



**The Bank of New York Mellon (Luxembourg) S.A.
Pillar 3 Disclosures for the year ended 31st December 2010**

Published on 31 March 2011

About Pillar 3 Disclosure

Basis for preparation

The Board Of Directors of The Bank of New York Mellon (Luxembourg) S.A. (the “Company” or the “Bank”) adopts this policy to comply with disclosure requirements laid down in CSSF Circular 06/273 and for assessing the appropriateness of the Company’s Pillar 3 Market disclosures, including their verification and frequency.

In this matter, the following terms will apply.

The information in Pillar 3 will be prepared solely to meet the disclosure requirements about Basel II and to provide certain specified information about capital and other risks and details about the management of those risks and for no other purpose. The disclosures will not constitute any form of Financial statement on the business nor will it constitute any form of contemporary or forward looking record or opinion about the business.

These disclosures will be subjected to internal review, challenge and approval. An audit trail to support disclosures will be maintained in accordance with normal company policy.

Wherever possible and relevant, the Board will ensure consistency between Pillar 3 disclosure, Pillar 1 reporting and Pillar 2 ICAAP content e.g. disclosure about risk management practices and capital resources at year end.

Policy and approach

Pillar 3 disclosures are required for a consolidated group and for those parts of the group covered by the Basel II framework. Pending implementation of the Basel II framework by The Bank of New York Mellon Corporation, there is currently no comparable disclosure provided on a consolidated basis by the firm’s parent undertaking. As such, this disclosure has been prepared for the Luxembourg regulated entity.

Disclosure will be made annually based on calendar year end Regulatory submissions (i.e. Pillar 1) and the Annual Report i.e. as at 31st December and will be published as soon as practicable after this date. Unaudited data may be used in these disclosures and a suitable health warning will be inserted in the disclosure pack.

The Company will reassess the need to publish some or all of the disclosures more frequently than annually in light of any significant change to the relevant characteristics of its business including disclosure about capital resources and adequacy and information about risk exposure and other items prone to rapid change.

Disclosures will be published on The Bank of New York Mellon group website (www.bnymellon.com), see section Investor relations, Financial reports, Other regulatory filings on the Company’s website.

The Board at its discretion may omit one or more of the disclosures if the information provided by such disclosures is not regarded as material. The criterion for materiality used in these disclosures is that the firm will regard as material any information where omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions.

The Board at its discretion may omit one or more of the disclosures if those items include information that, in the light of requirements is regarded as proprietary or confidential. In this circumstance, the Board will state in its disclosures the fact that specific items of information are not disclosed and the reason for non-disclosure and will publish more general information about the subject matter of the disclosure requirement except where these are to be classified as secret or confidential.

The Company undertakes no obligation to revise or to update any forward looking or other statement contained within this paper regardless of whether or not those statements are affected as a result of new information or future events.

This policy will be periodically reassessed and updated in light of market developments associated with Pillar 3.

BNYM (Luxembourg) S.A.

Pillar 3 Disclosures for the year ended 31st December 2010

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1. Introduction

These 2010 Basel II Pillar 3 disclosures are about The Bank of New York Mellon (Luxembourg) S.A. ('BNYML') and are published in accordance with the requirements of the Commission de Surveillance du Secteur Financier ('CSSF') circular 06/273. Pillar 3 disclosures are made in respect of BNYML and its branch undertakings. BNYML implemented the Basel II Standardised Approach for calculating credit, market and operational risk on 1st January 2008. The Company first prepared Pillar 3 disclosures for year end 31st December 2008.

1.1. Purpose of Pillar 3

Basel II is the international banking accord intended to strengthen the measurement and monitoring of financial institutions' capital. The Basel II framework was implemented in the EU through the Capital Requirements Directive (CRD), which is now law. Basel II framework establishes a more risk sensitive approach to capital management and is comprised of three pillars:

- **Pillar 1** establishes rules for the calculation of minimum capital for Credit, Market and Operational Risk.
- **Pillar 2** is an internal discipline to evaluate the adequacy of the regulatory capital requirement under Pillar 1 and other non Pillar 1 risks. This pillar requires the CSSF to undertake a supervisory review to assess the robustness of BNYML internal assessment.
- **Pillar 3** complements the other pillars and effects market discipline through public disclosure. Expanded disclosure about capital and risk enables interested parties to better understand the risk profile of individual banks and to make comparisons.

1.2. Key events

There were no key events in 2010

2. Scope and Application of Directive Requirements

BNYML is a subsidiary of BNY International Financing Corporation which is, in turn, a subsidiary of The Bank of New York Mellon Corporation (BNYMC). In 2010 BNYML had one foreign branch, The Bank of New York Mellon (Luxembourg) S.A., Italian Branch (the "Branch").

BNYML provides custody services, fund administration, transfer agency services, depository services to open-ended investment companies as well as corporate trust services.

There were no instances during 2010 where Capital resources were less than the required minimum.

3. Risk Management Objectives and Policies

3.1. Risk Objectives

BNYML, through its operating entities seeks to proactively manage and minimise risks specifically, credit, operational, compliance, and business risks.

BNYML operates in the Asset Servicing and Issuer Services sectors of The Bank of New York Mellon Group (BNYM). The designated risk specialist for each Line of Business has been closely involved in the risk assessment processes (further described in the Internal Capital Adequacy Assessment Process (ICAAP)). The methodology applied in BNYML's current and prospective operations to identify risks and assess the quality of controls is driven by a specific self assessment that is overseen by independent Risk Management.

