension plans that will be amortised from AOCL into benefit expense over the 2016 full fiscal year is \$1.7 million. The estimated portion of the net actuarial loss and the prior service credit for the post-retirement medical benefit plan that will be amortised from AOCL into benefit expense over the 2016 full fiscal year is \$2.6 million for the net actuarial loss and a credit of \$6.3 million for the net prior service credit.

### Actuarial Assumptions

	Year ended		31 December 2014	
	31 December 2015	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
<b>Actuarial assumptions used to determine annual benefit expense</b>				
Weighted average discount rate	3.80%	4.20%	4.75%	5.10%
Weighted average rate of compensation increases <sup>1</sup>	2.20%	N/A	4.30%	N/A
Weighted average expected long-term rate of return on plan assets	5.10%	N/A	5.80%	N/A
Weighted average annual medical cost increase rate (sensitivity shown below)	N/A	7.1% to 4.5% in 2027	N/A	7.3% to 4.5% in 2027

<sup>1</sup> Excludes the inactive Bermuda defined benefit pension plan.

### Actuarial assumptions used to determine benefit obligations at end of year

Weighted average discount rate	4.20%	4.70%	3.80%	4.20%
Weighted average rate of compensation increases	2.30%	N/A	2.80%	N/A
Weighted average annual medical cost increase rate (sensitivity shown below)	N/A	8.0% to 4.5% in 2035	N/A	7.1% to 4.5% in 2027

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Post-retirement medical benefit plan sensitivity to trend rate assumptions

The effect of a one percentage point increase or decrease in the assumed medical cost increase rate on the aggregate of service and interest costs is as follow:

a. One percent increase in trend rate				
i. Effect on total service cost and interest cost components for the year	N/A	909	N/A	952
ii. Effect on benefit obligation at year-end	N/A	18,792	N/A	20,339
a. One percent increase in trend rate				
i. Effect on total service cost and interest cost components for the year	N/A	(781)	N/A	(771)
ii. Effect on benefit obligation at year-end	N/A	(15,496)	N/A	(16,514)

To develop the expected long-term rate of return on the plan assets assumption for each plan, the Bank considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocations of the assets. The weighted average discount rate used to determine benefit obligations at the end of the year is derived from interest rates on high quality corporate bonds with maturities that match the expected benefit payments.

### Investments Policies and Strategies

The pension plans' assets are managed according to each plan's investment policy statement, which outlines the purpose of the plan, statement of objectives and guidelines and investment policy. The asset allocation is diversified and any use of derivatives is limited to hedging purposes only.

	31 December 2015		31 December 2014	
	Actual allocation	Target allocation	Actual allocation	Target allocation
<b>Weighted average actual and target asset allocations of the pension plans by asset category</b>				
Debt securities (including debt mutual funds)	42%	53%	49%	50%
Equity securities (including equity mutual funds)	58%	47%	45%	48%
Other	0%	0%	6%	2%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

### Fair Value Measurements of Pension Plans' Assets

The following table presents the fair value of plans' assets by category and level of inputs used in their respective fair value determination as described in Note 2:

	31 December 2015				31 December 2014			
	Fair value determination				Fair value determination			
	Level 1	Level 2	Level 3	Total fair value	Level 1	Level 2	Level 3	Total fair value
US government and federal agencies	-	7,532	-	7,532	-	7,707	-	7,707
Corporate debt securities	-	68,166	-	68,166	-	62,466	-	62,466
Debt securities issued by non-US governments	-	-	-	-	-	17,342	-	17,342
Equity securities and mutual funds	11,845	91,702	-	103,547	12,747	92,962	-	105,709
Other	-	716	-	716	-	783	-	783
<b>Total fair value of plans' assets</b>	<b>11,845</b>	<b>168,116</b>	<b>-</b>	<b>179,961</b>	<b>12,747</b>	<b>181,260</b>	<b>-</b>	<b>194,007</b>

At 31 December 2015, 34.8% (31 December 2014: 35.9 %) of the assets of the pension plans were mutual funds and equity securities managed or administered by wholly-owned subsidiaries of the Bank. At 31 December 2015, 0.3% and 1.2% (31 December 2014: 0.3% and 1.1%) of the plans' assets were invested in common and preference shares of the Bank respectively.

The investments of the pension funds are diversified across a range of asset classes and are diversified within each asset class. The assets are generally actively managed with the goal of adding some incremental value through security selection and asset allocation.

Estimated 2016 Bank contribution to and estimated benefit payments for the next ten years under the pension and post-retirement medical benefit plans are as follows:

	Pension plans	Post-retirement medical benefit plan
<b>Estimated Bank contributions for the full year ending 31 December 2016</b>	<b>592</b>	<b>4,183</b>
<b>Estimated benefit payments by year:</b>		
2016	7,400	4,183
2017	7,400	4,496
2018	7,400	4,822
2019	7,400	5,167
2020	7,400	5,511
2021-2024	37,000	32,986

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 12: Credit related arrangements and commitments

#### Commitments

As at 31 December 2015, the Bank was committed to expenditures under contract for sourcing and leases of \$16.3 million and \$20.0 million respectively (31 December 2014: \$33.1 million and \$20.0 million respectively). Rental expense for premises leased on a long-term basis for the year ended 31 December 2015 amounted to \$4.8 million (31 December 2014: \$5.3 million).

The following table summarises the Bank's commitments for sourcing, long-term leases and other agreements:

Year ending 31 December	Sourcing	Leases	Other	Total
2016	16,312	5,235	2,376	23,923
2017	-	4,212	536	4,748
2018	-	3,346	497	3,843
2019	-	2,523	458	2,981
2020	-	2,382	458	2,840
2021 & thereafter	-	2,294	458	2,752
<b>Total commitments</b>	<b>16,312</b>	<b>19,992</b>	<b>4,783</b>	<b>41,087</b>

#### Credit-Related Arrangements

Standby letters of credit and letters of guarantee are issued at the request of a Bank customer in order to secure the customer's payment or performance obligations to a third party. These guarantees represent an irrevocable obligation of the Bank to pay the third party beneficiary upon presentation of the guarantee and satisfaction of the documentary requirements stipulated therein, without investigation as to the validity of the beneficiary's claim against the customer. Generally, the term of the standby letters of credit does not exceed one year, whilst the term of the letters of guarantee does not exceed four years. The types and amounts of collateral security held by the Bank for these standby letters of credit and letters of guarantee is generally represented by deposits with the Bank or a charge over assets held in mutual funds.

The Bank considers the fees collected in connection with the issuance of standby letters of credit and letters of guarantee to be representative of the fair value of its obligation undertaken in issuing the guarantee. In accordance with applicable accounting standards related to guarantees, the Bank defers fees collected in connection with the issuance of standby letters of credit and letters of guarantee. The fees are then recognised in income proportionately over the life of the credit agreements.

The following table presents the outstanding financial guarantees:

	31 December 2015			31 December 2014		
	Gross	Collateral	Net	Gross	Collateral	Net
Standby letters of credit	258,851	257,200	1,651	225,718	224,158	1,560
Letters of guarantee	9,137	8,418	719	10,227	7,594	2,633
<b>Total</b>	<b>267,988</b>	<b>265,618</b>	<b>2,370</b>	<b>235,945</b>	<b>231,752</b>	<b>4,193</b>

Collateral is shown at estimated market value less selling cost. Where cash is the collateral, this is shown gross including interest income.

The Bank enters into contractual commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. Substantially all of the Bank's commitments to extend credit are contingent upon customers maintaining specific credit standards at the time of loan funding. Management assesses the credit risk associated with certain commitments to extend credit in determining the level of the allowance for possible loan losses.

The following table presents the unfunded legally binding commitments to extend credit:

	31 December 2015	31 December 2014
Commitments to extend credit	390,497	257,266
Documentary and commercial letters of credit	455	1,927
<b>Total unfunded commitments to extend credit</b>	<b>390,952</b>	<b>259,193</b>

The Bank has a facility by one of its custodians, whereby the Bank may offer up to US\$200 million of standby letters of credit to its customers on a fully secured basis. Under the standard terms of the facility, the custodian has the right to set-off against securities held of 110% of the utilised facility. At 31 December 2015, \$123.7 million (31 December 2014: \$91.8 million) of standby letters of credit were issued under this facility.

#### Legal Proceedings

There are actions and legal proceedings pending against the Bank and its subsidiaries which arose in the normal course of its business. Management, after reviewing all actions and proceedings pending against or involving the Bank and its subsidiaries, considers that the resolution of these matters would in the aggregate not be material to the consolidated financial position of the Bank, except as noted in the following paragraphs.

As publicly announced, in November 2013, the US Attorney's Office for the Southern District of New York applied for and secured the issuance of so-called John Doe Summonses to six US financial institutions with which the Bank had correspondent bank relationships. The Bank has been fully cooperating with the US authorities in their ongoing investigation. Specifically, the Bank has conducted an extensive review and account remediation exercise to determine the US tax compliance status of US person account holders. The review process and results have been shared with the US authorities.

Management believes that, at this stage, a provision of \$4.8 million, which has been recorded as of 31 December 2015, is appropriate based on the methodology used in similar settlements for other financial institutions. As the investigation remains ongoing at this time, the timing and terms of the final resolution, including any fines or penalties, remain uncertain and the financial impact to the Bank could exceed the amount of the provision. In this regard, we note that the US authorities have not approved or commented on the adequacy or reasonableness of the estimate. The provision is included on the consolidated balance sheets under other liabilities and on the consolidated statements of operations under other expenses.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Pending business acquisition

In November 2015, the Bank announced that it had reached an agreement to acquire Bermuda Trust Company Ltd. and the private banking investment management operations of HSBC Bank Bermuda Limited. HSBC Bank Bermuda Limited has also entered into an agreement to refer its existing private banking clients to the Bank. The transaction is expected to be completed in the first half of 2016.

