Butterfield

The Bank of N.T. Butterfield & Son Limited
65 Front Street, Hamilton, Bermuda

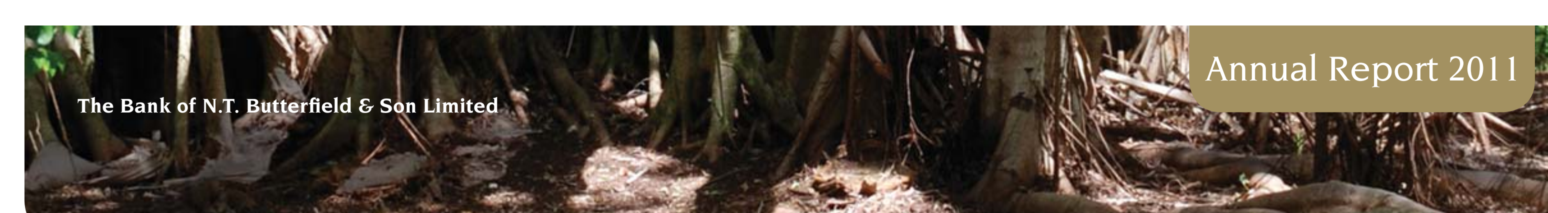
www.butterfieldgroup.com

Butterfield

Annual Report 2011

A Foundation for *Growth*

Butterfield



Cover: Banyan tree, Hamilton Parish, Bermuda

About Butterfield

Butterfield is a diversified financial services Group operating in seven jurisdictions. We have total assets of $8.8 billion and $71.7 billion of client assets under administration. We employ over 1,300 people around the world. The parent company, The Bank of N.T. Butterfield & Son Limited, is a publicly traded company with a primary share listing on the Bermuda Stock Exchange and a secondary listing on the Cayman Islands Stock Exchange. Additional information can be obtained from our website, **www.butterfieldgroup.com.**

"Butterfield is pursuing a strategy that will continue to strengthen the company and promote its long-term growth."

CHAIRMAN'S LETTER TO THE SHAREHOLDERS

I am pleased to report that Butterfield returned to profitability in 2011, producing net income of $40.5 million and delivering operating profits in each quarter. The Bank's 2011 income is modest by historical standards, reflecting a period of protracted economic dislocation and low interest rates. Against that backdrop, the Bank's financial performance in 2011 should be viewed as an important accomplishment and evidence that the Bank is on a solid financial base following an extremely difficult period.

Butterfield was adversely impacted during the global financial crisis by investments in troubled asset-backed securities and the non-performance of certain loans. In response, the Bank raised $750 million of new capital during 2009 and 2010, and over the past two years, has deployed that capital to de-risk the Balance Sheet and enhance business systems and structures. The resulting dilutive impact of the recapitalisation on legacy Shareholders' ownership was severe, but the actions taken to address underperforming assets, improve the Bank's operating infrastructure and control costs have created a foundation for rebuilding Shareholder value. Butterfield is pursuing a strategy that will continue to strengthen the company and promote its long-term growth.

During 2011, Butterfield paid dividends totalling $16 million on outstanding Preference Shares. Consistent with the Board's view that the distribution of profits should be suspended until such time as the Bank is generating sufficient income to allow for a meaningful per-Share dividend, no dividends were declared or paid on Common Shares in 2011. Holders of Contingent Value Convertible Preference Shares ("CVCP Shares"), issued in 2010 as part of our rights offering, were eligible for certain distributions in connection with the sale or public offering of the Bank's equity interest in fund administrator Butterfield Fulcrum Group Limited ("BFG"). In the second quarter, the Bank completed the sale of its minority interest in BFG, resulting in a distribution of $3.3 million (or $0.42 per CVCP Share).

I committed to Shareholders that, following the recapitalisation, we would work to accomplish an orderly transition of the Board to provide continuity of experience. As part of this transition I have advised the Board that I will retire as a member of the Board and Chairman effective at the close of the 2012 Annual General Meeting. Robert Steinhoff, Vice Chairman, has similarly announced his retirement from the Board effective at the close of the 2012 Annual General Meeting.

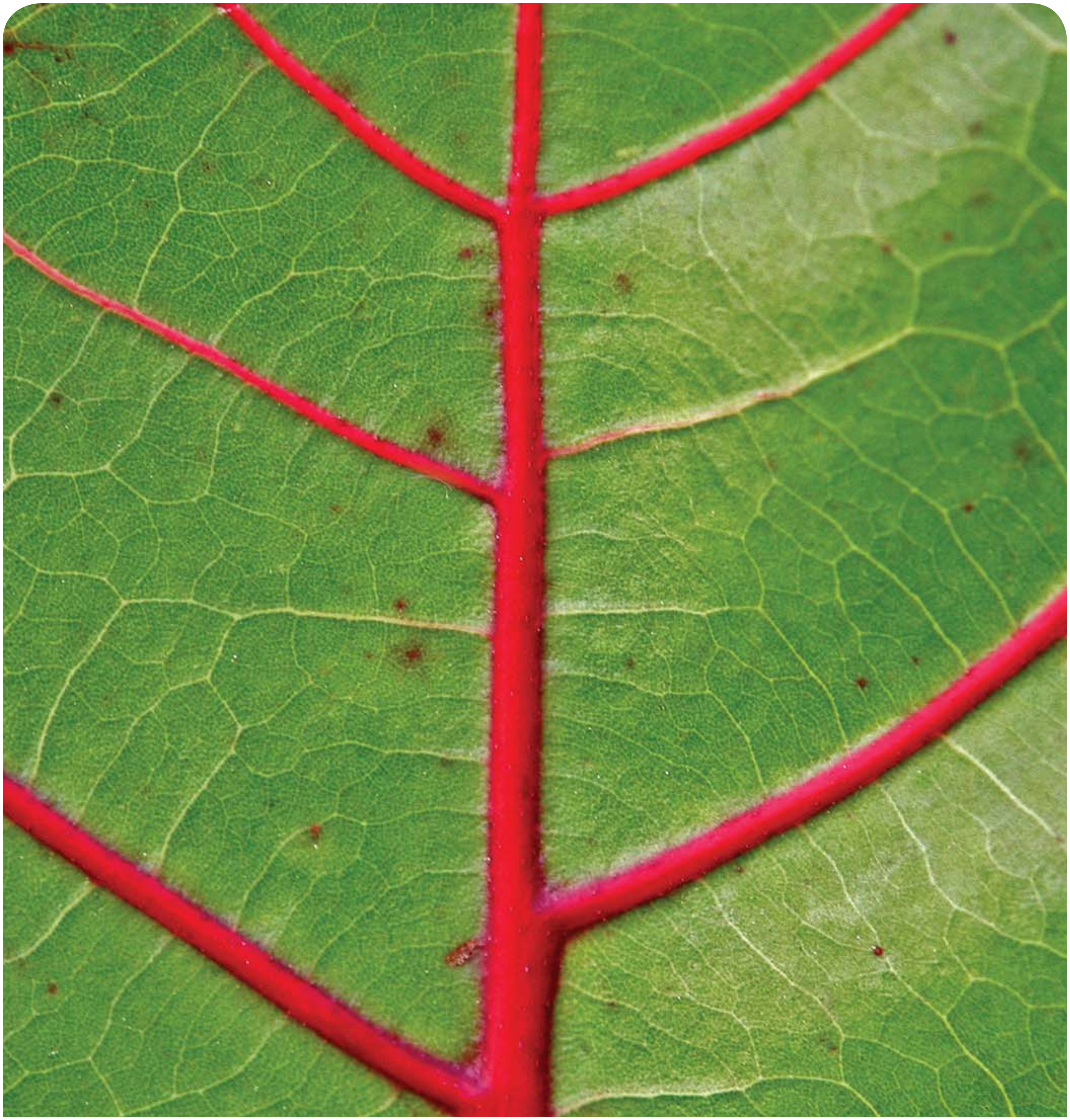
Subject to his election to the Board, the Directors intend to appoint Brendan McDonagh to the position of Executive Chairman of the Bank. Mr. McDonagh is a career banker with more than 30 years of international experience in consumer finance, retail and commercial banking and wealth management. His knowledge and experience will be advantageous to the Board as it works to continue to move the Bank forward on its current, profitable trajectory.

The Board transition also saw Barclay Simmons join as a Director in April 2011, filling the vacancy created by the earlier resignation of Julian Francis. Additionally, Victor Dodig replaced John Orr as one of CIBC's nominees to the Board in August. James Burr, whose term as a Director expires in 2012, will not stand for re-election. Olivier Sarkozy is nominated to replace Mr. Burr as one of Carlyle's two nominees to the Board.

It has been my honour to have been a member of the Board for the past 15 years and Chairman since February 2008; unfortunately the beginning of the financial crisis and the toughest years in Butterfield's 154-year history. I have had the opportunity to work closely with many talented Directors and the Bank's dedicated employees. I believe that the Bank, its employees and the communities we serve are in an excellent position following the Bank's recapitalisation.

I extend my sincere best wishes to Mr. McDonagh. I am confident that, under his leadership, the Board will continue to successfully rebuild value for the benefit of Butterfield Shareholders.

Robert A. Mulderig
Chairman of the Board



"We have realigned our resources to areas with greater growth potential..."

PRESIDENT & CHIEF EXECUTIVE OFFICER'S REPORT

2011 was a year of transition for Butterfield; one in which we continued to build a foundation for future growth. Our focus was on enhancing profitability, maintaining and further strengthening our Balance Sheet and investing in our core businesses of community banking and wealth management.

ENHANCING PROFITABILITY

Despite a difficult operating environment for banks, with low interest rates and depressed demand for some services, Butterfield generated net income of $40.5 million for the year, with four profitable quarters.