The Luxembourg Risk Committee and the BNYM EMEA (Europe, Middle East, and Africa) Risk Committee ('EMEA RC') have overseen this disclosure for recommendation to the Board of BNYML.

The ICAAP considers the above arrangements as a key input into its assessment of risk effectiveness.

BNYML considers that the regulatory capital treatments generally provide an adequate cushion to meet 'business as usual' risks or risks arising from stressed events. Daily capital adequacy and liquidity verifications and metrics are in place and reported to Senior Management.

3.2. Structure and Organisation of Risk Management

BNYM Luxembourg SA Board of Directors

The Board of Directors, in consultation with management and the internal auditors, is responsible for reviewing significant financial and other risk exposures and the steps Management has taken to monitor, control and report such exposures. The Board of Directors has adopted suitable policies and procedures in order to ensure that an appropriate level of risk management is directed at the relevant elements of its business.

The Board receives a summary of the profit and loss account as well as the balance sheet of the Bank at each Board Meeting. The Board also receives the daily capital adequacy and liquidity ratios in graphical form. All these reports are presented and commented on by the Chief Financial Officer.

Luxembourg Risk Committee

The Luxembourg Risk Committee acts as a formal governance committee overseeing the risk management activities of BNYML and acting on behalf of the Board of Directors in ensuring that risks are being managed in accordance with defined risk appetite and tolerances.

The committee meets monthly and is chaired by the General Manager of BNYML and includes all Risk Managers together with the Heads of operating departments as well as Legal, Compliance, Internal Audit, and Finance. It reviews all risk related matters as well as any issues which may impact on the Bank's ICAAP.

The following is reported and discussed during each risk committee: New clients / non-standard fund launches.

Risk items; Risk and control self assessment (status update and summary of outstanding action plans); Key risk indicators (KRIs); Quarterly high level risk assessment; Significant events; Significant business process change / New product; New risk identified that may have an impact on ICAAP calculation; Nostro account Reconciliations; Internal audit: Past due date action items and internal audit reports; Compliance monitoring: Compliance monitoring review reports; Legal updates; Finance: Capital adequacy ratio, Liquidity ratio, any large exposures which have occurred.

EMEA Risk & Compliance Committee

This committee meets monthly and is chaired by the EMEA Chief Risk Officer. The membership includes Heads of Business Lines, Risk Management, Finance, Internal Audit, Compliance, Legal and IT. The Committee receives regular reports from each control discipline summarising the key emerging risk issues. Risk issues emanating from Luxembourg are escalated to the EMEA Risk Committee as appropriate.

EMEA Executive Committee

The most senior European regional governance committee is the EMEA Executive Committee which also receives updates on the most material emerging risks across the region.

Roles and responsibility in managing risk:

It is the policy of the Bank to manage risk at the **Business Unit** and business process level. Each Business Unit is responsible for actively identifying, assessing and managing the risks it faces, and for the development of a Continuous Risk Management Process. The goal of the Bank's approach to Risk Management is to ensure that all material risks in each business line are defined, understood, and effectively managed using well-designed policies and controls.

General Management - Primary responsibility and accountability for risks and risk mitigation lies with the General Management. In fulfilling these obligations, management receive a series of reports which show:

- The actual monthly profit and loss accounts and balance sheets for the period;
- The performance of each line of business each month compared to budget;
- The daily capital adequacy ratio in graphical form;
- The daily liquidity ratio in graphical form.

A monthly forecast update is also sent to the General Management.

Each department manager receives a report detailing their revenues, costs and staff numbers as applicable, compared to budget for their department. They also receive the details of their departmental budget each year as soon as the budget is finalised.

A dedicated team within the Finance Department specialises in the production of these reports, as well as in the provision of ad hoc information and analysis.

The role of the **Risk Managers** is to ensure that risks are effectively managed and BNYM policies are implemented consistently throughout the Bank. They also assist the line of business with analysis, expertise, and problem solving as well as provide oversight.

Embedded Control Managers – An internal group within Operations, that work with the Operations Managers to ensure that control environment across all areas is sound and is meeting client needs. A key distinction between Embedded Control and the Risk Management function is that Embedded Control are resources provided by and reporting to the line of business. These resources can be focused by the business on any emerging risk issue eg reporting, investigation or control issue.

Risk Management and Compliance Sector are responsible for establishing overall policy and process framework for managing risk and approving any deviations from this Risk Management Framework or other Corporate Risk Management policies.

Internal Audit Department - responsible for providing reliable and timely information to the Board of Directors and Management regarding the Company's effectiveness in identifying and appropriately controlling Risks. Audit will review business practices against business policies and procedures to provide reasonable assurance that they are being followed. Audit will also independently review Risk and Control Self Assessments (RCSAs) to confirm that significant risks and control gaps have been identified and that appropriate action plans have been developed.

Compliance department - seeks to ensure that businesses maintain appropriate processes to comply with all applicable laws, regulations, bank policies and ethical practices.

Credit Risk Management - BNYM has adopted a regional approach to the risk management of credit, with a Credit Risk Management Team located in London having responsibility for the EMEA region (including Luxembourg). Credit Risk is managed in accordance with the policies of the wider BNYM group.

3.2.1. Credit Risk

Credit Risk covers the default risk on the balance sheet from counterparties or clients for loans, commitments, securities, receivables and other assets where realisation of the value of the asset is dependent on counterparties' ability to perform.