### Note 13: Exit cost obligations

During December 2015, the Bank agreed to commence an orderly wind-down of the deposit taking and investment management businesses in the United Kingdom segment as reflected in management segment reporting described in Note 15: Segmented Information. In making this determination, the Bank considered the increasing regulatory pressure along with periods of negative profitability and made the determination that an orderly wind-down of the deposit taking and investment management businesses in the United Kingdom was prudent for Butterfield as a group. The orderly wind-down is expected to be completed over the next 12 months. Certain expenses and related liabilities have been recognized during and as of the year ended 31 December 2015 pertaining to this orderly wind-down plan. The tables below present information about these liabilities and expenses:

	Total costs expected to be incurred	Year ended 31 December 2015		Exit cost liability as at 31 December 2015
		Expense recognised	Amounts paid	
Staff redundancy expenses	3,955	634	-	634
Professional services	4,125	1,549	-	1,549
Lease termination expenses	2,210	-	-	-
Other expenses	1,620	-	-	-
<b>Total</b>	<b>11,910</b>	<b>2,183</b>	<b>-</b>	<b>2,183</b>

The amounts expensed above are all included in the consolidated statements of operations as "Restructuring costs" under non-interest expenses.

Related to this orderly wind-down, it was determined that the core banking system utilized in the operations of the United Kingdom segment was impaired (currently held under "Premises, equipment and computer software" on the consolidated balance sheets). This determination was based upon the realisable value of this software upon completion of the orderly wind-down. A total of \$5.1 million was incurred and expensed during the year ended 31 December 2015 and is included as "Impairment of fixed assets" on the consolidated statements of operations.

### Note 14: Loan interest income

	Year ended	
	31 December 2015	31 December 2014
<b>Contractual interest</b>		
Contractual interest earned on mortgages	104,194	106,321
Contractual interest earned on other loans	79,506	82,395
<b>Subtotal contractual interest earned</b>	<b>183,700</b>	<b>188,716</b>
<b>Amortisation</b>		
Amortisation of fair value hedge	(1,471)	(1,548)
Amortisation of loan origination fees (net of amortised costs)	4,257	4,818
<b>Total loan interest income</b>	<b>186,486</b>	<b>191,986</b>
<b>Balance of unamortised fair value hedge as at year end</b>	<b>(4,335)</b>	<b>(5,806)</b>
<b>Balance of unamortised loan fees as at year end</b>	<b>8,107</b>	<b>7,526</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 15: Segmented information

As at 31 December 2015, for Management reporting purposes, the operations of the Bank are grouped into the following six business segments based upon the geographic location of the Bank's operations: Bermuda, Cayman, Guernsey, Switzerland, The Bahamas and the United Kingdom. Accounting policies of the reportable segments are the same as those described in Note 2.

**Bermuda** provides a full range of retail, commercial and private banking services. Retail services are offered to individuals and small to medium-sized businesses through five branch locations and through Internet banking, mobile banking, automated teller machines ("ATMs") and debit cards. Retail services include deposit services, consumer and mortgage lending, credit cards and personal insurance products. Commercial banking includes commercial lending and mortgages, cash management, payroll services, remote banking and letters of credit. Treasury services include money market and foreign exchange activities. Bermuda's wealth management offering consists of Butterfield Asset Management Limited, which provides investment management, advisory and brokerage services and Butterfield Trust (Bermuda) Limited, which provides trust, estate, company management and custody services.

The **Cayman** segment provides a comprehensive range of retail, commercial and private banking services. Retail services are offered to individuals and small to medium-sized businesses through three branch locations and through Internet banking, mobile banking, ATMs and debit cards. Retail services include deposit services, consumer and mortgage lending, credit cards and property/auto insurance. Commercial banking includes commercial lending and mortgages, cash management, payroll services, remote banking and letters of credit. Treasury services include money market and foreign exchange activities. Cayman's wealth management offering comprises investment management, advisory and brokerage services and Butterfield Trust (Cayman) Limited, which provides trust, estate and company management.

The **Guernsey** segment provides a broad range of services to private clients and financial institutions including private banking and treasury services, Internet banking, administered bank services, wealth management and fiduciary services.

The **Switzerland** segment provides fiduciary services. The **Bahamas** segment provides fiduciary and ancillary services.

The **United Kingdom** segment provides a broad range of services including private banking and treasury services, Internet banking and wealth management and fiduciary services to high net worth individuals and privately owned businesses. As described in Note 13, during December 2015, the Bank agreed to commence an orderly wind-down plan of the deposit taking and investment management businesses in the United Kingdom segment.

	31 December 2015	31 December 2014
<b>Total Assets by Segment</b>		
Bermuda	5,113,718	4,797,235
Cayman	3,282,319	2,863,624
Guernsey	1,391,126	1,639,334
Switzerland	2,713	2,000
The Bahamas	49,434	70,265
United Kingdom	788,433	832,591
<b>Total assets before inter-segment eliminations</b>	<b>10,627,743</b>	<b>10,205,049</b>
Less: inter-segment eliminations	(352,180)	(346,609)
<b>Total</b>	<b>10,275,563</b>	<b>9,858,440</b>

Year ended	Net interest income		Provision for	Non-interest	Revenue	Total	Net income	Gains and	
31 December 2015	Customer	Inter- segment	credit losses	income	before gains and losses	expenses	before gains and losses	losses	Net income
Bermuda	142,488	2,600	(3,625)	61,050	202,513	159,474	43,039	(2,503)	40,536
Cayman	66,317	608	(466)	39,508	105,967	58,115	47,852	(793)	47,059
Guernsey	17,025	(427)	(103)	26,171	42,666	39,872	2,794	(1,066)	1,728
Switzerland	-	-	-	3,420	3,420	3,320	100	-	100
The Bahamas	8	116	-	5,295	5,419	5,068	351	1	352
United Kingdom	13,428	(2,897)	(1,547)	6,307	15,291	22,251	(6,960)	(5,076)	(12,036)
<b>Total before eliminations</b>	<b>239,266</b>	<b>-</b>	<b>(5,741)</b>	<b>141,751</b>	<b>375,276</b>	<b>288,100</b>	<b>87,176</b>	<b>(9,437)</b>	<b>77,739</b>
Inter-segment eliminations	-	-	-	(1,579)	(1,579)	(1,579)	-	-	-
<b>Total</b>	<b>239,266</b>	<b>-</b>	<b>(5,741)</b>	<b>140,172</b>	<b>373,697</b>	<b>286,521</b>	<b>87,176</b>	<b>(9,437)</b>	<b>77,739</b>

Year ended	Net interest income		Provision for	Non-interest	Revenue	Total	Net income	Gains and	
31 December 2014	Customer	Inter- segment	credit losses	income	before gains and losses	expenses	before gains and losses	losses	Net income
Bermuda	141,528	3,164	(6,425)	60,692	198,959	145,696	53,263	6,908	60,171
Cayman	58,442	928	(557)	33,515	92,328	58,829	33,499	36	33,535
Guernsey	19,303	(1,242)	(154)	26,814	44,721	39,580	5,141	4,432	9,573
Switzerland	-	-	-	2,486	2,486	2,867	(381)	-	(381)
The Bahamas	(15)	166	-	5,492	5,643	5,548	95	-	95
United Kingdom	19,229	(3,016)	(912)	7,717	23,018	22,164	854	4,312	5,166
<b>Total before eliminations</b>	<b>238,487</b>	<b>-</b>	<b>(8,048)</b>	<b>136,716</b>	<b>367,155</b>	<b>274,684</b>	<b>92,471</b>	<b>15,688</b>	<b>108,159</b>
Inter-segment eliminations	-	-	-	(1,886)	(1,886)	(1,886)	-	-	-
<b>Total</b>	<b>238,487</b>	<b>-</b>	<b>(8,048)</b>	<b>134,830</b>	<b>365,269</b>	<b>272,798</b>	<b>92,471</b>	<b>15,688</b>	<b>108,159</b>

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**  
*(In thousands of Bermuda dollars, unless otherwise stated)*

**Note 16: Derivative instruments and risk management**

The Bank uses derivatives for risk management purposes and to meet the needs of its customers. The Bank's derivative contracts principally involve over-the-counter ("OTC") transactions that are privately negotiated between the Bank and the counterparty to the contract and include interest rate contracts and foreign exchange contracts.

The Bank may pursue opportunities to reduce its exposure to credit losses on derivatives by entering into International Swaps and Derivatives Association master agreements ("ISDAs"). Depending on the nature of the derivative transaction, bilateral collateral arrangements may be used as well. When the Bank is engaged in more than one outstanding derivative transaction with the same counterparty, and also has a legally enforceable master netting agreement with that counterparty, the net marked to market exposure represents the netting of the positive and negative exposures with that counterparty. When there is a net negative exposure, the Bank regards its credit exposure to the counterparty as being zero. The net marked to market position with a particular counterparty represents a reasonable measure of credit risk when there is a legally enforceable master netting agreement between the Bank and that counterparty.

Certain of these agreements contain credit risk-related contingent features in which the counterparty has the option to accelerate cash settlement of the Bank's net derivative liabilities with the counterparty in the event the Bank's credit rating falls below specified levels or the liabilities reach certain levels.

All derivative financial instruments, whether designated as hedges or not, are recorded on the consolidated balance sheets at fair value within other assets or other liabilities. These amounts include the effect of netting. The accounting for changes in the fair value of a derivative in the consolidated statements of operations depends on whether the contract has been designated as a hedge and qualifies for hedge accounting.