Revenue was up by $30.5 million versus normalised 2010 figures. Contributing substantially to our 2011 earnings was an increase in net interest income before provisions for credit losses of $34.8 million. The Bank's net interest margin increased by 47 basis points to 2.50% in 2011.

As a result of streamlining certain processes, the introduction of new technology and a reduced demand for some services, headcount was reduced by 135 across the Group.

Butterfield had no significant investment losses and recognised no other-than-temporary impairments on investments during 2011, having dealt decisively with its problematic assets following the capital raise in 2010. Charge-offs against loans were $23.8 million in 2011 amidst ongoing economic challenges (compared to $107.9 million in 2010).

STRENGTHENING THE BALANCE SHEET

As a result of ongoing diligence with respect to the quality of investments and loans we make, our Balance Sheet was further strengthened in 2011.

Total assets decreased by $799 million to end the year at $8.8 billion, the year-on-year decrease owed primarily to fluctuations in hedge fund deposits and some loss of non-core deposits that migrated to institutions paying higher interest. Average deposits for 2011 decreased by $356 million versus 2010. The Bank's core deposits, consisting primarily of demand deposits and savings deposits, remained stable.

The Bank also remained in a very liquid position, with the percentage of assets held in cash, cash equivalents, short-term investments and investments totalling 46.5% at year end.

Reflective of our conservative investment stance, the Bank sought to limit its exposure to the debt crisis in Europe and actively reduced its exposure to Continental Europe in the fourth quarter.

Although we have seen an increase in the incidence of delinquencies in loan and mortgage payments, the increase is commensurate with the general economic decline. Non-accrual loans as a percentage of total loans declined to 2.8% at the end of 2011 from 3.9% in 2010, whilst non-performing assets as a percentage of total assets was 1.7%, a reflection of the transfer of $27.4 million of non-accrual loans to the "Other Real Estate Owned" category in settlement of certain commercial loans and foreclosed residential property. The Bank employs conservative standards in its lending activities and, during these challenging times, has exercised flexibility with customers who are experiencing difficulty in repaying loans on the original terms.

Through our private banking businesses in Guernsey and the United Kingdom, we began targeting under-served segments of the lending market in 2011, increasing residential lending to high net worth clients who purchased prime Central London properties. The addition of these high quality assets, in combination with the extension of additional credit facilities to the Government of Bermuda, contributed to an increase in the loan portfolio of $200 million during the year. Loans represented a conservative 48.1% of total assets and 57.4% of customer deposits at year end.

CAPITAL

During 2011, the Bank's capital position improved from already-strong 2010 levels. The Tier 1 capital ratio was 17.7% at year end, and the total capital ratio stood at 23.5%, well ahead of both industry norms and regulatory minimums. Butterfield's tangible common equity ratio was 6.6% and the tangible total equity ratio was 8.9% at 31 December 2011.

INVESTING IN OUR CORE BUSINESSES

During the year, the Bank completed a three-year project to convert its core banking systems in Bermuda and the Cayman Islands to a new Oracle platform managed by HP. The new systems replace software that was beyond its service life and provide the Bank with a state-of-the-art platform. They allow the Bank to improve stability, risk management and customer service. With the same banking platform in place in our two largest jurisdictions, we also have more opportunities to gain efficiencies from the synchronisation of processes and product line ups moving forward.

We realigned our trust businesses across the Group under a centralised reporting structure in 2011. Bob Moore, who was previously Managing Director of our Guernsey bank, took on the role of Head of Group Trust in July and is working to harmonise our offerings and approach to the marketing and delivery of fiduciary services across the Group. Work continues on installing new systems for our Group trust businesses in key jurisdictions.

Michael Neff, Head of Group Asset Management, who joined Butterfield in early 2011, is working to strengthen and grow the asset management offerings across the Group. Our asset management strategy involves the rationalisation of the Butterfield Fund line up, partnering with third-party investment managers to deliver new products and tailoring products and services to clients' life stages and advisory requirements.

During the year, we introduced a managed portfolio service and an online brokerage service in Bermuda—the first of its kind in the jurisdiction—making a wide range of US exchange-traded securities available to self-directed retail investors. The online brokerage service will continue to be expanded to include third-party funds. For institutional clients, we introduced the BNY Mellon Butterfield Income Advantage Fund, a fixed income fund with a low risk profile that aims to deliver higher returns than money market funds.

SERVING OUR COMMUNITIES

Community banking is a core Butterfield business and investing in people and projects that are helping improve the prosperity and well-being of people in our markets is viewed as an important investment for the Bank. To that end, we provided sponsorship, donations and the helping hands of employee volunteers to deserving organisations and events across our jurisdictions in 2011.

Working together, the Board, the Bank's Management team and our employees have made great progress under our strategy to streamline and strengthen our businesses and processes. We have realigned our resources to areas with greater growth potential, and trimmed underperforming assets and offerings in the interest of fostering future profitability.

Our success in strengthening the Bank financially has been recognised by the rating agencies. In 2011, both Fitch and Standard & Poor's affirmed our ratings, the latter on more stringent criteria that saw many international banks downgraded during the year.

The financial press, too, has acknowledged our progress and recognised our people for their expertise. Several of our senior executives in Europe were included among *Citywealth's* honoured practitioners in the areas of trust, investment management and private banking. *Euromoney* recently identified Butterfield in Bermuda and the Caribbean as providing the "Best Private Banking Services" in a number of key areas.

On behalf of the Management team, I would like to thank Chairman Robert Mulderig and Vice Chairman Robert Steinhoff, who will both retire following the 2012 Annual General Meeting, for their many years of service to Butterfield. Both Mr. Mulderig and Mr. Steinhoff were instrumental in helping Butterfield secure new sources of capital to enable the Bank to survive the financial crisis and emerge in a position to prosper as the global economy recovers. I would also like to extend thanks to Director James Burr, who will be leaving the Board in 2012, for his valued contributions to Butterfield.

Finally, I would like to express my appreciation for the ongoing support we enjoy from our clients and Shareholders.

Bradford Kopp
President & Chief Executive Officer

BOARD OF DIRECTORS & PRINCIPAL BOARD COMMITTEES

L to R - Back Row: Richard Venn, Victor G. Dodig, Wolfgang Schoellkopf, Bradford Kopp, Brendan McDonagh, Barclay Simmons, James Burr, Shaun Morris
Front Row: Sheila Lines, Robert Steinhoff, Robert A. Mulderig, Pauline Richards, John Wright

COMMITTEES INDICATED BY NUMBERS

1,5
CHAIRMAN
ROBERT A. MULDERIG*
Retired Chariman & Chief Executive Officer,
Mutual Risk Management Ltd.
Chairman, Woodmont Trust Co. Ltd.

1,2,5
VICE CHAIRMAN*
ROBERT STEINHOFF
Retired Partner, KPMG
Director, Argus Insurance Co. Ltd.

2,5,6
JAMES BURR
Managing Director,
Carlyle Global Financial Services Group

3,4
VICTOR G. DODIG
Senior Executive Vice-President
and Group Head, Wealth Management, CIBC

1
BRADFORD KOPP
President & Chief Executive Officer,
The Bank of N.T. Butterfield & Son Limited

2,4,6
SHEILA LINES*
Chief Executive Officer,
KeyTech Limited

1,4
SHAUN MORRIS*
Partner,
Appleby Bermuda law firm

2,4,6
PAULINE RICHARDS*
Chief Operating Officer,
Armour Group Holdings Limited
Director, Wyndham Worldwide Inc.
Director, Apollo Global Management, LLC
Former Director and Audit Committee Chair,
Cendant Corporation

1,3
WOLFGANG SCHOELLKOPF
Managing Partner,
Lykos Capital Management

3,5
BARCLAY SIMMONS*
Managing Partner,
Attride-Stirling & Woloniecki,
Barristers & Attorneys

1,3,5
RICHARD VENN
Senior Executive Vice-President,
Advisor to the CEO Office, CIBC

3,6
JOHN WRIGHT*
Retired Bank Chief Executive

*Independent, Non-Executive Director. On an annual basis, the Corporate Governance Committee ensures the appropriate composition of the Board and its Committees in accordance with the Group's Corporate Governance Policy. The assessment of the independence of a Director is based upon a number of factors including, but not limited to: whether he or she has been employed by the Group within the last five years; whether he or she has had, within the last three years, a material relationship with the Group; and whether he or she represents a significant Shareholder.

PRINCIPAL BOARD COMMITTEES

1. **EXECUTIVE COMMITTEE OF THE BOARD OF DIRECTORS**
   Supports the Board in fulfilling its overall governance responsibilities.

2. **AUDIT COMMITTEE**
   Oversees Butterfield's financial reports, internal financial controls, internal audit processes and compliance.

3. **RISK POLICY & COMPLIANCE COMMITTEE**
   Focuses on credit, market and operational risk.

4. **CORPORATE GOVERNANCE COMMITTEE**
   Focuses on Directors' and Board Committee governance, performance and Directors' nominations.

5. **COMPENSATION & HUMAN RESOURCES COMMITTEE**
   Focuses on compensation and benefits, employee development and succession.

6. **AD HOC I.T. COMMITTEE**
   Focuses on technology and systems development.

On 5 January 2012, the Bank announced that Brendan McDonagh, who was previously Chief Executive Officer, HSBC North America and Group Managing Director, HSBC Holdings plc, will be nominated for election to its Board of Directors at the 2012 Annual General Meeting of Shareholders. Subject to his election, the Directors intend to appoint Mr. McDonagh to the position of Executive Chairman of the Bank.

DIRECTORS' CODE OF PRACTICE AND GROUP CODE OF CONDUCT

The Directors have adopted a *Code of Best Practice* based upon recommended principles of corporate governance. In implementing the *Code*, the Board meets regularly, retains full effective control over the Bank, and monitors Executive Management. A *Group Code of Conduct* applies to Directors and employees and imposes Butterfield's principles of business, including ethics and conflicts of interest. Copies of the *Codes* can be accessed on www.butterfieldgroup.com.