Credit risk is seen as relatively low, given a BNYML deposit focused liability driven balance sheet. No wholesale funding is currently required. The majority of funds are placed with banks within the BNYMC group. Daily net credit balances remain on Nostro accounts. The Bank is also exposed to several counterparties and has a relationship with many sub custodians. The firm does not have a trading book and does not have any derivatives in its banking book. Credit is not actively sold nor provided to clients to support operational activity. Client overdraft activity is rare and limited to situations where payments are to be covered by immediately available funds from a verified source. Payments against uncollected funds have the potential to cause overdrafts on an overnight basis. Intraday timing differences and processing errors can lead to such exposures, which need measuring and monitoring. Although it does not anticipate significant overdraft exposure on a routine basis, from time to time such events do arise and BNYML may find itself in a position of seeking recovery of funds paid out to third parties.

The Bank has established intraday payment credit lines with certain clients in order to facilitate the disbursement of a client's funds in BNYML accounts (whether in connection with cash payments or security transactions) to their investors prior to the credit of covering funds in the client's BNYML accounts. The Bank has either a contractually defined lien on assets or a guarantee from the promoter of the funds for most of the clients. The Bank has implemented the following monitoring and reporting process:

- Significant overdrafts are monitored daily by the DepotBank department.
- Large exposures (overdrafts amounting to more than 25% of the Own Funds) are monitored daily by Finance and escalated to Senior Management. They are reported as soon as possible to the CSSF.
- BNYM Network Management Brussels in conjunction with Credit Risk in New York performs Sub Custodian Review and provide appropriate feedback to BNYML in case of issues to report.

3.2.2. Market Risk

Market Risk is the risk to a firm's financial condition as a result of adverse movements in the market. BNYM defines it as the risk of potential valuation changes in foreign exchange and other derivative positions and in fixed income instruments, as well as venture capital and other equity investments.

Market risk is a systemic risk. Movements in markets are beyond the control of the Bank. Market risk to the Bank is reviewed below in two contexts: impact on the Bank's balance sheet and impact on the Bank's revenues and therefore profitability.

The Bank does not run a trading book and matches its interest rate risk on its non-trading book. The only unmatched interest rate risk in the Bank's books is for the fixed rate of interest payable on the subordinated debt capital provided by its parent.

The Bank is exposed to two types of market risk: (a) foreign exchange risk and (b) interest rate risk.

- a) The Bank's revenues are denominated in a mix of currencies whereas a high proportion of its costs are denominated in Euro. Apart from the risk of an operational execution error, the Bank is not significantly exposed to this risk. Foreign exchange risk in the Bank's non-trading book is managed by matching of assets and liabilities. Income received in foreign currencies is converted to EUR in a timely manner to avoid being exposed to currency risk.
- b) While the Bank has no significant Balance Sheet interest rate risk exposure. BNYML exposure to interest rate risk is principally related to interest earnings on its own cash deposits. The Bank seeks to earn competitive interest rates on the cash balances held but adopts a very low risk approach (on call deposits only). Its interest rate income is subject to the risk that when market interest rates tend toward zero, the Bank cannot pass all of the interest rate reductions to its clients (known as spread compression). The Bank does not run a trading book and matches its interest rate risk on its non-trading book. The only unmatched interest rate risk in the Bank's books is for the fixed rate of interest payable on the subordinated debt capital provided by its parent. Interest rate risk in the non-trading book is discussed in Section 11.

3.2.3. Operational Risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. BNYML is subject to a number of corporate policies relating to Operational Risk and the Risk Management Framework.

Operational Risk at BNYML is managed under the Risk Governance Framework. The level of BNYML's residual operational risk is managed through rigorous operating policies, procedures and controls set by the

Board and implemented by Operations and Risk Management.

BNYML business managers are responsible for risk control self assessment, which includes identification of the risks associated with key business processes, identifying and measuring the effectiveness of controls in place to manage risk and for remediation of any weakness. The Risk Manager oversees the output and recording of this assessment with support and approval of Senior Management.

The Board of BNYML monitors Operational Risks and the appropriateness of controls through the Management Committee and independent reporting from risk managers. This requires BNYML to update regularly its Risk and Control Self Assessment (RCSA), as well as monthly Key Risk Indicators (KRI) and prompt reporting of any significant financial impacts as a result of errors.

All internal risks are reviewed at least on a quarterly basis in partnership with the appropriate department heads of the firm and focus on the risks faced and the controls in place to manage or mitigate any crystallisation of risks. In parallel, Risk Management performs monitoring appropriate to the business and identified risks, which includes KRI reporting, significant event analysis and ad hoc reviews. Risk Management is also required to formally review the ICAAP at least annually. Moreover the key elements of the RCSA, internal control environment, monitoring and governance arrangements are routinely reviewed and challenged by the Risk Committee.

3.2.4. Liquidity Risk

Liquidity risk is the risk that a firm either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can only secure such resources at excessive cost.

In terms of global liquidity management, BNYMC enjoys a strong base of core client deposits for its funding which arises from its role as a leading asset custodian and trustee. BNYMC does not rely on either retail funding or wholesale funding in its business model. Asset/liability management is managed globally through treasury activities in key financial centres, such as New York, London and Brussels, and is driven by client cash needs and transactions.

BNYM firms are required to have in place robust strategies, policies, processes and systems to identify, measure, manage and monitor the liquidity risks to which they may be exposed, including intra-day risk.

Firms must have reliable management information to ensure appropriate and timely forward-looking information on the liquidity risk of the firm and early warning indicators to identify increases in liquidity risk.

BNYML will at all times maintain liquidity resources which are adequate both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met in full as they fall due.