**Notional Amounts**

The notional amounts are not recorded as assets or liabilities on the consolidated balance sheets as they represent the face amount of the contract to which a rate or price is applied to determine the amount of cash flows to be exchanged. Notional amounts represent the volume of outstanding transactions and do not represent the potential gain or loss associated with market risk or credit risk of such instruments. Credit risk is limited to the positive fair value of the derivative instrument, which is significantly less than the notional amount.

**Fair Value**

Derivative instruments, in the absence of any compensating up-front cash payments, generally have no market value at inception. They obtain value, positive or negative, as relevant interest rates, exchange rates, equity or commodity prices or indices change. The potential for derivatives to increase or decrease in value as a result of the foregoing factors is generally referred to as market risk. Market risk is managed within clearly defined parameters as prescribed by senior management of the Bank. The fair value is defined as the profit or loss associated with replacing the derivative contracts at prevailing market prices.

**Risk Management Derivatives**

The Bank enters into interest derivative contracts as part of its overall interest rate risk management strategy to minimise significant unplanned fluctuations in earnings that are caused by interest rate volatility. The Bank's goal is to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain consolidated balance sheet assets and liabilities so that movements in interest rates do not adversely affect the net interest margin. Derivative instruments that are used as part of the Bank's risk management strategy include interest rate swap contracts that have indices related to the pricing of specific consolidated balance sheet assets and liabilities. Interest rate swaps generally involve the exchange of fixed and variable-rate interest payments between two parties, based on a common notional principal amount and maturity date. The Bank uses foreign currency derivative instruments to hedge its exposure to foreign currency risk. Certain hedging relationships are formally designated and qualify for hedge accounting as fair value or net investment hedges. Risk management derivatives comprise the following:

**Fair value hedges**

Derivatives are designated as fair value hedges to minimise the Bank's exposure to changes in the fair value of assets and liabilities due to movements in interest rates. The Bank enters into interest rate swaps to convert its fixed-rate long-term loans to floating-rate loans, and convert fixed-rate deposits to floating-rate deposits. Changes in fair value of these derivatives are recognised in income. For fair value hedges, the Bank applies the "shortcut" method of accounting, which assumes there is no ineffectiveness in a hedge. As a result, changes recorded in the fair value of the hedged item are equal to the offsetting gain or loss on the derivative and are reflected in the same line item. During the year ended 31 December 2011, the Bank cancelled its interest rate swaps designated as fair value hedges of loans receivable and therefore discontinued hedge accounting for these financial instruments. The fair value attributable to the hedged loans are accounted for prospectively and are being amortised to net income over the remaining life of each individual loan using the effective interest method.

**Net investment hedges**

Foreign currency swaps and qualifying non-derivative instruments designated as net investment hedges are used to minimise the Bank's exposure to variability in the foreign currency translation of net investments in foreign operations. The effective portion of changes in the fair value of the hedging instrument is recognised in AOCL consistent with the related translation gains and losses of the hedged net investment. For net investment hedges, all critical terms of the hedged item and the hedging instrument are matched at inception and on an ongoing basis to minimise the risk of hedge ineffectiveness.

For derivatives designated as net investment hedges, the Bank follows the forward-rate method in measuring the amount of ineffectiveness in a net investment hedge. According to that method, all changes in fair value, including changes related to the forward-rate component and the time value of currency swaps, are recorded in the foreign currency translation adjustment account within AOCL. To the extent all terms are not perfectly matched, any ineffectiveness is measured using the hypothetical derivative method. Ineffectiveness resulting from net investment hedges is recorded in foreign exchange income. Amounts recorded in AOCL are reclassified to earnings only upon the sale or liquidation of an investment in a foreign subsidiary.

For foreign-currency-denominated debt instruments that are designated as hedges of net investments in foreign operations, the translation gain or loss that is recorded in AOCL is based on the spot exchange rate between the reporting currency of the Bank and the functional currency of the respective subsidiary.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Derivatives not formally designated as hedges

Derivatives not formally designated as hedges are entered into to manage the interest rate risk of fixed rate deposits and foreign exchange risk of the Banks' exposure. Changes in the fair value of derivative instruments not formally designated as hedges are recognised in foreign exchange income.

### Client service derivatives

The Bank enters into foreign exchange contracts and interest rate caps primarily to meet the foreign exchange needs of its customers. Foreign exchange contracts are agreements to exchange specific amounts of currencies at a future date at a specified rate of exchange. Changes in the fair value of client services derivative instruments are recognised in foreign exchange income.

The following table shows the aggregate notional amounts of derivative contracts outstanding listed by type and respective gross positive or negative fair values and classified by those used for risk management (sub-classified as hedging and those that do not qualify for hedge accounting), client services and credit derivatives. Fair value of derivatives is recorded in the consolidated balance sheets in other assets and other liabilities. Gross positive fair values are recorded in other assets and gross negative fair values are recorded in other liabilities, subject to netting when master netting agreements are in place.

The following table shows the notional amounts and related fair value measurements of derivative instruments as at the balance sheet date:

31 December 2015	Derivative instrument	Notional amounts	Gross positive fair value	Gross negative fair value	Net fair value
<b>Risk management derivatives</b>					
Net investment hedges	Currency swaps	77,670	4,122	-	4,122
Derivatives not formally designated as hedging instruments	Currency swaps	77,881	273	(95)	178
Subtotal risk management derivatives		155,551	4,395	(95)	4,300
<b>Client services derivatives</b>					
	Spot and forward foreign exchange	2,572,525	16,426	(15,961)	465
<b>Total derivative instruments</b>		<b>2,728,076</b>	<b>20,821</b>	<b>(16,056)</b>	<b>4,765</b>
31 December 2014	Derivative instrument	Notional amounts	Gross positive fair value	Gross negative fair value	Net fair value
<b>Risk management derivatives</b>					
Net investment hedges	Currency swaps	114,759	1,095	(3,559)	(2,464)
Derivatives not formally designated as hedging instruments	Currency swaps	113,981	284	(1,749)	(1,465)
Subtotal risk management derivatives		228,740	1,379	(5,308)	(3,929)
<b>Client services derivatives</b>					
	Spot and forward foreign exchange	2,424,176	20,856	(20,500)	356
<b>Total derivative instruments</b>		<b>2,652,916</b>	<b>22,235</b>	<b>(25,808)</b>	<b>(3,573)</b>

In addition to the above, as at 31 December 2015 foreign denominated deposits of \$39.4 million (31 December 2014: \$15.7 million), were designated as a hedge of foreign exchange risk associated with the net investment in foreign operations.



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

We manage derivative exposure by monitoring the credit risk associated with each counterparty using counterparty specific credit risk limits, using master netting arrangements where appropriate and obtaining collateral. The Bank elected to offset in the consolidated balance sheets certain gross derivative assets and liabilities subject to netting agreements.

The Bank also elected not to offset certain derivative assets or liabilities and all collaterals received or paid that the Bank or the counterparties could legally offset in the event of default. In the tables below, these positions are deducted from the net fair value presented in the consolidated balance sheets in order to present the net exposures. The collateral values presented in the following table are limited to the related net derivative asset or liability balance and, accordingly, do not include excess collateral received or paid.

				Less: positions not offset in the consolidated balance sheets		
	Gross fair value recognised	Less: offset applied under master netting agreements	Net fair value presented in the consolidated balance sheets	Gross fair value of derivatives	Cash collateral received / paid	Net exposures
<b>31 December 2015</b>						
<b>Derivative assets</b>						
Spot and forward foreign exchange and currency swaps	20,821	(7,127)	13,694	(78)	(232)	13,384
<b>Derivative liabilities</b>						
Spot and forward foreign exchange and currency swaps	16,056	(7,127)	8,929	(78)	(148)	8,703
<b>Net positive fair value</b>			4,765	-		

				Less: positions not offset in the consolidated balance sheets		
	Gross fair value recognised	Less: offset applied under master netting agreements	Net fair value presented in the consolidated balance sheets	Gross fair value of derivatives	Cash collateral received / paid	Net exposures
<b>31 December 2014</b>						
<b>Derivative assets</b>						
Spot and forward foreign exchange and currency swaps	22,235	(5,384)	16,851	-	(3,411)	13,440
<b>Derivative liabilities</b>						
Spot and forward foreign exchange and currency swaps	25,808	(5,384)	20,424	-	(5,073)	15,351
<b>Net negative fair value</b>			(3,573)			

The following table shows the location and amount of gains (losses) recorded in the consolidated statements of operations on derivative instruments outstanding:

		Year ended	
Derivative instrument	Consolidated statements of operations line item	31 December 2015	31 December 2014
Spot and forward foreign exchange	Foreign exchange revenue	(228)	(332)
Total net losses recognised in net income		(228)	(332)

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 17: Fair value measurements

The following table presents the financial assets and liabilities that are measured at fair value on a recurring basis. Management classifies these items based on the type of inputs used in their respective fair value determination as described in Note 2.

Management reviews the price of each security monthly, comparing market values to expectations and to the prior month's price. Management's expectations are based upon knowledge of prevailing market conditions and developments relating to specific issuers and/or asset classes held in the investment portfolio. Where there are unusual or significant price movements, or where a certain asset class has performed out-of-line with expectations, the matter is reviewed by the Group Asset and Liability Committee.

Financial instruments in Level 1 include actively traded redeemable mutual funds.

Financial instruments in Level 2 include equity securities not actively traded, certificates of deposit, corporate bonds, mortgage-backed securities and other asset-backed securities, interest rate swaps and caps, forward foreign exchange contracts, and mutual funds not actively traded.

Financial instruments in Level 3 include asset-backed securities for which the market is relatively illiquid and for which information about actual trading prices is not readily available.