SENIOR MANAGEMENT

BRADFORD KOPP*
President & Chief Executive Officer

MICHAEL COLLINS*
Senior Executive Vice President,
Bermuda

CONOR O'DEA*
Senior Executive Vice President,
International Banking and Managing
Director, Butterfield Bank (Cayman) Limited

CURTIS BALLANTYNE
Senior Vice President,
Chief Credit Officer

SHEILA BROWN
Senior Vice President,
Investment Services, Bermuda

CURTIS DICKINSON
Executive Vice President,
Group Capital Markets & Treasury

ERWIN DIKAU
Chief Financial Officer,
Butterfield Bank (Cayman) Limited

WILTON DOLLOFF*
Executive Vice President,
Chief Operating Officer

DANIEL FRUMKIN*
Executive Vice President,
Chief Risk Officer

DONNA HARVEY MAYBURY*
Executive Vice President,
Human Resources

PAUL HODGSON
Managing Director,
Butterfield Trust (Guernsey) Limited

*Member, Group Executive Committee

PHILIP JONES
Senior Relationship Manager &
Deputy Head of Corporate Banking,
Bermuda

CHARLES LAWRENCE
Senior Vice President,
Treasury, Bermuda

SEAN LEE
Executive Vice President,
Retail Banking, Bermuda

JOHN MARAGLIANO
Senior Vice President,
Finance

JULIEN MARTEL
Managing Director,
Butterfield Bank (Bahamas) Limited

MICHAEL MCWATT
Executive Vice President,
Banking and Deputy Managing Director,
Butterfield Bank (Cayman) Limited

JAMES MCPHERSON*
Senior Vice President,
Group Internal Audit

ROBERT MOORE*
Executive Vice President,
Head of Group Trust

MICHAEL NEFF*
Executive Vice President,
Head of Group Asset Management

JIM PARKER
Managing Director,
Butterfield Trust (Switzerland) Limited

MARTIN POLLOCK
Managing Director,
Butterfield Trust (Bermuda) Limited

JONATHAN RAYNOR
Senior Vice President,
Group Head of Compliance & Risk Change

JOHN ROBINSON
Managing Director,
Butterfield Bank (Guernsey) Limited

BRADLEY ROWSE*
Executive Vice President,
Chief Financial Officer

NIR SADEH
Senior Vice President,
Private Banking, Bermuda

RICHARD SAUNDERS
Head of European Asset Management

W. AARON M. SPENCER
Senior Vice President,
Operations and Information Technology

RAYMOND SYKES
Managing Director,
Butterfield Bank (UK) Limited

LLOYD WIGGAN
Managing Director,
Butterfield Bank (Barbados) Limited

BOB WILSON
Executive Vice President,
Corporate Banking, Bermuda

CONTENTS

MANAGEMENT'S DISCUSSION & ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

The financial overview of results of operations and financial condition should be read in conjunction with our Consolidated Financial Statements and the related notes. The Financial Statements and notes have been prepared in accordance with generally accepted accounting principles in the United States of America (GAAP). All references to "Butterfield", the "Group" or the "Bank" refer to The Bank of N.T. Butterfield & Son Limited and its subsidiaries on a consolidated basis. Certain statements in this discussion and analysis may be deemed to include "forward looking statements" and are based on Management's current expectations and are subject to uncertainty and changes in circumstances. Forward looking statements are not historical facts but instead represent only Management's belief regarding future events, many of which by their nature are inherently uncertain and outside of Management's control. Actual results may differ materially from those included in these statements due to a variety of factors, including worldwide economic conditions, success in business retention and obtaining new business and other factors.

PERFORMANCE MEASUREMENT

We use a number of financial measures to assess the performance of our business lines. Some measures are calculated in accordance with GAAP while other measures do not have a standardised meaning under GAAP. Accordingly, these measures, described below, may not be comparable with similar measures used by other companies. Investors may, however, find these non-GAAP financial measures useful in analysing financial performance.

Return on Assets ("ROA")

ROA is an indicator of profitability relative to total assets. ROA demonstrates how efficient Management is at using assets to generate earnings. The ROA ratio is calculated as Annual earnings / Average total assets.

Return on Common Shareholders' Equity ("ROE")

ROE measures profitability by revealing how much profit is generated with the money invested by Shareholders. ROE is the amount of net income returned as a percentage of Shareholders' Equity and calculated as Net Income / Average Shareholders' Equity. Net income is for the full fiscal year (before dividends paid to Common stock holders but after dividends to Preferred stock). Common Shareholders' Equity does not include the $200 million liquidation preference on Preference Shares.

Tier 1 Capital Ratio

The Tier 1 Capital Ratio is the ratio of the Bank's core equity capital, as measured under Basel II, to its total risk-weighted assets ("RWA"). RWA are the total of all assets held by the Bank weighted by credit risk according to a formula determined by the Regulator. The Bank follows the Basel Committee on Banking Supervision (BCBS) guidelines in setting formulae for asset risk weights.

Tier 1 Common Ratio

The Tier 1 Common Ratio is the same as the Tier 1 Capital Ratio but only includes Common equity in the numerator and deducts the $200 million liquidation preference on Preference Shares.

Total Capital Ratio

The Total Capital Ratio measures the amount of the Bank's capital in relation to the amount of risk it is taking. All banks must ensure that a reasonable proportion of their risk is covered by permanent capital. Under Basel II, Pillar I, banks must maintain a minimum total capital ratio of 8%. In effect, this means that 8% of RWA must be covered by permanent or near permanent capital. At least half of the regulatory capital must fall into Tier 1, which only takes into account the pure equity capital so the Tier 1 ratio must be at least 6%. The risk weighting process takes into account the relative risk of various types of lending. The higher the capital adequacy ratio a bank has, the greater the level of unexpected losses it can absorb before becoming insolvent.

Tangible Common Equity / Tangible Asset Ratio ("TCE / TA")

TCE / TA is used to determine how much loss the Bank can take before Shareholder equity is impacted. The TCE / TA ratio is calculated as (Common equity - Intangible assets - Goodwill) / Tangible assets. Common equity is the Bank's Total Shareholders' equity less the $200 million liquidation preference on Preference Shares. Tangible assets are the Bank's total assets less goodwill and intangibles.

Net Interest Margin ("NIM")

NIM is a performance metric that examines how successful the Bank's investment decisions are compared to its cost of funding assets and is calculated as (Interest income – Interest expenses) / Average Interest Earning Assets. The daily average was used in calculating the average balance for deposits to avoid any distortion caused by large fluctuations.

Efficiency Ratio

The Efficiency Ratio is defined as non-interest expenses before amortisation of intangible assets and income taxes as a percentage of total revenue before gains and losses and provisions for credit losses.

ABOUT BUTTERFIELD

Established in 1858, Butterfield provides community banking and wealth management in Bermuda and select markets in the Caribbean and Europe. Today we are the largest independent bank in Bermuda and have a significant market position in the Cayman Islands. Group-wide, we have over 1,300 employees across seven jurisdictions. Butterfield offers a full range of community banking services in Bermuda, Barbados and the Cayman Islands, consisting of institutional, corporate, commercial and retail banking and treasury activities. In wealth management, we provide private banking, asset management, custody and trust services to individual, family, institutional and corporate clients from our headquarters in Bermuda and subsidiary offices in The Bahamas, the Cayman Islands, Guernsey, Switzerland and the United Kingdom.

BUSINESS STRATEGY

Whilst remaining well capitalised with strong liquidity, our strategic focus is on building Shareholder value by expanding our share of the community and private banking markets in jurisdictions in which we have a meaningful presence and a depth of local market knowledge. Our strategy also involves leveraging our multi-jurisdictional trust, custody and asset management offerings to build our wealth management business from both cross-referrals with existing customers and new client generation from our core and new growth markets. We aim to build upon our relationship-based business approach by delivering exceptional client service experiences, as well as a wide range of products to meet our clients' financial services needs.

The wide range of products we offer is reflective of our strategy of pursuing diversified business lines, including private banking, asset management, custody, corporate trust and personal trust services. Those diverse businesses directly contribute to the high level of fee income relative to our total income. Despite the current economic environment reducing the volume of customer activity, our fee income remains at almost 39% of revenue before provisions and gains or losses.

To build on our community banking and wealth management strategies, we will also leverage our strong and loyal client base. Unlike many banks, Butterfield is almost exclusively funded by our Shareholders and our customers. Our core customer deposits have been remarkably stable throughout the crisis. In 2011, we focused on these core deposits and pricing discipline to significantly improve their contribution to net interest income. This contribution reflects the strength of being a deposit-led organisation even in times of low interest rates.

To support our strategy, we have realigned our Management structure to focus on lines of business and central support services with less emphasis on independent management and support teams by jurisdiction. However, we remain flexible and nimble in each jurisdiction, with decision making on client service-related matters based locally. In addition, we have invested heavily—and continue to invest—in new technology that allows for new and flexible products, enhanced customer service and a streamlined, more efficient operation. We expect our recent investment in new core banking systems in our two largest markets—Bermuda and the Cayman Islands—will help drive new revenue opportunities, improved internal control, and operational efficiencies. Our strategy of moving to centralised support services and centres of excellence is enhanced by these technological investments and will drive further efficiencies.