Senior management is responsible for establishing appropriate liquidity risk tolerances; for approving, reviewing and updating the firm's approach to managing liquidity risk; and for reviewing the firm's liquidity position including compliance with the local rules and regularly reporting this information to the governing body.

BNYML falls under an EMEA Programme designed to ensure that the company complies with new or improved Liquidity risk management standards. This is an ongoing Programme of work which, with respect to BNYML is currently focused on upgrading governance standards.

BNYML does not have any collateral positions to manage, nor is it necessary to actively manage liquidity across legal entities, business lines or currencies. Metrics about each firm's liquidity position are reported to EMEA ALCO.

BNYML is self-sufficient within the group liquidity framework and complies with local capital and liquidity regulations. The Board of BNYML has approved a specific policy for liquidity risk management. BNYML maintains and monitors a daily liquidity ratio in accordance with CSSF circular IML 93/104. This ratio is reported to Senior Management and to the Board. Liquidity risk is seen as relatively low given that both client deposits and own cash are on call. There is thus no significant maturity mismatch.

3.2.5. Compliance Risk

Compliance Risk covers the impact on earnings or capital from violation, or non-conformance with laws, rules, regulations, prescribed practices or ethical standards which may, in turn, expose the firm and its executors to fines, payment of damages, the voiding of contracts and damaged reputation (with accompanying indirect costs).

The goal of BNYML's compliance process is to ensure that all compliance responsibilities, enterprise-wide, are defined, understood, and met effectively through well-designed policies and procedures, by knowledgeable and trained employees, and through effective controls, including appropriate assessment, testing and documentation of procedures and remediation of any weakness. The BNYML Compliance Officer presents a report to every Board meeting.

As a subsidiary of BNYMC, BNYML is subject to a number of corporate compliance policies and benefits from corporate wide training around compliance and ethics matters. An independent Compliance function oversees the operations within BNYML. The role of the Compliance function is to provide leadership, guidance, and oversight to help business units identify applicable laws and regulations and implement effective measures to meet the specific requirements, including the execution of a risk based compliance monitoring program, the results of which are escalated to senior management. Compliance takes a proactive approach by anticipating evolving regulatory standards and being aware of industry best practices, legislative initiatives, competitive issues, and public expectations and perceptions.

The Compliance function is part of a global compliance organisation which reports through the Head of International Compliance to the Chief Compliance and Ethics Officer for The Bank of New York Mellon Corporation. The Chief Compliance and Ethics Officer reports to the Chief Risk Officer, is a member of all critical committees of BNYMC and provides regular updates to the group Audit & Examining Committee of the Board of Directors.

3.2.6. Business Risk

Business risk is the risk of loss that the business environment poses to the firm's profitability. It normally consists of items such as changes in the external macro environment or client behaviour, inappropriate management actions, performance of competitors, etc.

Business risk for Asset Servicing sector is mainly driven by the fact that fees are significantly based on clients' Net Asset Value for Fund Accounting and Custody. As business risk is difficult to assess, it has been defined as the residual risks that confronts the firm, after taking all the known and quantifiable risks into consideration.

3.2.7. Outsourcing Risk

The risk that failure in respect of the provision of services by third party provider(s) that could potentially damage an entity's operations, or if contracts with any of the third party providers are terminated, that the entity may not be able to find alternative providers on a timely basis or on equivalent terms.

BNYML's operating model is largely based on utilizing The BNY Mellon Group's operating hubs of excellence in Ireland, Manchester, Pune, Everett and New York (for Fund Accounting), in Brussels (for Custody), and in Singapore (sub transfer agency services for some funds distributed in Asia) to which BNYML has delegated certain operational and administrative tasks.

There are two areas of outsourcing for BNYML: Information Technology (IT) outsourcing and general business process outsourcing (mainly Custody and Fund Accounting).

Business process outsourcing could create a number of dependencies on other BNYM entities from an operational standpoint (see operational risks 3.2.3).

In addition to the operational risks related to the outsourcing, there is also a regulatory risk for the Depositary in the context of its supervision role over the Luxembourg funds. This regulatory risk is most likely to increase further to the introduction of more stringent regulation such as the AIFM directive.

BNYML also places substantial deposits with The Bank of New York Mellon SA/NV (BNYM SA/NV) and therefore is exposed to credit concentration Risk.

Several controls and mitigants exist for the entities where business processes are being outsourced:

- SLAs or inter-company agreements are in place with delegates;
- KPIs are identified to measure performance;
- Entities are regulated and covered under SAS 70 reports or equivalent. These reports are used to perform due diligence on service providers;

- The entities maintain proper disaster recovery and business continuity plans, subject to yearly testing;
- The same technology (including system connectivity) is used across locations;
- Risk, compliance and audit resources are allocated to the ongoing monitoring of the performance;
- Staff must meet BNYM's corporate requirements in terms of behaviour, knowledge and training.

The Depot Bank team relies on BNYM's Network Management to perform thorough initial as well as ongoing due diligence on BNYM's sub-custodians. Significant exceptions that the Network Management team comes across during their due diligence reviews are brought to the attention of the Depot Bank team. In case of any material issues with existing sub-custodians, Network Management ensures they are resolved and keeps Depot Bank updated until either the issue is resolved or the sub-custodian is replaced. The BNYM Depot Bank / Trustee business line also meets the BNYM Global Network Management team on a yearly basis as part of the yearly due diligence visit.

The Depot Bank department reviews the result of the asset reconciliations back to the sub-custodians or correspondent banks as performed by the dedicated reconciliation teams in various operational centers such as London, Brussels, Pittsburgh, Pune, etc.