	31 December 2015			Total carrying amount / fair value	31 December 2014			Total carrying amount / fair value
	Fair value				Fair value			
	Level 1	Level 2	Level 3		Level 1	Level 2	Level 3	
Items that are recognised at fair value on a recurring basis:								
Financial assets								
Trading investments								
Certificates of deposit	-	-	-	-	37,743	-	37,743	
US government and federal agencies	-	279,343	-	279,343	-	312,507	312,507	
Debt securities issued	-	7,489	-	7,489	-	7,652	7,652	
Asset-backed securities - Student loans	-	28,285	-	28,285	-	52,597	52,597	
Mutual funds	5,903	279	-	6,182	6,038	848	6,886	
Total trading	5,903	315,396	-	321,299	6,038	411,347	417,385	
Available-for-sale investments								
US government and federal agencies	-	1,404,499	-	1,404,499	-	1,575,363	1,575,363	
Debt securities issued	-	-	-	-	-	-	-	
by non-US governments	-	29,575	-	29,575	-	30,673	30,673	
Corporate debt securities	-	506,144	-	506,144	-	399,289	399,289	
Asset-backed securities - Student loans	-	-	12,161	12,161	-	-	12,226	
Commercial mortgage-backed securities	-	148,726	-	148,726	-	151,169	151,169	
Residential mortgage-backed securities - Prime	-	100,244	-	100,244	-	64,829	64,829	
Total available-for-sale	-	2,189,188	12,161	2,201,349	-	2,221,323	2,233,549	
Other assets - Derivatives	-	13,694	-	13,694	-	16,851	16,851	
Financial liabilities								
Other liabilities - Derivatives	-	8,929	-	8,929	-	20,424	20,424	

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**  
*(In thousands of Bermuda dollars, unless otherwise stated)*

There were no transfers between Level 1 and Level 2 during the year ended 31 December 2015 and 2014.

The Level 3 Asset-backed securities - Student loans is a federal family education loan programme guaranteed student loan security and is valued using a non-binding broker quote. The fair value provided by the broker is based on the last trading price of similar securities but as the market for the security is illiquid, a Level 2 classification is not supported.

Significant increases (decreases) in any of the preceding inputs in isolation could result in a significantly different fair value measurement. Generally a change in assumption used for the probability of defaults is accompanied by a directionally similar change in the assumption used for the loss severity.

	<b>31 December 2015</b>	31 December 2014
<b>Level 3 Reconciliation</b>		
Carrying amount at beginning of year	<b>12,226</b>	45,304
Proceeds from sales, paydowns and maturities	-	(36,439)
Accretion recognised in net income	-	915
Realised and unrealised gains (losses) recognised in other comprehensive income	<b>(65)</b>	(6,286)
Realised and unrealised gains recognised in net income	-	8,732
<b>Carrying amount at end of year</b>	<b>12,161</b>	12,226

**Items Other Than Those Recognised at Fair Value on a Recurring Basis:**

		<b>31 December 2015</b>			<b>31 December 2014</b>		
	<b>Level</b>	<b>Carrying amount</b>	<b>Fair value</b>	<b>Appreciation / (depreciation)</b>	<b>Carrying amount</b>	<b>Fair value</b>	<b>Appreciation / (depreciation)</b>
<b>Financial assets</b>							
Cash due from banks	Level 1	<b>2,288,890</b>	<b>2,288,890</b>	-	2,063,311	2,063,311	-
Short-term investments	Level 1	<b>409,482</b>	<b>409,482</b>	-	394,770	394,770	-
Investments held-to-maturity	Level 2	<b>701,282</b>	<b>701,495</b>	<b>213</b>	338,177	343,989	5,812
Loans, net of allowance for credit losses	Level 2	<b>4,000,155</b>	<b>3,996,443</b>	<b>(3,712)</b>	4,019,128	4,015,764	(3,364)
Other real estate owned <sup>1</sup>	Level 2	<b>11,206</b>	<b>11,206</b>	-	19,300	19,300	-
<b>Financial liabilities</b>							
Customer deposits							
Demand deposits	Level 2	<b>7,654,643</b>	<b>7,654,643</b>	-	6,737,644	6,737,644	-
Term deposits	Level 2	<b>1,513,025</b>	<b>1,514,126</b>	<b>(1,101)</b>	1,894,027	1,895,558	(1,531)
Deposits from banks	Level 2	<b>14,478</b>	<b>14,478</b>	-	39,906	39,906	-
Long-term debt	Level 2	<b>117,000</b>	<b>116,606</b>	<b>394</b>	117,000	115,936	1,064

<sup>1</sup> The current carrying value of OREO is adjusted to fair value only when there is devaluation below carrying value.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 18: Interest rate risk

The following tables set out the assets, liabilities and shareholders' equity and off-balance sheet instruments on the date of the earlier of contractual maturity, expected maturity or repricing date. Use of these tables to derive information about the Bank's interest rate risk position is limited by the fact that customers may choose to terminate their financial instruments at a date earlier than the contractual maturity or repricing date. Examples of this include fixed-rate mortgages, which are shown at contractual maturity but which may prepay earlier, and certain term deposits, which are shown at contractual maturity but which may be withdrawn before their contractual maturity subject to prepayment penalties. Investments are shown based on remaining contractual maturities. The remaining contractual principal maturities for mortgage-backed securities (primarily US Government agencies) do not consider prepayments. Remaining expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations before the underlying mortgages mature.

#### 31 December 2015

(in \$ millions)	Earlier of contractual maturity or repricing date						Total
	Within 3 months	3 to 6 months	6 to 12 months	1 to 5 years	After 5 years	Non-interest bearing funds	
<b>Assets</b>							
Cash due from banks	2,178	-	-	-	-	111	2,289
Short-term investments	117	291	1	-	-	-	409
Investments	871	79	19	620	1,629	6	3,224
Loans	3,735	84	53	67	47	14	4,000
Other assets	-	-	-	-	-	354	354
<b>Total assets</b>	<b>6,901</b>	<b>454</b>	<b>73</b>	<b>687</b>	<b>1,676</b>	<b>485</b>	<b>10,276</b>
<b>Liabilities and shareholders' equity</b>							
Shareholders' equity	-	-	-	-	-	750	750
Demand deposits	5,783	-	-	-	-	1,882	7,665
Term deposits	989	296	153	79	-	-	1,517
Other liabilities	-	-	-	-	-	227	227
Long-term debt	92	-	-	25	-	-	117
<b>Total liabilities and shareholders' equity</b>	<b>6,864</b>	<b>296</b>	<b>153</b>	<b>104</b>	<b>-</b>	<b>2,859</b>	<b>10,276</b>
Interest rate sensitivity gap	37	158	(80)	583	1,676	(2,374)	-
Cumulative interest rate sensitivity gap	37	195	115	698	2,374	-	-

#### 31 December 2014

(in \$ millions)	Earlier of contractual maturity or repricing date						Total
	Within 3 months	3 to 6 months	6 to 12 months	1 to 5 years	After 5 years	Non-interest bearing funds	
<b>Assets</b>							
Cash due from banks	1,923	-	-	-	-	140	2,063
Short-term investments	155	224	16	-	-	-	395
Investments	422	37	105	470	1,948	7	2,989
Loans	3,685	133	20	112	45	24	4,019
Other assets	-	-	-	-	-	392	392
<b>Total assets</b>	<b>6,185</b>	<b>394</b>	<b>141</b>	<b>582</b>	<b>1,993</b>	<b>563</b>	<b>9,858</b>
<b>Liabilities and shareholders' equity</b>							
Shareholders' equity	-	-	-	-	-	849	849
Demand deposits	5,142	64	-	-	-	1,559	6,765
Term deposits	1,168	344	316	79	-	-	1,907
Other liabilities	-	-	-	-	-	220	220
Long-term debt	47	-	45	25	-	-	117
<b>Total liabilities and shareholders' equity</b>	<b>6,357</b>	<b>408</b>	<b>361</b>	<b>104</b>	<b>-</b>	<b>2,628</b>	<b>9,858</b>
Interest rate sensitivity gap	(172)	(14)	(220)	478	1,993	(2,065)	-
Cumulative interest rate sensitivity gap	(172)	(186)	(406)	72	2,065	-	-

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 19: Long-term debt

On 28 May 2003, the Bank issued US \$125 million of Subordinated Lower Tier II capital notes. The notes were issued at par and in two tranches, namely US \$78 million in Series A notes due 2013 and US \$47 million in Series B notes due 2018. The issuance was by way of private placement with US institutional investors. The notes are listed on the Bermuda Stock Exchange ("BSX") in the specialist debt securities category. Part proceeds of the issue were used to repay the entire amount of the US \$75 million outstanding subordinated notes redeemed in July 2003. The notes issued under Series A paid a fixed coupon of 3.94% until 27 May 2008 when it was redeemed in whole by the Bank. The Series B notes paid a fixed coupon of 5.15% until 27 May 2013 when they became redeemable in whole at the Bank's option. The Series B notes were priced at a spread of 1.35% over the 10-year US Treasury yield.

On 27 June 2005, the Bank issued US \$150 million of Subordinated Lower Tier II capital notes. The notes were issued at par in two tranches, namely US \$90 million in Series A notes due 2015 and US \$60 million in Series B notes due 2020. The issuance was by way of private placement with US institutional investors. The notes are listed on the BSX in the specialist debt securities category. The notes issued under Series A paid a fixed coupon of 4.81% until 2 July 2010 after which the coupon rate became floating and the principal became redeemable in whole at the Bank's option. The Series B notes pay a fixed coupon of 5.11% until 2 July 2015 when they also become redeemable in whole at the Bank's option. The Series A notes were priced at a spread of 1.00% over the five-year US Treasury yield and the Series B notes were priced at a spread of 1.10% over the 10-year US Treasury yield. During September 2011, the Bank repurchased a portion of the outstanding 5.11% 2005 Series B Subordinated notes ("the Note"). The face value of the portion of the Note repurchased was \$15 million and the purchase price paid for the repurchase was \$13.875 million, which realised a gain of \$1.125 million. During January 2014, the Bank fully redeemed the 2005 issuance Series A subordinated debt for its nominal value of \$90 million.