Given the large, loyal customer deposit base enjoyed in our main jurisdictions, and the relatively low volume of lending demand from our customer base, our investment strategy is more important than to most financial institutions. At 31 December 2011, we had $4.1 billion of cash and investments representing almost 47% of total assets. In recognition of this defining characteristic of Butterfield, we have adopted a conservative approach to our investments, including significantly reducing the list of international banks from whom we will purchase certificates of deposit. 2011 also represented a significant advancement in reducing our Interest Rate Risk, which measures the degree to which our profitability is at risk due to changes in interest rates. This advancement has allowed us to improve the profitability of our investments despite the ongoing challenges of a low and volatile investment climate and without increasing credit risk. Our continued management of Interest Rate Risk requires us to purchase fixed rate investments that, while complying with our credit safety requirements, will experience temporary declines in market values when rates start to increase. Rising interest rates will improve the profitability of Butterfield, such that these anticipated negative marks are part of our strategy—they will not affect earnings, as they are not credit related, but they will potentially give rise to negative impacts in equity through "Other Comprehensive Income". To minimise the impact on our equity in such circumstances, while implementing proper management of Interest Rate Risk, we have instituted a Held to Maturity ("HTM") portfolio of $64.8 million at year end. This portfolio is expected to grow to up to $250 million and the range of permitted investments is very limited to ensure a very high credit quality. Unless modified by the Board of Directors, the HTM investments must be explicitly or implicitly guaranteed by a G7 nation or supranational, rated AA+ or better in either case.

2011 OVERVIEW

During 2011, we continued to build our core infrastructure, made progress in rightsizing our cost base, and generated revenue growth of 9.8%. Overall, we are pleased with the direction of Butterfield's financial performance in 2011, delivering net income of $40.5 million following two years of significant losses. However, our goal of returning to a position of greater sustainable profitability remains a work in progress. We are resolute in our commitment to continuing the positive momentum we have developed and to improving Shareholder value.

More effective deployment of liquidity, combined with disciplined deposit pricing drove a 19.4% increase in net interest income before credit losses. Cost management objectives established in 2010 were achieved, contributing to a 3.5% decrease in operating costs, a reduction in headcount of 135, and a 10.4% improvement in the efficiency ratio. However, these improvements were partially offset by declines in non-interest income as the recessionary environment caused continued declines in transaction volumes with some loss of business from customers restructuring their own businesses. Our core deposits remained stable in all jurisdictions, whilst maturing higher priced deposits in Bermuda, Guernsey and the United Kingdom migrated to financial institutions willing to pay higher deposit rates.

Key Accomplishments in 2011 were as follows:

- **Systems:** We implemented new core banking systems in Bermuda and the Cayman Islands.
- **Capital:** We maintained a strong capital position, with over $1.0 billion of regulatory capital, a Tier 1 capital ratio of 17.7% at 31 December 2011, with a TCE / TA ratio of 6.6%, up 13.8% from 5.8% in 2010.
- **Profitability:** The Bank delivered four consecutive quarters of profitability; with net income for the year rising from $14.8 million normalised in 2010 to $40.5 million in 2011.
- **Investment strategy:** We implemented a new investment strategy for the deployment of excess liquidity that contributed to our NIM increasing by 47 basis points, from 2.03% in 2010 to 2.50% in 2011, despite an environment of falling interest rates and our dedication to conservative investments.
- **Expenses:** We reduced non-interest expenses by $10.9 million, from $309.4 million in 2010, to $298.5 million in 2011.
- **Headcount:** Across the Group, headcount was reduced by 135, from 1,519 as at 31 December 2010 to 1,384 by the end of 2011.
- **Deposits:** The Bank maintained stable core deposits, whilst decreasing deposit costs by 13 basis points, from 65 basis points in 2010 to 52 basis points in 2011.
- **Loan quality:** Gross non-accrual loans as a percentage of gross loans decreased to 2.8% at year-end 2011 from 3.9% at year-end 2010 as certain properties previously used by customers as security for loans are now held directly by the Bank as Other Real Estate Owned.
- **Asset quality:** Non-performing assets as a percentage of total assets remained stable at 1.7% at year-end 2011. This ratio is a new measure comprising both non-accrual loans and Other Real Estate Owned.
- **Ratings reaffirmed:** Standard & Poor's ratings reaffirmed at A- under new ratings methodology; Fitch reaffirmed at A-.

MARKET ENVIRONMENT

For much of 2011, the impact of the sovereign debt crisis in Europe overshadowed the more encouraging economic news from western economies, creating uncertainty and market volatility as market participants attempted to interpret the impact on the near-term macro economic direction. The fear of a double-dip recession in the United States subsided in the second half of the year, whilst European political disputes and threats of disruption of oil production in the Middle East violently swayed markets. Consistent with the volatility, the impacts in the economies in which we operate were mixed. Island economies have generally experienced rising unemployment and shrinking populations as companies have downsized and moved central support services to less expensive jurisdictions. This has had a ripple effect as demand for local business services has declined. In Bermuda and the Cayman Islands, the worst impact was felt in the construction and quarrying sectors, as both the number and value of construction projects continued to decline during the year. Tourism continued to struggle, given the high correlation with the United States economy, but some strengthening was seen in 2011 with increases in air arrivals and hotel occupancy levels in both Bermuda and the Cayman Islands, albeit at significantly reduced levels from the highs seen in 2007. These factors contributed to a muted business environment in our Bermuda and Caribbean operations with little loan demand and limited growth opportunities.

Our customers have not been immune to the economic downturn, and we saw more pressure on their ability to service loan payment obligations during the year. However, our close relationship with our customers and hands-on approach to working with them to address loan servicing challenges has softened the impact on our non-performing assets. Conversely, our private banking business in Europe enjoyed strong loan demand as some European banks withdrew from sectors of the lending market appropriate for our private banking businesses. We were able to advance more quality loans to high net worth customers, improve our low loan-to-deposit ratio and grow our European lending book. Additionally, we have seen increasing demand for wealth management products from high net worth individuals seeking asset protection strategies in defence of uncertainty and volatility.

2012 OUTLOOK

Although 2011 provided a difficult economic climate in which to operate, Butterfield made progress against our strategic priorities and emerged profitable. 2012 is beginning to show some cause for optimism, partially as a result of the heightened level of new company registrations and levelling off of population declines seen in Bermuda and the Cayman Islands in 2011. In Bermuda, we are seeing strong political will to make the necessary changes to immigration and land ownership policies that are expected to attract new international businesses to the island, as well as efforts to reduce deficit levels. This optimism is tempered by the ongoing economic challenges, high unemployment and low interest rates.

In the Cayman Islands, a special economic zone was officially launched in 2012 to help attract new businesses to the country, known as "Cayman Enterprise City"; it is expected to welcome its first businesses in the first quarter. Temporary accommodations have been gazetted to allow operations to commence immediately while phase one of Cayman Enterprise City's permanent campus is constructed.

In our European operations, we expect that competitive pressures on deposit pricing will be sustained, but we continue to benefit from high quality, low loan-to-value lending opportunities to high net worth private clients.

After several years in 'rebuilding' mode, and having completed our strategy to de-risk the Balance Sheet, and made significant progress in restructuring operations and enhancing our technology, Butterfield is well positioned to take advantage of market opportunities as they emerge. With a strong total capital ratio of over 23%, good liquidity versus our peer banks (with a loan-to-asset ratio of only 48%), low cost core deposits (at only 52 basis points), stable loan quality metrics, and new systems in our two largest jurisdictions, we are optimistic about our ability to compete for new business.

In 2012, we are focusing our attention on product development and customer service, which we expect will drive revenue growth from both cross selling to our existing client base and winning new business. Business development plans are continually being refined by our Executive Management team and are closely monitored by the Board of Directors to ensure targets are being met. Incentive plans have been more closely aligned with business development targets and metrics that reflect Shareholders' interests.

On 25 January 2012, officials from the United States Federal Reserve announced that they expect interest rates to remain low until at least late 2014. We reduced our exposure to declining interest rates in this sustained low-rate environment and have successfully increased our investment returns and net interest margin by employing our conservative investment strategy and with the help of our investment advisers, building a laddered, high quality securities portfolio. However, our Balance Sheet will benefit significantly from a rising rate environment due to our asset sensitivity. Through the continued employment of this strategy, we expect the returns on our investments in 2012 will modestly exceed the returns achieved in 2011, but is dependent on our ability to purchase qualifying assets as maturities fall due.

We expect to be able to continue to realise cost efficiencies in 2012 based on leveraging our previous investments in technology. The use of common systems, lapsing support contracts on legacy systems, redesigning processes and centralising support services are anticipated to drive further cost savings in 2012.

FINANCIAL SUMMARY (in $ thousands, except per share data)