BNYML also performs other custody oversight controls (eg. Monitoring sub-custodian's network, Review of asset and cash breaks, Collateral monitoring, Monitoring free deliveries, Reconciliation against third party position statement, Checking failed trades, Review of past due / aged income payment, corporate actions and tax reclaims);

3.3. Scope and Nature of Risk Reporting Systems

The purpose of the company's risk measurement and reporting systems is to ensure that all risks and exposures are comprehensively captured, with all of the attributes necessary to support robust decision making by senior management and risk mitigation within approved risk appetite levels.

Risk measurement and reporting systems are subject to a robust governance framework, to ensure that their design is fit for purpose and that they are functioning properly and that controls are effective. The operation and development of risk rating and management systems and processes are subject to oversight by various levels of management up to the Board of Directors.

The measurement and monitoring of the major risks encountered by the company including operational risks, are increasingly delivered by central systems or, where for sound business reasons this is not the case, through structures and processes that support comprehensive oversight by senior management.

There is regular reporting on risk to business line management, to specialist functions and to the senior management of the company.

All of BNYML activities are included in the Basel II COREP capital reporting (credit and market risk Standardised approach). Operational Risk data is captured on internally developed risk management systems.

3.4. Governance, Policies & Risk Management Structure

Policies and procedures in place to govern and manage the business are common to all BNY Mellon entities. Suitable policies and procedures have been adopted by BNYML to ensure that an appropriate level of risk management is directed at each element of the business.

The Board has both governance and decision making functions. In the opinion of the Board, such arrangements and independent oversight activities are adequate for the effective management of risks to the business.

The Risk Management organisation is based on a tiered approach, including Corporate, Sector, Line of Business and risk specialists (e.g.: credit risk). Within the EMEA region there is a further EMEA Risk Management oversight layer whose responsibilities include ensuring that Line of Business implement policies and procedures on a consistent basis.

The Board has delegated to the Executive Management, supported by the Luxembourg and EMEA Risk Committees, oversight of Risk Management, while retaining ownership and responsibility. To further strengthen this framework, Embedded Control Managers working closely with business line management oversee day-to-day risk management controls, monitor the Key Risk Indicators and oversee the effective management of operational events. As a global business, BNYMC organises its activities into sectors eg: Asset Servicing. Each

Sector has its own independent risk management arrangements covering, amongst others the implementation of corporate risk policies and processes that identify risk.

The Board meets at least three times a year and receives reports from Risk Management, Compliance, Finance and Audit to evaluate the effectiveness of the existing control environment and ensure that they are being actioned effectively and in a timely manner. In the opinion of the Board of Directors such arrangements and monitoring activities are adequate for the effective operation of the businesses in Luxembourg. A special Board meeting is also convened annually to specifically review BNYML's Pillar 3 Disclosures.

4. Capital Resources

During the year ended 31st December 2010, BNYML complied with all of the externally imposed capital requirements to which it was subject.

The following table summarises the composition of the BNYML regulatory capital as reported to the CSSF as at 31st December 2010. The Company does not have any Innovative Tier 1 capital nor Tier 3 capital as at 31st December 2010 (31st December 2009: nil).

Capital resources	2010	2009 ¹
	EUR 000's	EUR 000's
Tier 1 capital		
Called up share capital	43,701	43,701
Retained earnings and other reserves	3,904	7,648
Net (loss) / profit	(1,991)	(3,744)
	45,614	47,605
Deductions from Tier 1 capital		
Intangible assets –goodwill	(3,427)	(3,427)
Total Tier 1 capital after deductions	42,187	44,178
Tier 2 capital		
<i>Upper Tier 2 instruments</i>		
Loan capital perpetual subordinated debt	31,130	31,130
	31,130	31,130
Total Tier 2 capital	31,130	31,130
Total capital resources after deductions	73,317	75,308

¹ 2009 audited figures are used in these disclosures

5. Capital Requirements and Adequacy

The Board through setting its risk appetite and focusing on risk assessment evaluates its current and projected capital requirements, under business as usual or stress conditions.

As part of the Pillar 2 Internal Capital Adequacy Assessment Process (ICAAP) in 2010 the main sources of risk have been identified, assessed (*impact & likelihood* methodology) and approved by the relevant senior managers after taking into account the mitigating controls and rationale for direction of risk, in light of the risk appetite set by the Board.

The following table summarises the BNYML capital requirements by exposure class and capital adequacy surplus as at 31st December 2010.

Exposure class	2010 Gross exposure	2010 Mitigat -ions ²	2010 Net exposure	2009 Gross exposure	2009 Mitigat -ions	2009 Net exposure
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Credit risk – Standardised approach						
Institutions	21,342	0	21,342	18,271	(13)	18,258
Corporates	1,564	(210)	1,354	369	(14)	355
Collective Investment Undertakings	0	0	0	0	0	0
Other Items ³	1,052	(56)	996	580	(3)	577
Total	23,958	(266)	23,692	19,220	(30)	19,190

Operational Risk - Standardised approach ⁴	3,636	3,066
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Market risk ⁵

Foreign currency Position Risk Requirement	254	0
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Total Market Risk capital requirements	254	0
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Total Pillar 1 capital requirements	27,582	22,256
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Total Pillar 1 capital surplus	45,735	53,052
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Capital adequacy ratio (%)

Capital resources / capital requirements (compared to 100%)	265.75%	338,75%
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Solvency ratio (%)

Capital resources / capital requirements (compared to 8%)	21.26%	27.07%
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There were no retail or material equity exposures as at 31st December 2010 (31st December 2009: nil).