On 27 May 2008, the Bank issued US \$78 million of Subordinated Lower Tier II capital notes. The notes were issued at par and in two tranches, namely US \$53 million in Series A notes due 2018 and US \$25 million in Series B notes due 2023. The issuance was by way of private placement with US institutional investors. The notes are listed on the BSX in the specialist debt securities category. The proceeds of the issue were used to repay the entire amount of the US \$78 million outstanding subordinated notes redeemed in May 2008. The notes issued under Series A paid a fixed coupon of 7.59% until 27 May 2013 when they became redeemable in whole at the option of the Bank. In May 2013, the Bank exercised its option to redeem the Series A note outstanding at face value. The Series B notes pay a fixed coupon of 8.44% until 27 May 2018 when they also become redeemable in whole at the Bank's option. The Series B notes were priced at a spread of 4.51% over the 10-year US Treasury yield.

No interest was capitalised during the years ended 31 December 2015 and 2014.

The following table presents the contractual maturity and interest payments for long-term debt issued by the Bank as at 31 December 2015. The interest payments are calculated until contractual maturity using the current LIBOR rates.

Long-term debt	Earliest date redeemable at the Bank's option	Contractual maturity date	Interest rate until date redeemable	Interest rate from earliest date redeemable to contractual maturity	Principal Outstanding	Interest payments until contractual maturity		
						Within 1 year	1 to 5 years	After 5 years
<b>Bermuda</b>								
2003 issuance - Series B	27-May-2013	27-May-2018	5.15%	3 months US\$ LIBOR + 2.000%	47,000	1,248	1,862	-
2005 issuance - Series B	2-Jul-2015	2-Jul-2020	5.11%	3 months US\$ LIBOR + 1.695%	45,000	1,056	3,949	-
2008 issuance - Series B	27-May-2018	27-May-2023	8.44%	3 months US\$ LIBOR + 4.929%	25,000	2,110	6,686	3,506
<b>Total</b>					<b>117,000</b>	<b>4,414</b>	<b>12,497</b>	<b>3,506</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 20: Earnings per share

Earnings per share have been calculated using the weighted average number of common shares outstanding during the year after deduction of the shares held as treasury stock. The dilutive effect of share-based compensation plans was calculated using the treasury stock method, whereby the proceeds received from the exercise of share-based awards are assumed to be used to repurchase outstanding shares, using the average market price of the Bank's shares for the year. Numbers of shares are expressed in thousands.

	Year ended 31 December 2015	31 December 2014
<b>Basic Earnings Per Share</b>	<b>0.13</b>	0.17
Net income	77,739	108,159
Less: Preference dividends declared and guarantee fee	(16,455)	(16,546)
Less: Premium on preference share buyback	(28)	(96)
<b>Net income attributable for common shareholders</b>	<b>61,256</b>	91,517
Weighted average number of common shares issued	500,009	556,933
Weighted average number of common shares held as treasury stock	(10,788)	(9,336)
<b>Adjusted weighted average number of common shares (in thousands)</b>	<b>489,221</b>	547,597
<b>Diluted Earnings Per Share</b>	<b>0.12</b>	0.16
<b>Net income attributable for common shareholders</b>	<b>61,256</b>	91,517
Adjusted weighted average number of common shares issued	489,221	547,597
Net dilution impact related to options to purchase common shares	4,718	3,927
Net dilution impact related to awards of unvested common shares	6,089	4,958
<b>Adjusted weighted average number of diluted common shares (in thousands)</b>	<b>500,028</b>	556,482

Prior to their conversion into common shares on 31 March 2015, outstanding contingent value convertible preference ("CVCP") shares were classified as participating securities as they were entitled to dividends declared to common shareholders on a 1:1 basis and were therefore included in the basic earnings per share calculation.

During the year ended 31 December 2015, options to purchase an average of 29.0 million (31 December 2014: 31.1 million) shares of common stock, were outstanding. During the year ended 31 December 2015, the average number of outstanding awards of unvested common shares was 9.2 million (31 December 2014: 9.5 million). Only awards for which the sum of 1) the expense that will be recognised in the future (i.e. the unrecognised expense) and 2) its exercise price, if any, was lower than the average market price of the Bank's common stock were considered dilutive and, therefore, included in the computation of diluted earnings per share. An award's unrecognised expense is also considered to be the proceeds the employees would need to pay to purchase accelerated vesting of the awards. For purposes of calculating dilution, such proceeds are assumed to be used by the Bank to buy back common shares at the average market price. The weighted-average number of outstanding awards, net of the assumed weighted-average number of common shares bought back, is included in the number of diluted participating shares.

Warrants issued to the Government of Bermuda in exchange for the Government's guarantee of the preference shares, with an exercise price of \$3.47 (31 December 2014: \$3.49) for 4.32 million shares of common stock (31 December 2014: 4.30 million) were not included in the computation of earnings per share as at 31 December 2015 and 2014 because the exercise price was greater than the average market price of the Bank's common stock.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 21: Share-based payments

#### Stock Option Plans

##### 1997 Stock Option Plan

Prior to the capital raise on 2 March 2010, the Bank granted stock options to employees and Directors of the Bank that entitle the holder to purchase one common share at a subscription price equal to the market price on the effective date of the grant. Generally, the options granted vest 25 percent at the end of each year for four years, however as a result of the 2010 capital raise, the options granted under the Bank's 1997 Stock Option Plan to employees became fully vested and options awarded to certain executives were surrendered.

##### 2010 Stock Option Plan

In conjunction with the capital raise, the Board of Directors approved the 2010 Stock Option Plan. Under the Plan, five per cent of the Bank's fully diluted common shares, equal to approximately 29.5 million shares, are available for grant to certain officers. In May 2012, the Board of Directors approved an increase to the options allowed to be granted under the 2010 Stock Option Plan to 50 million shares.

Under the 2010 Stock Option Plan, options are awarded to Bank employees and executive management, based on predetermined vesting conditions that entitle the holder to purchase one common share at a subscription price usually equal to the price of the most recently traded common share when granted and have a term of 10 years. The subscription price will be reduced for all special dividends declared by the Bank.

The 2010 Stock Option Plan will vest based on two specific types of vesting conditions i.e., time and performance conditions, as detailed below:

#### Time vesting condition

50% of each option award is granted in the form of time vested options and vests 25% on each of the second, third, fourth and fifth anniversaries of the effective grant date.

#### Performance vesting condition

50% of each option award is granted in the form of performance options and vests (partially or fully) on a "valuation event" date (date any of the 2 March 2010 new investors transfers at least 5% of the total number of common shares or the date that there is a change in control and any of the new investors realises a predetermined multiple of invested capital ("MOIC"). In the event of a valuation event and the MOIC reaching 200% of the original \$1.21 per share invested capital, all performance options would vest. As at 31 December 2015 the grant date fair value not yet recognised in expenses of outstanding performance options is \$8.7 million (31 December 2014: \$8.9 million). If the probability of a valuation event becomes more likely than not, some or all of the unrecognised expense relating to the performance options will be recognised as an expense.

In addition to the time and performance vesting conditions noted above, the options will generally vest immediately:

- by reason of the employee's death or disability,
- upon termination, by the Bank, of the holder's employment, unless if in relation with the holder's misconduct, or
- in limited circumstances and specifically approved by the Board, as stipulated in the holder's employment contract.

In the event of the employee's resignation, any unvested portion of the awards shall generally be forfeited and any vested portion of the options shall generally remain exercisable during the 90-day period following the termination date or, if earlier, until the expiration date, and any vested portion of the options not exercised as of the expiration of such period shall be forfeited without any consideration therefore.

	Time vested options	Performance vested options
<b>Weighted average fair value of stock options granted</b>		
Year ended 31 December 2012 (most recent year during which options were granted)	\$0.42	\$0.44
Year ended 31 December 2011	\$0.41	\$0.43

The weighted average fair value of stock options granted in the years ended 31 December 2012 and 2011 was calculated using the Black-Scholes-Merton option-pricing model for the time vested options and a lattice-based binomial option-pricing model for the performance options using the following weighted average assumptions:

	Time vested options	Performance vested options
Projected dividend yield	0% for 2011-2013 1.0% for 2014 2.0% for 2015 and later years	0% for 2011-2013 1.0% for 2014 2.0% for 2015 and later years
Risk-free interest rate	0.94% to 1.44%	0% to 2.09%
Projected volatility	36% to 38%	36% to 38%
Expected life (years)	6.75 years	8 to 10 years



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Changes in Outstanding Stock Options

Year ended	Number of shares transferable upon exercise (thousands)			Weighted average exercise price (\$)		Weighted average remaining life (years)		Aggregate intrinsic value (\$ thousands)
	1997 Stock Option Plan	2010 Stock Option Plan	Total	1997 Stock Option Plan	2010 Stock Option Plan	1997 Stock Option Plan	2010 Stock Option Plan	
<b>31 December 2015</b>								
Outstanding at beginning of year	3,525	26,780	30,305	13.07	1.17			
Exercised	-	(554)	(554)	-	1.15			
Forfeitures and cancellations	(1,349)	(24)	(1,373)	12.33	1.15			
Resignations, retirements, redundancies	-	(132)	(132)	-	1.15			
<b>Outstanding at end of year</b>	<b>2,176</b>	<b>26,070</b>	<b>28,246</b>	<b>13.52</b>	<b>1.16</b>	<b>1.78</b>	<b>4.67</b>	<b>20,594</b>
<b>Vested and exercisable at end of year</b>	<b>2,176</b>	<b>12,423</b>	<b>14,599</b>	<b>13.52</b>	<b>1.16</b>	<b>1.78</b>	<b>4.94</b>	