As at 31 December	2011	2010	2009	2008	2007
Cash and cash equivalents	**1,979,458**	2,429,699	1,986,798	2,221,390	2,517,012
Short-term investments	**34,814**	26,392	N/A	N/A	N/A
Investments in debt and equity securities	**2,089,726**	2,629,144	2,926,901	3,824,079	4,744,989
Loans, net of allowance for credit losses	**4,247,260**	4,043,360	4,218,332	4,418,277	4,124,764
Premises, equipment and computer software	**276,114**	261,955	244,242	197,155	215,379
Goodwill and intangible assets	**49,184**	54,963	66,841	71,614	106,490
Total assets	**8,824,109**	9,623,060	9,594,602	10,911,844	11,910,920
Total deposits	**7,525,440**	8,228,059	8,696,619	9,801,269	10,747,971
Subordinated capital	**267,755**	282,799	283,085	282,296	284,191
Shareholders' equity					
Liquidation preference of Preference Shares	**200,000**	200,000	200,000	-	-
Common and Contingent Value Preferred equity	**629,725**	609,288	155,460	518,440	629,330
For the year ended					
Net interest income before provision for credit losses	**213,735**	178,942	186,907	254,481	252,600
Provision for credit losses	**(14,326)**	(41,970)	(104,879)	(3,045)	(1,983)
Non-interest income (as reported)	**135,246**	143,420	151,705	212,941	219,682
Non-interest income (excluding fund administration services business)	**135,246**	143,420	151,705	177,358	170,426
Salaries and other employee benefits	**150,752**	159,082	156,839	183,152	184,751
Other non-interest expenses (including income taxes)	**147,706**	148,408	143,351	167,335	139,217
Net income before gains and losses	**36,197**	(27,098)	(66,457)	113,890	146,331
Gains and losses	**4,275**	(180,517)	(146,956)	(109,051)	(336)
Net income (loss)	**40,472**	(207,615)	(213,413)	4,839	145,995
Dividends and guarantee fee of Preference Shares	**21,270**	18,000	9,450	-	-
Net income (loss) available to Common Shareholders	**19,202**	(225,615)	(222,863)	4,839	145,995
Common dividends paid	-	-	14,938	57,733	54,366
Financial ratios					
Return on assets	**0.4%**	(2.2%)	(2.1%)	0.0%	1.2%
Return on Common Shareholders' equity [(1)]	**3.0%**	(44.3%)	(47.0%)	0.8%	25.2%
Tier 1 capital ratio	**17.7%**	15.7%	7.2%	7.5%	8.6%
Total capital ratio	**23.5%**	21.6%	10.1%	11.2%	13.0%
Tangible common equity ratio	**6.6%**	5.8%	0.9%	4.1%	4.4%
Net interest margin	**2.50%**	2.03%	1.95%	2.18%	2.20%
Efficiency ratio [(3)]	**83.9%**	94.3%	89.0%	72.8%	65.7%
Per participating Share ($) [(1) (2)]					
Net income (diluted)	**0.03**	(0.47)	(2.34)	0.05	1.48
Cash dividends	-	-	0.12	0.52	0.64
Net book value	**1.14**	1.10	1.64	5.44	6.53
Number of employees					
Bermuda	**664**	732	761	803	843
Overseas	**720**	787	845	889	1,007
Total	**1,384**	1,519	1,606	1,692	1,850
Other data					
Average number of participating Shares on a fully diluted basis	**555,615**	477,225	95,065	96,683	98,732
Risk-weighted assets	**4,425,639**	4,934,569	5,734,096	6,199,963	6,345,754

[(1)] Includes both Common and Contingent Value Convertible Preferred equity. [(2)] All prior period per Common Share data and number of Common Shares, with the exception of dividends, have been restated to reflect the $0.04 stock dividend declared for March, May, August and November 2009 and the one-for-ten stock dividend of February 2008. All prior period per Share data has been restated to reflect the three-for-one stock split of August 2007. [(3)] 2010 & 2009 calculated based on normalised income for comparability purposes.

CONSOLIDATED RESULTS OF OPERATIONS AND DISCUSSION FOR FISCAL YEAR ENDED 31 DECEMBER 2011

In 2010, we evaluated our performance on a reported basis (i.e., as reported in our Consolidated Financial Statements prepared in accordance with GAAP) as well as on a normalised basis. In 2011, we discontinued reporting normalised income as we believe our 2011 financial results better reflect normal ongoing operations. For comparative purposes, we have included comparison to 2010 normalised income as reported in the prior year. For 2010, transactions that were viewed by Management not to be in the normal course of day-to-day business and were unusual in nature were excluded from normalised earnings as they obscure or distort the analysis of trends. Certain earnings measures, such as normalised earnings, do not have standardised meanings as prescribed by GAAP and therefore are unlikely to be comparable to similar measures presented by other companies.

Net Income (Loss)

The Bank reported net income of $40.5 million for the year ended 31 December 2011, compared to a net loss of $207.6 million in 2010. Results in both years were adversely affected by various non-operating gains and losses. After deduction of dividends ($19.3 million) and the guarantee fee ($2.0 million) on Preference Shares, the net income available to Common Shareholders was $19.2 million ($0.03 per share) in 2011 compared to a reported loss of $225.6 million ($0.47 per Share) in 2010. On a normalised basis, after non-recurring normalisation adjustments, the 2010 loss was $3.2 million ($0.01) per Share.

The following table states reported earnings for 2011 compared to normalised 2010 earnings (the Bank discontinued reporting normalised earnings in 2011):

	Year ended 31 December				
(in $ millions)	2011 Reported	2010 Normalised	2010 Reported	$ change [1]	% change [1]
Non-interest income	**135.2**	139.6	143.4	(4.4)	(3.2%)
Net interest income before provision for credit losses	**213.7**	178.9	179.0	34.8	19.4%
Total revenue before provision for credit losses and gains and losses	**348.9**	318.5	322.4	30.4	9.5%
Net gains and losses	**4.3**	0.0	(180.5)	4.3	100.0%
Provision for credit losses	**(14.3)**	(10.1)	(42.0)	(4.2)	41.6%
Total revenue	**338.9**	308.4	99.9	30.5	9.8%
Total non-interest expenses	**(298.5)**	(292.0)	(309.5)	(6.5)	2.2%
Net income before taxes	**40.4**	16.4	(209.6)	24.0	146.3%
Income tax	**0.1**	(1.6)	2.0	1.7	106.3%
Net income	**40.5**	14.8	(207.6)	25.7	173.6%
Dividends and guarantee fee of Preference Shares	**(21.3)**	(18.0)	(18.0)	(3.3)	18.3%
Net income (loss) / earnings attributable to Common Shareholders	**19.2**	(3.2)	(225.6)	22.4	700.0%
Net income (loss) / earnings per Common Share					
Basic	**0.03**	(0.01)	(0.47)	0.04	133.3%
Diluted	**0.03**	(0.01)	(0.47)	0.04	133.3%

[1] Change shown is reported 2011 compared to normalised 2010.

The following table reconciles the Bank's GAAP reported net income for 2010 with normalised earnings for 2010. There were no normalisation adjustments in 2011.

(in $ millions)	Year ended 31 December 2010	
	Net income (loss)	**Diluted EPS**
Net loss as reported	**(207.6)**	**(0.47)**
Non-core items:		
Net other gains & losses [1]	**172.9**	**0.36**
Investments in affiliates	**1.5**	**-**
Specific provision for credit losses [2]	**31.8**	**0.06**
Legal fees pertaining to liquidity facility	**7.4**	**0.02**
Non-recurring organisational change costs [3]	**12.4**	**0.03**
Non-recurring taxation credit	**(3.6)**	**(0.01)**
Net normalised income	**14.8**	**(0.01)**

Transactions that are viewed by Management not to be in the normal course of day-to-day business and are unusual in nature are excluded from normalised earnings for the year ended 31 December 2010 as they obscure or distort the analysis of trends.

Normalisation adjustments for 2010 include:

(1) Net other gains & losses as follows:

- Net realised losses of $107.0 million, of which $113.8 million relates to realised losses on the sale of asset-backed securities held in the Available For Sale portfolio, partially offset by realised gains of $1.9 million on the disposal of fixed income securities and realised gains of $4.7 million on the disposal of Structured Investment Vehicles ("SIVs") during 2010.
- Other-than-temporary impairments of $60.5 million on the Bank's holdings of SIVs.
- Realised loss on the sale of the Bank's subsidiaries in Hong Kong and Malta of $7.4 million.
- Write-down of $3.8 million of previously capitalised software development no longer in use.

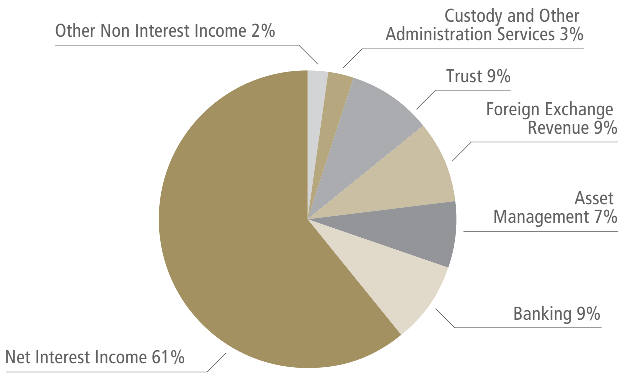
(2) Specific provisions for credit losses of $31.8 million primarily related to commercial mortgage facilities in the hospitality industry in Bermuda and The Bahamas, as well as private banking exposures in the United Kingdom.

(3) The organisational change costs are non-recurring expenses incurred, which comprise acceleration of vesting on stock options on change in control, restructuring fees relating to changes to Executive Management and rationalisation of headcount in various jurisdictions.

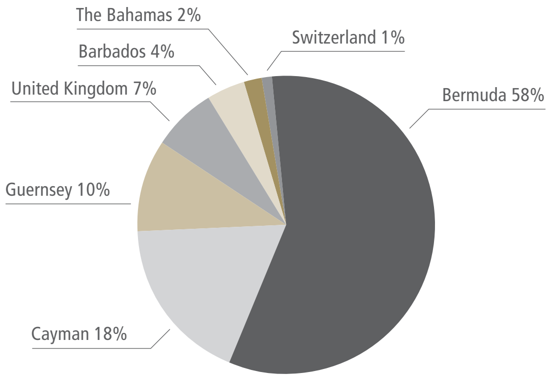
Revenue (Actual 2011 Versus Normalised 2010)

Total revenue before provisions for credit losses and gains and losses for 2011 was $348.9 million, up $30.4 million (9.5%) from $318.5 million in 2010. Total non-interest income was down $4.4 million (3.2%) from $139.6 million in 2010 to $135.2 million in 2011; the decrease was primarily attributable to the sale of our Hong Kong and Malta businesses in 2010, which had related revenue of $3.0 million in the prior year. Net interest income before provisions for credit losses rebounded by $34.8 million (19.4%) from $178.9 million in 2010 to $213.7 million in 2011, driven by a 47 basis point increase in the net interest margin from 2.03% in 2010 rising to 2.50% in 2011. The efficient deployment of excess liquidity under our new investment strategy, along with disciplined deposit pricing drove the improvement in the net interest margin, despite the sustained low interest rate environment.