² These amounts are liens on client cash accounts held with BNYML.

³ Other items Capital requirement is predominantly in respect of Other accruals and prepayments.

⁴ The Standardised approach has been adopted for Operational risk. The capital charge for each business line is calculated by multiplying gross income by a factor (denoted Beta). See Section 9.

⁵ The Company does not carry out any trading activities and therefore does not allocate capital for market risk exposure apart from foreign exchange risk. The foreign exchange risk capital charge is based on historic foreign currency balances using the calculation required by the CSSF.

6. Counterparty Credit Risk

Counterparty credit risk (CCR) in the context of Pillar 3 disclosure is the risk that a counterparty to a derivative contract recorded in either the Trading Book or Banking Book could default before settlement of the transaction's final cash flows. As at 31st December 2010, BNYML did not have a Trading book and did not have any derivatives in a Banking book and therefore no further disclosure is required (31st December 2009: nil).

7. Credit Risk and Dilution Risk

7.1. Structure

There are two principle types of Credit Risk counterparties:

Banks

- **BNYMC Group banks and third party banks**

BNYML places its cash with other BNYMC Group banks and with certain other third party banks.

Clients

- **Daylight (intraday) Overdrafts**

Daylight overdraft limits are usually set for each client as a percentage of a client's assets under custody (subject to certain maximum levels); currently manual checks are made as to the validity of payments. As appropriate, payments are referred for approval, or otherwise, depending on circumstances. In instances where assets are not held in custody, a manual fixed limit may be agreed, if appropriate, after due consideration by an appropriate Credit Officer; again payments are subject to manual checks, prior to payment.

These arrangements allow clients to access proceeds of sales, or other expected funds, even though in many markets the proceeds are not formally received until late in the day.

- **Overdrafts**

BNYML recognises that overdrafts can occur for operational reasons and monitors such exposures closely to ensure underlying causes are investigated and understood so that repayment is effected swiftly.

BNYML does not, as a matter of course, provide advised overdraft facilities. Should such a need materialise, BNYML would make full use of its parent's expertise in securities-related lending, with each request being considered individually by specialist analysts in relation to the make up of the portfolio, amount requested, percentage of assets value requested and other factors. Approval would be in the hands of a totally independent Credit Officer, with specialist understanding of the collective funds/investment industry.

Client overdraft credit risk is mitigated by the existence of guarantees or liens on client assets.

A daily significant overdraft report is reviewed and any issues are escalated to Senior Management.

BNYML does not engage in hedging its Credit risk as it believes the policies in place are sufficient to ensure adequate credit quality. Should the situation arise where this became necessary, BNYML could call upon the expertise of its parent in these matters.

7.2. Credit risk exposure under Basel II

Credit exposure is computed under the Standardised approach. This method for calculating credit risk capital requirement uses supervisory risk weights.

7.2.1. Exposure

Except where stated, exposure is defined as **Exposure at Default (EAD) pre Credit Risk Mitigation (CRM)** i.e. a regulatory exposure value after the application of Credit Conversion Factors (CCF) for off balance sheet items (including undrawn commitments) and, after netting but before application of Credit Risk Mitigation factors (eg property, other physical collateral). The calculation of EAD therefore takes into account both current exposure and potential drawings prior to default over a 12 month time horizon. As such, Exposure in this context may differ from statutory GAAP accounting balance sheet carrying values.

i. Standardised gross Credit exposure (EAD pre CRM)

Standardised exposure classes	Total Exposure At Default pre CRM at 31st December 2010	Total Average Exposure At Default pre CRM at 31 st December 2010	Total Exposure At Default pre CRM at 31 st December 2009	Total Average Exposure At Default pre CRM at 31 st December 2009
	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central governments & Central banks	323,931	109,268	18,975	21,211
Institutions	1,333,863	1,437,154	1,141,286	1,056,670
Corporates	19,549	64,230	4,651	20,429
Collective Investment Undertakings	0	0	0	0
Other items	13,154	11,939	7,223	12,601
Total	1,690,497	1,622,591	1,172,135	1,110,911

Standardised exposure classes are defined by the CSSF.

Other items principally comprises Trade and other debtors, interest and accounts receivable and prepayments.

Average exposure is based on the 2010 quarterly Capital adequacy reporting.

ii. Standardised gross Credit exposure (EAD pre CRM) by geographic area

As at 31st December 2010

Standardised exposure classes	Luxembourg	Europe, Middle East & Africa	North America	Asia Pacific	Total
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central governments & Central banks	28,337	295,594	0	0	323,931
Institutions	14,992	1,282,088	31,769	5,014	1,333,863
Corporates	19,541	8	0	0	19,549
Collective Investment Undertakings	0	0	0	0	0
Other items	10,560	2,594	0	0	13,154
Total	73,430	1,580,284	31,769	5,014	1,690,497

Geographic distribution is based on the domicile of the borrower or obligor.