Year ended	Number of shares transferable upon exercise (thousands)			Weighted average exercise price (\$)		Weighted average remaining life (years)		Aggregate intrinsic value (\$ thousands)
	1997 Stock Option Plan	2010 Stock Option Plan	Total	1997 Stock Option Plan	2010 Stock Option Plan	1997 Stock Option Plan	2010 Stock Option Plan	
<b>31 December 2014</b>								
Outstanding at beginning of year	3,992	27,808	31,800	12.83	1.17			
Exercised	-	(1,027)	(1,027)	-	1.16			
Forfeitures and cancellations	(436)	(1)	(437)	10.86	1.16			
Resignations, retirements, redundancies	-	-	-	-	1.16			
Expiration at end of plan life	(31)	-	(31)	13.76	-			
<b>Outstanding at end of year</b>	<b>3,525</b>	<b>26,780</b>	<b>30,305</b>	<b>13.07</b>	<b>1.17</b>	<b>2.38</b>	<b>5.66</b>	<b>22,233</b>
<b>Vested and exercisable at end of year</b>	<b>3,525</b>	<b>8,677</b>	<b>12,202</b>	<b>13.07</b>	<b>1.17</b>	<b>2.38</b>	<b>5.65</b>	

### Share Based Plans

Recipients of unvested share awards are entitled to the related common shares at no cost, at the time the award vests. Recipients of unvested shares may be entitled to receive additional unvested shares having a value equal to the cash dividends that would have been paid had the unvested shares been issued and vested. Such additional unvested shares granted as dividend equivalents are subject to the same vesting schedule and conditions as the underlying unvested shares.

Unvested shares subject only to the time vesting condition generally vest upon retirement, death, disability or upon termination, by the Bank, of the holder's employment unless in relation with the holder's misconduct. Unvested shares subject to both time vesting and performance vesting conditions remain outstanding and unvested upon retirement and will vest only if the performance conditions are met. Unvested shares can also vest in limited circumstances and if specifically approved by the Board, as stipulated in the holder's employment contract. In all other circumstances, unvested shares are generally forfeited when employment ends.

### Employee Deferred Incentive Plan ("EDIP")

Under the Bank's EDIP Plan, shares were awarded to Bank employees and executive management based on the time vesting condition, which states that the shares will vest equally over a three-year period from the effective grant date.

### Executive Long-Term Incentive Share Plan ("ELTIP")

#### 2012 and 2011 ELTIP

Under the Bank's 2012 and 2011 ELTIP, shares were awarded to Bank employees and executive management, based on predetermined vesting conditions. Two types of vesting conditions upon which the shares were awarded comprise the ELTIP: 1) 50% of each share award were granted in the form of time vested shares, generally vesting equally over a three-year period from the effective grant date; and 2) 50% of each share award were granted in the form of performance shares, generally vesting upon the achievement of certain performance targets in the three-year period from the effective grant date.

#### 2015, 2014 and 2013 ELTIP

The 2015 ELTIP was approved on 11 February 2015. Under the Bank's 2015, 2014 and 2013 ELTIP, performance shares were awarded to executive management. These shares will generally vest upon the achievement of certain performance targets in the three-year period from the effective grant date.

Number of shares transferable upon vesting of the ELTIP and EDIP shares (in thousands of shares)	Year ended			
	31 December 2015		31 December 2014	
	EDIP	ELTIP	EDIP	ELTIP
Outstanding at beginning of year	2,660	7,062	2,183	6,441
Granted	1,739	2,530	1,510	2,550
Vested	(2,071)	(3,220)	(1,029)	(1,852)
Resignations, retirements, redundancies	(73)	(311)	(4)	(77)
<b>Outstanding at end of year</b>	<b>2,255</b>	<b>6,061</b>	<b>2,660</b>	<b>7,062</b>

(In thousands of Bermuda dollars, unless otherwise stated)

## Year ended

Share-based compensation cost

31 December 2015	31 December 2014
---------------------	---------------------

Time vesting options  
Performance vesting options

## EL TIP

The Bank initially introduced two share buy-back programmes on 1 May 2012 as a means to improve shareholder liquidity and facilitate growth in share value. Each programme was approved by the Board of Directors for a period of 12 months, in accordance with the regulations of the BSX. The BSX must be advised monthly of shares purchased pursuant to each programme.

Effective 1 April 2014, the Board approved the 2014 common share buy-back programme authorising the purchase for treasury of up to 15 million common shares.

On 26 February 2015, the Board approved, with effect from 1 April 2015, the 2015 common share buy-back programme, authorising the purchase for treasury of up to eight million common shares.

## Common share buy-backs

On 28 April 2014, the Board approved the 2014 preference share buy-back programme, authorising the purchase and cancellation of up to 26,600 preference shares.

On 26 February 2015, the Board approved, with effect from 5 May 2015, the 2015 preference share buy-back programme, authorising the purchase for cancellation of up to 5,000 preference shares.

### Preference share buy-backs

From time to time the Bank's associates, insiders and insiders' associates as defined by the BSX regulations may sell shares which may result in such shares being repurchased pursuant to each programme, provided no more than any such person's pro-rata share of the listed securities is repurchased. Pursuant to the BSX regulations, all repurchases made by any issuer pursuant to a securities repurchase programme must be made: (1) in the open market and not by private agreement; and (2) for a price not higher than the last independent trade for a round lot of the relevant class of securities. See Note 24, in which certain large one-time share buy-backs transactions are described.

**The Bank of N.T. Butterfield & Son Limited**  
**Notes to the Consolidated Financial Statements**

(In thousands of Bermuda dollars, unless otherwise stated)

**Note 23: Accumulated other comprehensive loss**

The table below presents the changes in AOCL by component for the year ended:

	Unrealised (losses) on translation of net investment in foreign operations	HTM investments	Unrealised gains (losses) on AFS investments	Employee benefit plans			Total AOCL
				Pension	Post-retirement healthcare	Subtotal - employee benefits plans	
<b>31 December 2015</b>							
<b>Balance at beginning of year</b>	(10,506)	-	9,021	(53,169)	(22,866)	(76,035)	(77,520)
Transfer of AFS investments to HTM investments	-	(2,715)	2,715	-	-	-	-
Other comprehensive income (loss), net of taxes	(3,139)	365	(11,793)	6,838	(5,248)	1,590	(12,977)
<b>Balance at end of year</b>	<b>(13,645)</b>	<b>(2,350)</b>	<b>(57)</b>	<b>(46,331)</b>	<b>(28,114)</b>	<b>(74,445)</b>	<b>(90,497)</b>

	Unrealised (losses) on translation of net investment in foreign operations	HTM investments	Unrealised gains (losses) on AFS investments	Employee benefit plans			Total AOCL
				Pension	Post-retirement healthcare	Subtotal - employee benefits plans	
<b>31 December 2014</b>							
<b>Balance at beginning of year</b>	(7,632)	-	(40,136)	(35,616)	6,724	(28,892)	(76,660)
Other comprehensive income (loss), net of taxes	(2,874)	-	40,085	(17,553)	(29,590)	(47,143)	(9,932)
Reclassification to accumulated deficit	-	-	9,072	-	-	-	9,072
<b>Balance at end of year</b>	<b>(10,506)</b>	<b>-</b>	<b>9,021</b>	<b>(53,169)</b>	<b>(22,866)</b>	<b>(76,035)</b>	<b>(77,520)</b>

**Net Change of AOCL Components**

		Year ended	
		31 December 2015	31 December 2014
Line item in the consolidated statements of operations, if any			
<b>Net unrealised gains (losses) on translation of net investment in foreign operations adjustments</b>			
Foreign currency translation adjustments	N/A	(9,723)	(10,574)
Gains on net investment hedge	N/A	6,584	7,700
<b>Net change</b>		<b>(3,139)</b>	<b>(2,874)</b>
<b>Held-to-maturity investment adjustments</b>			
Net unamortised losses transferred from AFS during the year	N/A	(2,715)	-
Amortisation of net losses to net income	Interest income on investments	378	-
Foreign currency translation adjustments of related balances	N/A	(13)	-
<b>Net change</b>		<b>(2,350)</b>	<b>-</b>
<b>Available-for-sale investment adjustments</b>			
Gross unrealised gains (losses) arising during the year	N/A	(16,337)	48,703
Net unrealised losses transferred to HTM during the year	N/A	2,715	-
Transfer of realised (gains) losses to net income	Net realised gains (losses) on AFS investments	4,407	(8,680)
Foreign currency translation adjustments of related balances	N/A	137	62
<b>Net change</b>		<b>(9,078)</b>	<b>40,085</b>
<b>Employee benefit plans adjustments</b>			
<b>Defined benefit pension plan</b>			
Net actuarial gain (loss)	N/A	5,096	(18,947)
Amortisation of actuarial losses	Salaries and other employee benefits	1,703	1,058
Change in deferred taxes	N/A	(391)	83
Foreign currency translation adjustments of related balances	N/A	430	253
<b>Net change</b>		<b>6,838</b>	<b>(17,553)</b>
<b>Post-retirement healthcare plan</b>			
Net actuarial (loss)	N/A	(2,252)	(15,892)
Prior service cost	N/A	-	(7,901)
Amortisation of net actuarial losses	Salaries and other employee benefits	3,347	922
Amortisation of prior service credit	Salaries and other employee benefits	(6,343)	(6,719)
<b>Net change</b>		<b>(5,248)</b>	<b>(29,590)</b>
<b>Other comprehensive (loss), net of taxes</b>		<b>(12,977)</b>	<b>(9,932)</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 24: Capital structure

#### Authorised Capital

The Bank's total authorised share capital as of 31 December 2015 and 2014 consisted of (i) 26 billion common shares of par value BD\$0.01, (ii) 100,200,001 preference shares of par value US\$0.01 and (iii) 50 million preference shares of par value £0.01.