DISTRIBUTION OF 2011 TOTAL REVENUES BEFORE PROVISIONS FOR CREDIT LOSSES AND GAINS AND LOSSES



DISTRIBUTION OF 2011 TOTAL REVENUES BY LOCATION BEFORE PROVISIONS FOR CREDIT LOSSES AND GAINS AND LOSSES



Non-Interest Income

Non-interest income is a function of a number of factors including the composition and value of client assets under management and administration, the volume and nature of clients' transaction activities, and the types of products and services our clients use. Our fee structure provides for varied pricing that depends on the value of client assets and the nature of services provided. As a result, it is not always possible to draw a direct relationship between the value of client assets and the level of non-interest income, although the trend of non-interest income generally follows the trend in client asset levels.

Total non-interest income was down $8.2 million from $143.4 million in 2010 to $135.2 million in 2011 and represents 38.8% of total revenues before provisions for credit losses and gains and losses for 2011, compared to 44.5% in 2010.

The following table presents the components of non-interest income for the years ended 31 December 2011 and 2010:

(in $ thousands)	2011	2010	$ change	% change
Asset management	22,942	24,544	(1,602)	(7.0%)
Banking	33,302	33,941	(639)	(1.9%)
Foreign exchange revenue	31,519	32,479	(960)	(3.0%)
Trust	29,995	30,534	(539)	(1.8%)
Custody and other administration services	11,780	13,574	(1,794)	(15.2%)
Other non-interest income	5,708	8,348	(2,640)	(46.3%)
Total non-interest income	135,246	143,420	(8,174)	(6.0%)

Asset Management

Asset management revenues are generally based on the market value of assets managed and the volume of transactions and fees for other services rendered. We provide asset management services from our offices in Bermuda, the Cayman Islands, Guernsey and the United Kingdom. Revenues from asset management were $22.9 million in 2011, down $1.6 million from $24.5 million in 2010; however, excluding the $1.9 million of revenue included in 2010 related to businesses sold in 2010, asset management revenues increased $0.3 million. Assets under management declined $433 million, primarily from redemption in the money market fund due to historically low rates, however a change in product mix to higher margin services increased revenues year on year.

The table that follows shows the changes in the year-end values of clients' assets under management, sub-divided between those managed for clients on a discretionary basis and those client funds invested in mutual funds that Butterfield manages:

(in $ millions)	2011	2010	$ change	% change
Butterfield Funds	3,375	3,677	(302)	(8.2%)
Discretionary	2,269	2,400	(131)	(5.5%)
Total assets under management	5,644	6,077	(433)	(7.1%)

Banking

During 2011, Butterfield provided a full range of community, commercial and private banking services in select jurisdictions. Retail and community banking services are offered to individuals and small to medium sized businesses through branch locations, telephone banking, Internet banking, automated teller machines and debit cards in Bermuda, the Cayman Islands and Barbados, whilst private banking services were offered in Bermuda, the Cayman Islands, Guernsey and the United Kingdom. Banking fee revenues reflect loan, transaction and processing, and other fees earned in these jurisdictions. Banking fee revenues fell by 1.9% in 2011 to $33.3 million, compared to $33.9 million in 2010, mainly due to a one-off fee earned in 2010 and the discontinuation of banking activities in The Bahamas.

Foreign Exchange

We provide foreign exchange services in the normal course of business in all jurisdictions. The major contributors to foreign exchange revenues are Bermuda and the Cayman Islands, accounting for 77% of the Group's foreign exchange revenue (2010: 76%). The Bank does not have a proprietary trading book. Foreign exchange income is thus generated from client-driven transactions and totalled $31.5 million in 2011, compared with $32.5 million in 2010. The $1.0 million year-on-year decrease reflects declining client volumes, in line with the slowing economic conditions.

Trust

We provide both personal and institutional trust services from our operations in Bermuda, The Bahamas, the Cayman Islands, Guernsey and Switzerland. Trust revenues are derived from a combination of fixed fees, fees based on the market values of assets held in trust and fees based on time spent in relation to the range of personal trust and company administration services and pension and employee benefit trust services we provide. In 2011, trust revenues totalled $30.0 million, marginally lower than the $30.5 million recorded in 2010; however, prior year included $1.0 million in revenue related to the Malta business that was sold in 2010 and when excluded, trust revenues increased $0.5 million. Trust revenues represented 22% of total non-interest income in 2011, up from 21% in 2010. Revenue increases were seen in four of our five trust operations: The Bahamas increased by 4.3%, Bermuda increased 3.6% and Guernsey rose 1.7%, while in Switzerland revenues were up 38.2% year on year. In December 2010, a restructuring of our Bahamas operations to focus predominantly on trust activities was announced. In September 2010, the Bank concluded the sale of its trust operations located in Malta, which did not contribute significantly to this line of business. Total Trust assets under administration were $40.7 billion as at 31 December 2011 compared to $40.5 billion the prior year.

Custody and Other Administration Services

Custody fees are generally based on market values of assets in custody, the volume of transactions and flat fees for other services rendered. We provide custody services from our offices in Bermuda, the Cayman Islands, Guernsey and the United Kingdom, and other administration services—primarily administered banking—in Guernsey. In 2011, revenues were $11.8 million compared to $13.6 million in 2010, down 13.2%, in part due to lower transaction volumes in our custody business, and partly due to a reduction in administered banking mandates as two large mandates wound down their operations. Total custody and other assets under administration (which includes the administered banking services operations provided by our Guernsey business) were $31.0 billion as at 31 December 2011, up $3.2 billion from $27.8 billion the prior year.

Other Non-Interest Income

The components of other non-interest income are set forth in the following table:

	Year ended 31 December	
(in $ thousands)	**2011**	**2010**
Net share of earnings (losses) from investments in affiliates	**884**	(1,587)
Rental income	**2,889**	2,779
Write back of unclaimed balances and dividends	**-**	5,785
Other	**1,935**	1,371
Total non-interest income	**5,708**	8,348

In 2010, we recorded equity pickup losses of $2.9 million in connection with our minority interest in Butterfield Fulcrum Group Limited ("BFG"), which is reflected in the 2010 net loss of $1.6 million from investments in affiliates. In the second quarter of 2011, the Bank sold all its remaining shares in BFG.

Rental income of $2.9 million in 2011, and $2.8 million in 2010, were received on various premises the Bank owns in Bermuda that are leased to tenants. Included in the "Other" category are maintenance fees from leased premises, Director fee income, and other miscellaneous charges.

Net Interest Income Before Provision For Loan Losses

Net interest income is the amount of interest earned on our interest-earning assets less interest paid on our interest-bearing liabilities. There are several drivers of the change in net interest income, including changes in the volume and mix of interest-earning assets and interest-bearing liabilities, their relative sensitivity to interest rate movements, and the proportion of non-interest-bearing sources of funds, such as equity and non-interest bearing current accounts.

The following table presents the components of net interest income for the years ended 31 December 2011 and 2010:

		2011			2010	
(in $ millions)	Average balance	Interest	Average rate	Average balance	Interest	Average rate
Assets						
Cash and cash equivalents and short-term investments	**1,932.5**	**10.8**	**0.56%**	2,107.6	11.0	0.52%
Investments	**2,486.0**	**45.6**	**1.84%**	2,595.6	28.3	1.09%
Loans	**4,132.8**	**202.6**	**4.90%**	4,119.6	198.1	4.81%
Interest-earning assets	**8,551.4**	**259.0**	**3.03%**	8,822.8	237.4	2.69%
Other assets	**466.3**	**-**	**-**	467.8	-	-
Total assets	**9,017.6**	**259.0**	**2.87%**	9,290.6	237.4	2.56%
Liabilities						
Deposits	**6,720.9**	**(34.7)**	**(0.52%)**	7,103.2	(46.0)	(0.65%)
Securities sold under repurchase agreements	**3.6**	**-**	**-**	-	-	-
Subordinated debt	**278.4**	**(10.5)**	**(3.77%)**	282.7	(12.5)	(4.41%)
Interest-bearing liabilities	**7,002.9**	**(45.2)**	**(0.65%)**	7,385.9	(58.5)	(0.79%)
Non-interest-bearing current accounts	**987.7**	**-**	**-**	961.6	-	-
Other liabilities	**192.3**	**-**	**-**	243.0	-	-
Total liabilities	**8,182.9**	**(45.2)**	**(0.55%)**	8,581.5	(58.5)	(0.68%)
Shareholders' equity	**834.7**	**-**	**-**	709.1	-	-
Total liabilities and Shareholders' equity	**9,017.6**			9,290.6		
Non-interest-bearing funds net of non-interest-earning assets (free balance)	**1,548.4**			1,436.9		
Net interest margin		**213.8**	**2.50%**		**178.9**	**2.03%**

Net interest income before provisions for credit losses increased by 19.4% to $213.7 million in 2011 compared to $178.9 million in 2010, of which 62% (2010: 63%) was generated in Bermuda and 18% (2010: 16%) in the Cayman Islands. Investment yields of 1.84% on $2.5 billion, up from 1.09% in 2010, combined with a 13 basis point decrease in deposit cost, drove a 47 basis point improvement in the net interest margin to 2.50% in 2011 compared to 2.03% in 2010. Although average interest-earning assets decreased by $275.5 million to $8.55 billion in 2011, the decrease had a positive impact on net interest income as the decline was driven by the migration of high-cost deposits which were deployed in lower yielding assets in the cash and cash equivalent category. Free balances of $1.5 billion in 2011 (2010: $1.4 billion) include non-interest-bearing current accounts of $1.0 billion (2010: $1.0 billion) and Shareholders' equity of $835 million (2010: $709 million) net of other assets and other liabilities. See the Risk Management section for more information on how interest rate risk is managed.