As at 31st December 2009

Standardised exposure classes	Luxembourg	Europe, Middle East & Africa	North America	Asia Pacific	Total
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central governments & Central banks	14,917	4,058	0	0	18,975
Institutions	6,939	1,121,513	7,036	5,798	1,141,286
Corporates	4,575	76	0	0	4,651
Collective Investment Undertakings	0	0	0	0	0
Other items	5,675	1,498	50	0	7,223
Total	32,106	1,127,145	7,086	5,798	1,172,135

Geographic distribution is based on the domicile of the borrower or obligor.

iii. Standardised gross Credit exposure (EAD pre CRM) by Industry sector

As at 31st December 2010

Industry sector	Central governments & Central banks	Institutions	Corporates	Collective Investment Undertakings	Other items	Total
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central & local government	323,931	0	0	0	0	323,931
Banks & Other financial	0	1,333,683	19,549	0	12,969	1,366,381
Other individual Loans & Advances	0	0	0	0	185	185
Total	323,931	1,333,863	19,549	0	13,154	1,690,497

Industry sectors are based on the CSSF economic classification of the counterparty.

As at 31st December 2009

Industry sector	Central governments & Central banks	Institutions	Corporates	Collective Investment Undertakings	Other items	Total
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central & local government	18,975	0	0	0	0	18,975
Banks & Other financial	0	1,141,286	4,651	0	7,100	1,153,037
Other individual Loans & Advances	0	0	0	0	123	123
Total	18,975	1,141,286	4,651	0	7,223	1,172,135

Industry sectors are based on the CSSF economic classification of the counterparty.

iv. Standardised gross Credit exposure (EAD pre CRM) by residual maturity

As at 31st December 2010

Exposures are allocated to maturity bands based on the residual contractual maturity dates and not expected or behaviourally adjusted dates.

Standardised exposure classes	On demand	Up to 1 year	Over 1 year and up to 3 years	Over 3 years and up to 5 years	Total
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central governments & Central banks	323,931	0	0	0	323,931
Institutions	1,333,863	0	0	0	1,333,863
Corporates	19,549	0	0	0	19,549
Collective Investment Undertakings	0	0	0	0	0
Other items	12,969	75	79	31	13,154
Total	1,690,312	82	73	30	1,690,497

As at 31st December 2009

Standardised exposure classes	On demand	Up to 1 year	Over 1 year and up to 3 years	Over 3 years and up to 5 years	Total
	EUR 000's	EUR 000's	EUR 000's	EUR 000's	EUR 000's
Central governments & Central banks	18,975	0	0	0	18,975
Institutions	1,141,286	0	0	0	1,141,286
Corporates	4,651	0	0	0	4,651
Collective Investment Undertakings	0	0	0	0	0
Other items	7,100	61	56	6	7,223
Total	1,171,334	61	56	6	1,172,135

Exposures are allocated to maturity bands based on the residual contractual maturity dates and not expected or behaviourally adjusted dates.

7.3. Impaired and Past due assets and Provisions

For BNYML, specific provisions are made against loans and advances when, in the opinion of the Directors, recovery in full is doubtful. A general provision is made to cover bad debts that have not been separately identified at the balance sheet date but are known to be present in client receivables. Specific and general statistical provisions are deducted from loans and advances. Loans and advances and suspended interest are written off in part or in whole when there is no realistic prospect of recovery.

As at 31st December 2010, BNYML has no material impaired assets for which a specific or general provision has been raised (31st December 2009: nil). There were no material assets past due greater than 90 days. BNYML did not incur any material write-offs of bad debts or make any recovery of amounts previously written off during the year to 31st December 2010 (31st December 2009: nil).

7.4. Pillar 1 Credit Risk Standardised Approach

Credit exposure is computed under the Standardised Approach. BNYML does not use external credit assessments provided by Fitch, Moody's, and Standard and Poor's (ECAIs) to determine the risk weighting of exposures in its portfolios depending on counterparty type and coverage. In accordance with CSSF circular 06/273 Part VII, and given that all cash balances with institutions are on call, these balances are allocated a 20% risk weighting. Client overdrafts are largely allocated a 100% risk weighting.

7.5. Credit Risk Mitigation

BNYML does not typically hold collateral to mitigate credit risk exposure in respect of banks. For clients, the standard custody agreement gives a lien over custody assets including equities, bonds, gilts; or guarantees. As at 31st December 2010, BNYML did not apply any financial collateral, third party guarantees, credit derivatives or other collateral as credit risk mitigation within the Pillar 1 calculation (31st December 2009: nil).

8. Market Risk

The majority of market risk exposure relating to BNYML business is borne by its clients.

BNYML does not take trading positions and therefore does not have market risk exposure apart from foreign currency position risk arising from day to day activities.

BNYML has limited tolerance for market risk and the Bank does not run a trading book and matches its interest rate risk on its non-trading book.

Foreign exchange risk in the Bank's non-trading book is managed by matching of assets and liabilities.

Other than the fact that a high proportion of the bank's costs are denominated in Euro, but its revenues are denominated in a mix of currencies; and apart from the risk of an operational execution error, the bank is not significantly exposed to this risk.

9. Operational Risk

For the purposes of calculating a Pillar 1 capital charge under the Basel II Standardised Approach it has been determined that BNYML falls under the Agency Services Basel business line. The standard indicator approach for operational risks sets out a 15% risk rate for a single indicator that is determined by the sum of net interest income and net non interest income. For the ICAAP, the operational risk is based on a 3 year projection.

For Pillar 2, Operational Risk regulatory capital is calculated using BNY Mellon's Operational Risk capital model. The corporate model is based on a Loss Distribution Approach (LDA), one of the methodologies recognized under the Basel II Advanced Measurement Approach, currently used by BNY Mellon in the US. In the LDA model, loss frequency and loss severity distributions are separately estimated from historical loss data and then combined by using Monte Carlo simulation to generate a loss distribution.

This methodology was recently applied to BNYML in two major steps:

1. Produce consolidated quantitative Operational Risk capital charge for BNYML estimate based on an LDA model for BNYML that uses the same framework as the corporate LDA model.