On 30 April 2015, Butterfield repurchased and cancelled 80,000,000 shares held by CIBC for \$1.50 per share, for a total of \$120 million. The remaining CIBC shareholding in Butterfield (representing 23,434,232 shares) was taken up by Carlyle Global Financial Services, L.P. at \$1.50 per share and subsequently sold to other investors.

On 13 August 2015, Butterfield repurchased and cancelled 4,000,000 shares held by two shareholders for \$1.49 per share, for a total of \$5.96 million.

#### Preference Shares

On 22 June 2009, the Bank issued 200,000 Government guaranteed, 8.00% non-cumulative perpetual limited voting preference shares (the "preference shares"). The issuance price was US\$1,000 per share. The preference share buy-backs are disclosed in Note 22: Share Buy-Back Plans.

The preference share principal and dividend payments are guaranteed by the Government of Bermuda. At any time after the expiry of the guarantee offered by the Government of Bermuda, and subject to the approval of the BMA, the Bank may redeem, in whole or in part, any preference shares at the time issued and outstanding, at a redemption price equal to the liquidation preference plus any unpaid dividends at the time.

Holders of preference shares will be entitled to receive, on each preference share only when, as and if declared by the Board of Directors, non-cumulative cash dividends at a rate per annum equal to 8.00% on the liquidation preference of US \$1,000 per preference share payable quarterly in arrears. In exchange for the Government's commitment, the Bank issued to the Government 4,279,601 warrants to purchase common shares of the Bank at an exercise price of \$7.01. The warrants expire on 22 June 2019. During 2010, the warrants issued to the Government were adjusted in accordance with the terms of the guarantee and as a result the Government now holds 4,320,613 warrants with an exercise price of \$3.47 as at 31 December 2015.

On 11 May 2010, the Bank's Rights offering was over subscribed with the maximum allowable number of rights of 107,438,016 exercised and subsequently converted on the ratio of 0.07692 CVCP shares for each right unit exercised amounting to 8,264,157 CVCP shares issued. The CVCP shares have specific rights and conditions attached, which are explained in detail in the prospectus of the rights offering. On 31 March 2015, all remaining CVCP shares were converted to common shares at a ratio of 1:1.

#### Dividends Declared

During the year ended 31 December 2015, the Bank declared cash dividends totalling \$0.05 (31 December 2014: \$0.05) for each common share and CVCP share on record (CVCP shares were all converted to common shares on 31 March 2015) as of the related record dates. During the years ended 31 December 2015 and 2014, the Bank declared the full 8.00% cash dividends on preference shares in each quarter.

The Bank is required to comply with Section 54 of the Companies Act 1981 issued by the Government of Bermuda (the "Companies Act") each time a dividend is declared or paid by the Bank and also obtain prior written approval from the BMA pursuant to the Banks and Deposit Companies Act 1999 for any dividends declared. The Bank has complied with Section 54 and has obtained BMA approval for all dividends declared during the periods under review.

#### Regulatory Capital

The Bank is subject to Basel II which is a risk-based capital adequacy framework developed by the Basel Committee on Banking Supervision (the "Basel Committee") and has been endorsed by the central bank governors and heads of bank supervision of the G10 countries. In December 2008, the BMA published final rules, effective 1 January 2009, with respect to the implementation of the Basel II framework. From this date the Bank has calculated its capital requirement on the Standardised approach under Basel II requirements.

Effective 1 January 2015, the BMA adopted capital and liquidity regulatory requirements consistent with Basel III, a framework released by the Basel Committee on Banking Supervision. The finalisation of the implementation is subject to ongoing consultation with the BMA regarding the implementation and interpretation of these new rules. The Bank is assessing the impact of the adoption of this guidance. The impact will likely increase capital requirements further and the Bank maintains adequate capital buffers to meet these requirements.

The Bank is fully compliant with all regulatory capital requirements and maintains capital ratios in excess of regulatory minimums as at 31 December 2015 and 2014. The following table sets forth the Bank's capital adequacy in accordance with Basel II framework:

	31 December 2015		31 December 2014	
	Actual	Regulatory minimum	Actual	Regulatory minimum
<b>Capital</b>				
Tier 1 capital	699,173	N/A	781,743	N/A
Tier 2 capital	119,163	N/A	130,788	N/A
Total capital	818,336	N/A	912,531	N/A
<b>Risk Weighted Assets</b>	4,305,350	N/A	4,113,404	N/A
<b>Capital Ratios (%)</b>				
Tier 1 common	12.0%	N/A	14.6%	N/A
Tier 1 Total	16.2%	4.0%	19.0%	4.0%
Total Capital	19.0%	14.46%	22.2%	14.64%

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 25: Income taxes

The Bank is incorporated in Bermuda, and pursuant to Bermuda law is not taxed on either income or capital gains. The Bank's subsidiaries in the Cayman Islands and The Bahamas are not subject to any taxes in their respective jurisdictions on either income or capital gains under current law applicable in the respective jurisdictions. The Bank's subsidiaries in the United Kingdom, Guernsey, and Switzerland are subject to the tax laws of those jurisdictions.

For the years ended 31 December 2015 and 2014, the Bank did not record any unrecognised tax benefits or expenses and has no uncertain tax positions as at 31 December 2015 and 2014.

The Bank records income taxes based on the enacted tax laws and rates applicable in the relevant jurisdictions for the years ended 31 December 2015 and 2014. For the years ended 31 December 2015 and 2014, the Bank did not incur any interest or pay any penalties.

	Year ended 31 December 2015	31 December 2014
<b>Income taxes in consolidated statements of operations</b>		
Current tax expense (benefit)	819	(169)
Deferred tax expense	457	-
<b>Total tax expense (benefit)</b>	<b>1,276</b>	<b>(169)</b>

### Reconciliation between the Effective Income Tax Rate And The Statutory Income Tax Rate

	Year ended		31 December 2014	
	31 December 2015		31 December 2014	
	\$	%	\$	%
Income tax expense at Bermuda corporation tax rate of 0%	-	-	-	-
Income tax expense in international offices taxed at different rates	(904)	(1)	1,501	2
Change in valuation allowance	466	1	(1,429)	(2)
Prior year tax adjustments	80	-	(956)	(1)
Other - net	1,634	2	715	1
<b>Income tax expense (benefit) at effective tax rate</b>	<b>1,276</b>	<b>2</b>	<b>(169)</b>	<b>-</b>

	31 December 2015	31 December 2014
<b>Deferred income taxes</b>		
<b>Deferred income tax asset</b>		
Tax loss carried forward	2,540	2,641
Pension liability	365	800
Fixed assets	741	1,067
Allowance for compensated absence	9	10
Onerous leases	11	11
<b>Deferred income tax asset before valuation allowance</b>	<b>3,666</b>	<b>4,529</b>
Less: valuation allowance	(3,105)	(3,068)
<b>Net deferred income tax assets</b>	<b>561</b>	<b>1,461</b>
<b>Deferred income tax liability</b>		
Other	-	-
<b>Net deferred income tax asset</b>	<b>561</b>	<b>1,461</b>

Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to use the existing deferred tax assets. A significant piece of objective negative evidence evaluated was the cumulative loss incurred in the UK bank over the year ended 31 December 2015. Such objective evidence limits the ability to consider other subjective evidence such as projections for future growth.

On the basis of this evaluation, as of 31 December 2015, a valuation allowance of \$3.1 million (31 December 2014: \$3.1 million) has been recognised to record only the portion of the deferred tax asset that more likely than not will be realised. The amount of the deferred tax asset considered realisable, however, could be adjusted if estimates of future taxable income during the carry-forward period are reduced or increased, or if objective negative evidence in the form of cumulative losses is no longer present and additional weight may be given to subjective evidence such as our projections for growth.

The Bank has net taxable loss carry forwards related to the Bank's international operations of approximately \$13.6 million (31 December 2014: \$12.3 million), which have an indefinite life.

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 26: Business combinations

#### Legis Acquisition

On 1 April 2014, the Bank via one of its subsidiaries, Butterfield Trust (Guernsey) Limited ("BTGL"), acquired all of the outstanding common shares of Legis T & C Holdings Limited ("Legis") for a maximum purchase price of up to \$39.6 million. Legis is a Guernsey-based trust and corporate services business. The acquisition was undertaken to enhance the Bank's market presence and widen the Bank's range of corporate and institutional trust services for private clients and institutional and corporate clients.

The acquisition date fair value of the cash consideration transferred amounted to \$34.8 million comprising cash settlement of \$31.9 million paid on 1 April 2014 and a contingent consideration of \$2.9 million. The contingent consideration is dependent on revenue performance and representation and warranties being met. The undiscounted contingent consideration ranges from \$2.3 million to \$5.4 million. The fair value is calculated as the discounted amount payable based on various case scenarios with equal probabilities assigned to the payouts being made under each scenario.

The fair value of the net assets acquired and allocation of purchase is summarised as follows:

	<b>As at 1 April 2014</b>
<b>Total consideration transferred</b>	<b>34,757</b>
<b>Assets acquired</b>	
Cash due from banks	1,466
Intangible assets	15,466
Other assets	158
<b>Total assets acquired</b>	<b>17,090</b>
<b>Liabilities acquired</b>	<b>1,624</b>
<b>Excess purchase price (Goodwill)</b>	<b>19,291</b>

The final consideration payable may differ from the initial estimated liability with any changes in the liability recorded in other gains (losses) in the consolidated statements of operations until the liability is settled. Subsequent to the acquisition date, and primarily as a result of the change in payment probabilities as estimates were updated for actual results, the estimated fair value of the contingent consideration liability increased to \$3.7 million as at 31 December 2014. At 31 December 2015, the estimated fair value of the contingent consideration liability was down to \$2.7 million primarily as a result of payments made, as well as changes in expected payments to be made in accordance with the terms of the acquisition. The contingent consideration is included in other liabilities in the consolidated balance sheets.