Provision For Credit Losses

The Bank's net provisions for credit losses in 2011 were $14.3 million compared to $42.0 million in 2010. The Bank anticipates the difficulties in the local economies, as well as the hospitality sector, will continue for the foreseeable future and has made sufficient provisions in anticipation of a difficult market. The incremental provisions were required principally for the specific reserves pertaining to commercial and residential exposures as well as enhancements to general provision.

Gains and Losses

The following table represents the components of gains and losses for the years ended 31 December 2011 and 2010:

(in $ thousands)	2011	2010
Net realised / unrealised (losses) gains on trading securities	(919)	971
Net realised gains (losses) on available for sale securities	2,059	(107,047)
Other-than-temporary impairment losses on held to maturity and available for sale investments	-	(60,522)
Loss on sale of Malta and Hong Kong located subsidiaries	-	(7,430)
Net other gains (losses)	3,135	(6,489)
Total gains and losses	4,275	(180,517)

Net Realised / Unrealised (Losses) Gains on Trading Securities

A $0.9 million loss was recorded with respect to trading securities in 2011 compared to a gain of $1.0 million in 2010, which primarily relates to the fair value adjustments of the Bank's seed money in shares of the Butterfield Select Investment Fund, the Butterfield Select Alternative Fund and $50 million in shares of the BNY Mellon Butterfield Income Advantage Fund, which was launched in 2011. During the year, we redeemed $3.8 million of our seed money as it was no longer required.

Net Realised Gains (Losses) on Available For Sale Securities

Net realised gains of $2.1 million were recorded on securities sold in the normal course of business as part of our asset and liability management strategy. The $107.0 million loss recorded in the prior year was a result of the sale of asset-backed securities as part of the Bank's Balance Sheet de-risking strategy.

Other-Than-Temporary Impairment ("OTTI") Losses on Held to Maturity and Available For Sale Investments

No OTTI losses were recognised in 2011 as Management believes there are no credit losses in the investments, compared to the 2010 OTTI credit loss of $60.5 million recognised.

Loss on Sale Of Malta And Hong Kong Located Subsidiaries

Consistent with Management's strategy of focusing resources in jurisdictions where we have a meaningful market presence and a depth of local market knowledge, in September 2010, the Bank sold its trust, wealth management and advisory businesses in Hong Kong and its trust operation in Malta with a resultant net loss of $7.4 million.

Net Other Gains (Losses)

Net other gains and losses were $3.1 million in 2011 compared to net other losses of $6.5 million in 2010.

Net other gains and losses in 2011 include the second quarter of 2011 BFG gain of $3.1 million, the gain on repayment of the subordinated debt of $1.1 million and the $1.4 million equity pick up losses of affiliates in the first quarter of 2011.

During the second quarter, Butterfield completed the sale of its equity interest in BFG for proceeds of $3.3 million, which triggered a dividend of $3.3 million ($0.42 per Share) to holders of Butterfield Contingent Value Convertible Preference Shares ("CVCP Shares"), which was paid on 16 August 2011 to Shareholders of record on 26 July 2011.

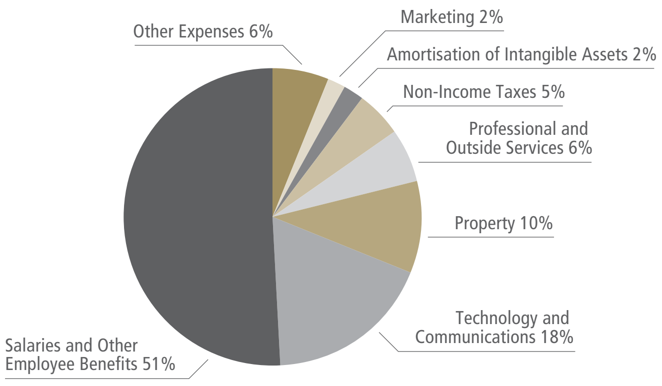
A realised gain of $1.1 million was recorded during the third quarter of 2011 as a result of the purchase and cancellation of $15.0 million of our own subordinated debt.

Net other losses of $6.5 million were recorded in 2010, which included: a write off of $3.8 million in respect of previously capitalised costs for the development of software that would no longer be used, a $1.5 million loss on the write down of an amount receivable from the Bank's charitable foundation; realised losses of $1.4 million on the Bank's equity holdings in two credit card companies, which were sold during 2010; losses of $0.7 million on the write down of a private equity investment and an investment in an affiliate to reflect lower expectations of proceeds on eventual sales; and a $1.2 million gain on interest rate swaps designated as trading instruments, as they did not qualify for hedge accounting but are used as part of the Bank's overall asset and liability management strategy.

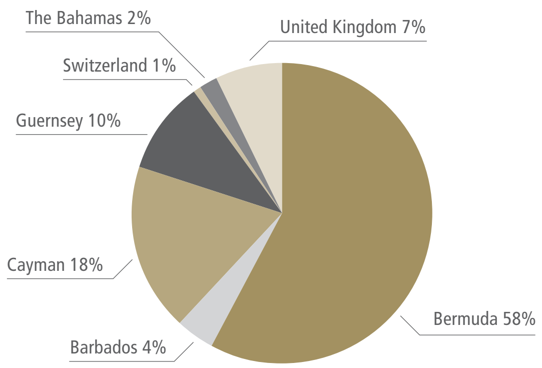
Non-Interest Expenses

Cost control continued to be a key focus of the Bank in 2011 as the recessionary economic conditions and persistently low interest rate environment challenged the banking business model. Total non-interest expenses in 2011 were $298.5 million compared to $309.5 million recorded in 2010. Salary and employee benefits account for 51% of non-interest expenses with technology, communications and property making up 28% combined. Bermuda expenses (including head office costs) represent the majority of the Group costs at 59% of total costs.

DISTRIBUTION OF 2011 EXPENSES



DISTRIBUTION OF 2011 EXPENSES BY LOCATION



The following table presents the components of non-interest expenses for the years ended 31 December 2011 and 2010:

(in $ thousands)	2011 Reported	2010 Reported	2010 Normalised	$ change vs. Normalised	% change vs. Normalised
Salaries and other employee benefits	150,752	159,082	147,113	3,639	2.5%
Technology and communications	55,037	54,037	54,037	1,000	1.9%
Property	29,316	27,469	28,169	1,147	4.1%
Professional and outside services	18,762	13,811	15,411	3,351	21.7%
Non-income taxes	14,500	15,405	15,405	(905)	(5.9%)
Amortisation of intangible assets	5,799	5,711	5,711	88	1.5%
Marketing	5,257	5,002	5,002	255	5.1%
Other non-interest expenses	19,068	28,948	21,116	(2,050)	(9.7%)
Total non-interest expenses	**298,491**	**309,465**	**291,964**	**6,525**	**2.2%**
Income tax benefit	(33)	(1,975)	1,960	(1,993)	(101.7%)
Total expenses	**298,458**	**311,440**	**293,924**	**4,532**	**1.5%**

Salaries and Other Employee Benefits

Salaries and other employee benefits of $150.8 million in 2011 represents a decrease of $8.3 million from 2010. Excluding the $12.0 million of non-recurring costs in 2010, salaries and other employee benefits increased by $3.7 million. However, during 2011, further staff reductions and the implementation of our new core banking system in Bermuda and the Cayman Islands resulted in additional one-off costs of $7.9 million. The 2011 one-off costs are made up of: $3.0 million in overtime and temporary employment services related to the systems implementation projects and $4.9 million in staff termination and redundancy costs. Net of one-off costs, salaries and other employee benefits declined by $4.2 million year over year. Salary cost reductions of $4.1 million, as a result of reduced headcount, which was down 135 from 1,519 at the end of 2010 to 1,384 by 2011, was partially offset by $1.5 million of annual merit increases. A further $7.9 million of savings was realised from reduced staff benefit costs, of which $7.5 million relates to a reduction in post-retirement health care expenses as a result of the changes to the benefit plan made in 2010. These savings were partially offset by a $6.3 million increase in staff incentive expenses, following several years of minimal incentive compensation awards, and also include the amortisation expense related to the previous year's stock option and Executive long-term Share plan awards.

In 2010, salaries and other employee benefits expenses included a charge of $6.2 million in connection with retention and termination payments and other staff-related benefits. These costs were incurred as part of the implementation of non-recurring organisational changes, including changes to Executive Management. Also included in salaries and other employee benefits expense in 2010 is a charge of $5.8 million related to Share-based compensation expenses that occurred as all stock options and deferred incentive shares immediately vested on the equity investment in March 2010. These costs are deducted to arrive at normalised earnings in 2010.

Technology and Communications

Technology and communication costs were $55.0 million in 2011, up $1.0 million on the $54.0 million recorded in 2010. This reflects the ramped-up run rate technology costs as the Bank's technology platforms have now been fully transitioned to our outsourcing partners, in addition to a partial-year increase of $1.5 million in depreciation from the costs capitalised as part of the new systems implementations in Bermuda and the Cayman Islands during the year. Offsetting these increases were savings of $0.8 million in communication costs from the migration of our traditional land line telephony system to a VOIP phone system.

Property

Property costs, which reflect occupancy expenses, building maintenance, and depreciation of property, plant and equipment, increased by $1.1 million to $29.3 million in 2011 versus the $28.2 million normalised expense of 2010. The increase was due to accelerated depreciation on certain premises totalling $1.6 million per year in additional depreciation.

Professional and Outside Services

Professional and outside services primarily include consulting, legal, audit, and other professional services. In 2011, the expense was $18.8 million, up $3.4 million compared to $15.4 million incurred in 2010 on a normalised basis; the increase driven mainly by increased investment advisory costs related to our investment advisory agreement with Carlyle Investment Management LLC. The 2011 fees included $1.2 million in consulting fees to assist in the development of future efficiencies.