2. Validate the BNYML LDA model output by quantitative and qualitative analysis of high impact low frequency scenarios specific to BNYML business activities.

BNYML has set extensive Operational risk policies that have been adopted by BNYML. Risk Management governance and oversight is organised on a global platform and within Europe at both the country and sector levels. Risk managers embedded within the operating entities work closely with business line management to identify risks, monitor key risk indicators and record and evaluate any operational events that arise.

Corporate Risk Management has developed the methodology that supports the risk assessment process. The Board has approved the methodology as a basis of input into the Pillar 2 processes. Independent Sector Risk Managers, in conjunction with the Business management, are responsible for advising on the completion and findings of the risk self assessment process.

The self-assessment process is aligned against global sector lines of business. BNYML operates within the Asset Servicing and Issuer Services sectors. The performance of self-assessment by line of business is recorded on a globally maintained platform. Platforms also capture key risk indicators and operational risk events (losses, gains and near misses). Business managers are responsible for performance of self-assessment, which is identifying the risks associated with key business processes, identifying and assessing the quality of controls in place to mitigate risk, and assigning accountability for maintaining the effectiveness of those controls and remediation of any weakness. The Risk Managers oversee the output and recording of this assessment with support and approval of Senior Management.

The objective of operational risk management is to prevent or minimise:

- Errors and service delivery failures, especially those with impact on customers
- Financial Losses or near miss events
- Compliance Breaches
- Reputation Damage.

Insurance for the purpose of mitigating Operational Risk - This disclosure is not relevant since BNYML does not use the Basel II Advanced Measurement Approach for the calculation of an operational risk capital requirement for Pillar 1 calculation but only for Pillar 2 calculation.

10. Non-trading book exposures in equities

BNYML did not have any non-trading book exposures in equities as at 31st December 2010 (31st December 2009: nil).

11. Interest Rate Risk in the non-trading book

The CSSF Circular 08/338 stipulates that banks must submit their non-trading book activities to a stress test on interest rate risk. This test shows the extent to which interest rate risk is likely to result in a decline in the economic value of the institution by more than 20% of its own funds.

The Bank has performed this analysis and has concluded that no capital is required to cover interest risk on its non-trading book activities. The Bank does not run a trading book and matches its interest rate risk on its non-trading book. The Bank has no material assets and liabilities subject to interest rate risk. The only unmatched interest rate risk in the Bank's books is for the fixed rate of interest payable on the subordinated debt capital provided by its parent.

While the bank has no significant Balance Sheet interest rate risk exposure, its interest rate income is subject to the risk that when market interest rates tend toward zero, the Bank cannot pass all of the interest rate reduction to its clients (known as spread compression).

12. Securitisation

As at 31st December 2010, BNYML did not have any securitisation risk weighted exposure calculated under CSSF circular 06/273 Part X (31st December 2009: nil). During the year ended 31st December 2010, BNYML was not active as originator or sponsor of any traditional or synthetic securitisation including securitised revolving exposures. As a result, at 31st December 2010 there were no impaired or past due assets previously securitised or associated gains or losses recognised during the year (31st December 2009: nil). BNYML did not have any investments in third party securitisations on its balance sheet at 31st December 2010 (31st December 2009: nil).

13. Glossary of terms

The following terms are used in this paper

- **ALCO** Asset and Liability Committee
- **Basel II** The June 2006 capital adequacy framework issued by the Basel Committee on Banking Supervision in the form of the 'International Convergence of Capital Measurement and Capital Standards'.
- **CCF** Credit Conversion Factor
- **CCR** Counterparty Credit Risk
- **CRD** Capital Requirements Directive
- **Credit risk mitigation** A technique to reduce the credit risk associated with an exposure by application of credit risk mitigants such as collateral, guarantees and credit protection.
- **Derivatives** A derivative is a financial instrument that derives its value from one or more underlying assets, for example bonds or currencies.
- **Exposure** A claim, contingent claim or position which carries a risk of financial loss.
- **Exposure at default (EAD)** The amount expected to be outstanding, after any credit risk mitigation, if and when a counterparty defaults. EAD reflects drawn balances as well as allowance for undrawn amounts of commitments and contingent exposures.
- **Exposure value** Exposure at default (EAD).
- **Institutions** Under the Standardised approach, Institutions are classified as credit institutions or investment firms.
- **Internal Capital Adequacy Assessment Process (ICAAP)** The Group's own assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints.
- **Residual maturity** The period outstanding from the reporting date to the maturity or end date of an exposure.
- **Risk appetite** A definition of the types and quantum of risks to which the firm wishes to be exposed.
- **Risk Governance Framework** The BNYML risk governance framework has been developed in conjunction with BNY Mellon requirements. Key elements of the framework are:
 - Formal governance committees, with mandates and attendees defined
 - Clearly defined escalation processes, both informally (management lines) and formally (governance committees, board, etc)
 - A clear BAU process for identification, management and control of risks
 - Regular reporting of risk issues
- **Securitisation** A transaction or scheme whereby the credit risk associated with an exposure, or pool of exposures, is tranching and where payments to investors in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures. A traditional securitisation involves the transfer of the exposures being securitised to an SPE which issues securities. In a synthetic securitisation, the tranching is achieved by the use of credit derivatives and the exposures are not removed from the balance sheet of the originator.
- **Standardised approach** In relation to credit risk, a method for calculating credit risk capital requirements using external credit assessment institution ratings and supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines.

14. Contacts

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