The purchase price paid by the Bank was for intangible assets in the form of customer relationships of \$15.5 million with an estimated finite useful life of 15 years and resulting goodwill of \$19.3 million. Goodwill is made up of expected cash flows to be derived from new business and expected synergies resulting from leveraging existing support services and infrastructure within the Bank.

The Bank incurred transaction expenses, comprising legal and professional fees, related to the Legis acquisition in the amount of \$1.2 million which were expensed during the year ended 31 December 2014.

Effective 1 April 2014 the operating results of Legis are included in the consolidated financial statements. For the year ended 31 December 2015, net revenue of \$7.8 million (31 December 2014: \$6.4 million) and operating expenses of \$6.2 million (31 December 2014: \$4.9 million) from the Legis business are included in the consolidated financial statements.

The following selected unaudited pro forma financial information has been provided to present a summary of the combined results of the Bank and Legis, assuming the transaction had been effected on 1 January 2014. The unaudited pro forma data is for informational purposes only and does not necessarily represent results that would have occurred if the transaction had taken place on the basis assumed above. No unaudited pro forma data is prepared for the year ended 31 December 2015 as the operating results of Legis were fully integrated throughout the year and are included in the consolidated statements of operations.

For the year ended 31 December 2014

Total net revenue	373,554
Total non-interest operating expense (including income tax expense)	273,750
<b>Pro forma net income post business combination</b>	<b>99,804</b>

# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### HSBC Acquisition

On 7 November 2014, the Bank via one of its subsidiaries, Butterfield Bank (Cayman) Limited ("BNTB Cayman"), acquired substantially all the retail loans and deposits of HSBC Bank (Cayman) Limited ("HSBC Cayman") for a cash purchase price of \$5.3 million. The acquisition was undertaken to enhance the Bank's market presence and expand its community banking customer base in the Cayman Islands. The acquisition was accounted for as a business combination as the Bank acquired substantially all the loans and deposits of HSBC Cayman and deemed to obtain control over the business.

Disclosure of the unaudited pro forma financial information to present a summary of the combined results of the Bank and HSBC Cayman acquisition is impracticable for the year ended 31 December 2014. The disclosure is impracticable as the Bank did not acquire the legal entity and therefore does not have access to the historical revenue and expense data as it relates to the loans and deposits acquired. No unaudited pro forma data is prepared for the year ended 31 December 2015 as the operating results of HSBC Cayman were fully integrated throughout the year and are included in the consolidated statements of operations.

The fair value of the net assets acquired and allocation of purchase is summarised as follows:

	As at 7 November 2014		
	Acquisition value	Fair value adjustment	Fair value
<b>Total consideration transferred</b>			<b>5,341</b>
<b>Assets acquired</b>			
Cash due from banks	315,919	-	315,919
Loans			
Performing loans			
Residential mortgages <sup>(a)</sup>	112,491	(1,784)	110,707
Government loans <sup>(a)</sup>	20,000	(120)	19,880
Commercial loans <sup>(a)</sup>	1,721	(21)	1,700
Other loans <sup>(a)</sup>	4,175	(43)	4,132
Purchased credit impaired loans - residential mortgages <sup>(a)</sup>	11,001	(3,804)	7,197
Accrued interest receivable	522	-	522
<b>Total tangible assets acquired</b>	<b>465,829</b>	<b>(5,772)</b>	<b>460,057</b>
<b>Liabilities assumed</b>			
Deposits	465,810	-	465,810
Accrued interest payable	19	-	19
<b>Total tangible liabilities assumed</b>	<b>465,829</b>	<b>-</b>	<b>465,829</b>
Intangible assets <sup>(b)</sup>	-	11,113	11,113
<b>Excess purchase price (Goodwill)</b>			<b>-</b>

<sup>(a)</sup> Adjustment reflects the fair value adjustments based on the Bank's evaluation of the acquired loan portfolio. When assessing the fair value adjustment, the Bank has considered prepayments for purchased credit impaired loans by estimating the future cash flows of liquidated collateral.

<sup>(b)</sup> Estimated finite useful life of 15 years.

The Bank incurred transaction expenses, comprising legal and professional fees, related to the HSBC Cayman acquisition in the amount of \$1.6 million which was expensed during the year ended 31 December 2014.



# The Bank of N.T. Butterfield & Son Limited

## Notes to the Consolidated Financial Statements

(In thousands of Bermuda dollars, unless otherwise stated)

### Note 27: Related party transactions

#### Financing Transactions

As of 17 May 2005, the Bank established a programme to offer loans with preferential rates to eligible Bank employees, subject to certain conditions set by the Bank and provided that such employees meet certain credit criteria. Loan payments are serviced by automatically debiting the employee's chequing or savings account with the Bank. Applications for loans are handled according to the same policies as those for the Bank's regular retail banking clients. The Bank's ability to offer preferential rates on loans depends upon a number of factors, including market conditions, regulations and the Bank's overall profitability. The Bank has the right to change its employee loan policy at any time after notifying participants. The staff loans outstanding at 31 December 2015 amount to \$207.2 million (31 December 2014: \$208.0 million) resulting in an interest rate benefit to employees of \$5.4 million (31 December 2014: \$6.4 million).

Certain Directors of the Bank, companies in which they are principal owners, and trusts in which they are involved, have loans with the Bank. These loans were made in the ordinary course of business at normal credit terms, including interest rate and collateral requirements. As at 31 December 2015, related party Director loan balances were \$61.1 million (31 December 2014: \$58.0 million).

On 27 June 2013, the Bank executed a \$95 million loan agreement with an investment fund managed by a significant shareholder which provides for maturity on 30 June 2017. This loan was made in the ordinary course of business on normal commercial terms. At 31 December 2015, \$nil (31 December 2014: \$65.7 million) was outstanding under this agreement. For the year ended 31 December 2015, \$1.0 million (31 December 2014: \$2.7 million) of interest income has been recognised in the consolidated statements of operations.

#### Capital Transaction

Investments partnerships associated with the Carlyle Group hold approximately 23% of the Bank's equity voting power along with the right to designate two persons for nomination for election by the shareholders as members of the Bank's Board of Directors. Prior to 30 April 2015, Canadian Imperial Bank of Commerce ("CIBC") held approximately 19% of the Bank's equity voting power. On 30 April 2015, the Bank completed the transaction with CIBC to repurchase for cancellation approximately 77% of CIBC's shares for \$1.50 per share, or a total of \$120 million, representing 80,000,000 common shares. The remaining 23% of CIBC's shareholding in Butterfield (representing 23.4 million shares) were taken up by Carlyle Global Financial Services, L.P. and subsequently sold to other investors.

#### Financial Transactions With Related Parties

The Bank holds seed investments in several Butterfield mutual funds, which are managed by a wholly-owned subsidiary of the Bank. As at 31 December 2015, these investments have a fair value of \$5.0 million with an unrealized gain of \$0.9 million (31 December 2014: \$5.0 million and \$1.0 million respectively) and were included in trading investments at their fair value. During the year-ended 31 December 2015, the Bank earned \$6.4 million (2014: \$4.3 million) in asset management revenue from funds managed by a wholly-owned subsidiary of the Bank.

At 31 December 2014, the Bank held \$239.3 million in cash due from banks with CIBC. As at 31 December 2014, the Bank held forward exchange contracts with CIBC with a notional amount of \$372.9 million with unrealised losses of \$6.2 million. From 30 April 2015 onward, CIBC was no longer considered a related party to the Bank.

#### Repurchase Facility Agreement

During 2013, the Bank entered into a repurchase agreement with CIBC for a \$225 million line at market rates and terms. From 30 April 2015 onward, CIBC was no longer considered a related party to the Bank. As at 31 December 2014 and since that time, the repurchase agreement balance with CIBC was \$ nil.

### Note 28: Comparative information

Certain prior year figures have been reclassified or revised to conform to current year presentation.

During the year ended 31 December 2015, the Bank determined that certain investments classified as AFS for its operations in Guernsey and the United Kingdom should have been classified as trading securities since 2011. There is no impact to comprehensive income or total shareholders' equity in previous years as a result of this mis-classification. The Bank has revised the relevant 2014 amounts presented in the comparative year's results, and presented the accumulated effect of these revised classifications prior to 2014 as an increase of \$9.1 million to accumulated deficit and a corresponding decrease to accumulated other comprehensive loss on 1 January 2014. Included in the \$9.1 million amount are amounts of \$15.5 million unrealised losses, \$0.9 million unrealised gains and \$5.5 million unrealised gains relating to 2013, 2012 and 2011, respectively. Further, the 2014 revisions include an increase and corresponding decrease of \$9.8 million to net income and other comprehensive loss respectively as well as the re-classification of \$410.5 million of investments from AFS to trading.

### Note 29: Subsequent events

Subsequent to year-end, the Bank's subsidiary operating in the United Kingdom announced plans to commence an orderly wind-down of the deposit taking and investment management businesses of Butterfield Bank (UK) Limited. As the announcement of the orderly wind-down was more likely than not as of 31 December 2015, certain expenses relating to this were accrued for and expensed at 31 December 2015, as seen in Note 13: Exit Cost Obligations.

On 19 February 2016, the Board of Directors declared a fourth interim dividend of \$0.01 per common share to be paid on 24 March 2016 to shareholders of record on 11 March 2016.

On 19 February 2016, the Board approved, with effect from 1 April 2016, the 2015 common share buy-back programme, authorising the purchase for treasury of up to eight million common shares.

The Bank has performed an evaluation of subsequent events through to 22 February 2016, the date the consolidated financial statements were approved for issuance.