Non-Income Taxes

These taxes reflect non-income-related taxes levied on us in the various jurisdictions in which we operate, including those associated with employee-related costs such as payroll tax, customs duties and business licenses. In 2011, we incurred costs of $14.5 million compared to $15.4 million in 2010, the decrease reflecting lower payroll tax in Bermuda due to a decreased number of employees.

Amortisation of Intangible Assets

Intangible assets relate to client relationships acquired from business acquisitions and are amortised on a straight-line basis over their estimated useful lives, not exceeding 15 years. Acquired intangible assets estimated lives are re-evaluated annually and tested for impairment. The amortisation expense associated with intangible assets was $5.8 million in 2011, compared to $5.7 million in 2010, as the Bank did not acquire or sell intangible assets during 2011.

Marketing

Marketing expenses reflect costs incurred in advertising and promoting our products and services. They totalled $5.3 million in 2011, up $0.3 million from 2010.

Other Non-Interest Expenses

(in $ thousands)	2011	2010	$ change
Stationery & supplies	**1,945**	2,209	(264)
Custodian & handling	**1,752**	1,810	(58)
Charitable donations	**1,239**	1,240	(1)
Insurance	**2,944**	3,241	(297)
Other expenses			
Maintenance fees for liquidity facility	**356**	1,765	(1,409)
Cheque processing	**1,615**	1,662	(47)
Dues and subscriptions	**590**	676	(86)
Registrar and transfer agent fee	**822**	931	(109)
Agent commission fees	**639**	848	(209)
Foreign bank charges	**948**	755	193
Directors' fees	**845**	747	98
ATM fees	**426**	506	(80)
General expenses	**1,455**	1,396	59
Other	**3,492**	3,330	160
Total normalised non-interest expenses	**19,068**	**21,116**	**(2,050)**
Commitment and legal fees to establish a liquidity facility with CIBC	-	7,480	(7,480)
Other non-recurring organisational costs	-	352	(352)
Total non-interest expenses	**19,068**	**28,948**	**(9,882)**

Other expenses were $19.1 million in 2011, a decrease of $2.1 million compared to 2010 normalised, primarily driven by the cancellation of the liquidity facility with CIBC in early 2011.

Income Taxes

In 2011, income tax expenses associated with our businesses in taxable jurisdictions, namely Barbados, Guernsey, Switzerland and the United Kingdom, were netted to nil compared to a benefit of $2.0 million in 2010. 2011 taxes reflect a tax benefit of $1.2 million (2010: $3.3 million) for our UK operation, which recorded a net loss in 2011, offset by income tax expenses of $0.8 million (2010: $0.6 million) in Guernsey and $0.3 million (2010: $0.8 million) in Barbados.

CONSOLIDATED BALANCE SHEET AND DISCUSSION

The following table shows the Balance Sheet as reported as at 31 December 2011 and 31 December 2010.

(in $ millions)	2011	2010
Assets		
Cash and cash equivalents	1,979	2,430
Short-term investments	34	26
Investments	2,090	2,629
Loans, net of allowance for credit losses	4,247	4,043
Premises, equipment and computer software	276	262
Other assets	196	233
Total assets	8,824	9,623
Liabilities		
Total deposits	7,525	8,228
Total other liabilities	201	303
Subordinated capital	268	283
Total liabilities	7,994	8,814
Liquidation preference of Preference Shares	200	200
Common equity	630	609
Total Shareholders' equity	830	809
Total liabilities and Shareholders' equity	8,824	9,623
Capital Ratios		
Risk weighted assets	4,426	4,935
Tangible Common equity (TCE)	581	554
Tangible assets (TA)	8,775	9,568
TCE/TA	6.6%	5.8%
Tier 1 Common ratio	13.1%	11.6%
Tier 1 ratio	17.7%	15.7%
Total Capital ratio	23.5%	21.6%

The Bank maintains a highly liquid Balance Sheet and is very well capitalised. On 31 December 2011, total assets of the Bank stood at $8.8 billion, down $0.8 billon from year-end 2010, reflecting lower year-end customer deposit balances in Bermuda, Guernsey and United Kingdom. At 31 December 2011, the total of cash and cash equivalents, short-term investments and investments represented $4.1 billion, or 46.5% of total assets, down from 52.8% at year-end 2010. At 31 December 2011, Butterfield's capital ratios were strong, having improved from year-end 2010, with the TCE / TA ratio ending 2011 at 6.6% (2010: 5.8%), whilst the Total Capital ratio and Tier 1 Capital ratios were of 23.5% (2010: 21.6%) and 17.7% (2010: 15.7%) respectively. These ratios are well in excess of regulatory minimums.

Cash, Cash Equivalents and Short-Term Investments

The Bank only places deposits with highly rated institutions and ensures there is appropriate geographic diversification in its exposures. Limits are set for aggregate geographic exposures for each institution and are monitored and reviewed by our Credit Risk Management ("CRM") division and approved by the Financial Institutions Committee. Effective 1 January 2011, the Bank changed its accounting policy with respect to cash and cash equivalents for the purposes of the Consolidated Statement of Cash Flows. The Bank defines cash and cash equivalents to 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, treasury bills and securities purchased under agreements to resell. Investments of a similar nature that are either restricted or have a maturity of more than three months but less that one year are classified as short-term investments. Previously, cash and demand deposits with banks only included cash and demand deposits, vault cash and cash in transit for the purposes of the Consolidated Statement of Cash Flows. The Bank believes the new policy is preferable as it more closely reflects the manner in which the Bank manages its liquid assets. As at 31 December 2011, cash and cash equivalents and short-term investments were $2.0 billion, compared to $2.5 billion as at 31 December 2010.

See "Note 3: Change in accounting policy" and "Note 4: Cash and cash equivalents" in the 31 December 2011 audited Financial Statements for additional tables and information.

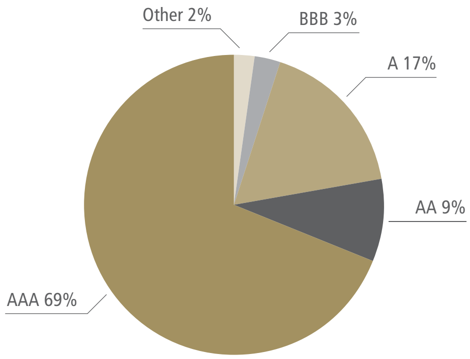
Investments

Total investments were $2.1 billion as at 31 December 2011, down $0.5 billion from the prior year-end balance, due primarily to the sale of the majority of our European exposures in the fourth quarter of 2011 and the purchase of treasury securities, which are included in the cash and cash equivalents category.

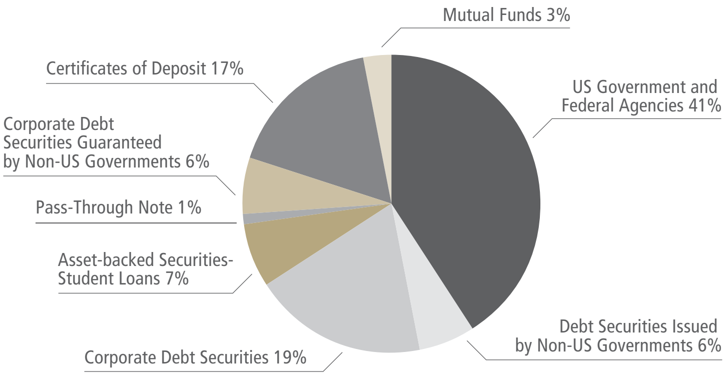
Effective 1 October 2010, the Bank entered into an investment advisory agreement with Carlyle Investment Management LLC, an affiliated company of the Carlyle Group. Under the agreement, Carlyle has agreed to provide Balance Sheet management advisory services to the Bank including, but not limited to: development of investment strategies for consideration by the Bank's Asset and Liability Committee; Balance Sheet simulation analysis, including interest rate sensitivity, economic value at risk, interest at risk and stress testing; detailed investment portfolio reporting; cash flows and net interest income forecasting; deposit behaviour analysis and pricing strategies; and assistance with credit advisory and workout strategies.

Our investment policies require Management to maintain a portfolio of securities that will provide the liquidity necessary to facilitate the funding of loans and cover deposit fluctuations, and to mitigate our overall Balance Sheet exposure to interest rate risk, whilst achieving a satisfactory return on the funds invested. The securities in which we may invest are limited to securities that are considered investment grade. Securities in our investment portfolio are accounted for under US GAAP as either Trading, Available For Sale or Held to Maturity. Investment policies are approved by the Board of Directors, governed by The Group Asset and Liability Management Committee and monitored daily by Group Market Risk, a division of Enterprise Risk Management.

31 DECEMBER 2011 INVESTMENT PORTFOLIO BY LONG-TERM DEBT RATING



31 DECEMBER 2011 INVESTMENT PORTFOLIO BY TYPE



Trading securities, consisting of holdings of non-US government securities, corporate equities and seed money invested in mutual funds managed by us, totalled $62.6 million at year-end 2011, compared to $18.1 million at year-end 2010, primarily reflecting the $50 million initial seed money invested by the Bank in BNY Mellon Butterfield Income Advantage Fund, which was off set by the disposal of the Butterfield Systematic Equity Fund in 2011.

Available for Sale ("AFS") securities totalled $2.0 billion at year-end 2011, compared to $2.6 billion at year-end 2010. As at 31 December 2011, 40.3% or $790.8 million (2010: 35% or $917.5 million) of AFS securities consisted of holdings of mortgage-backed securities issued by US government agencies. Corporate debt securities, certain of which are guaranteed by non-US governments totalled 27.0%, or $530.6 million (2010: 19.0% or $497.2 million), and certificates of deposit represented 18.2% or $356.5 million (2010: 33.0% or $859.1 million). The remaining 14.7% AFS securities are comprised primarily of debt securities issued by non-US governments ($113.0 million), government guaranteed student loan-backed securities ($144.3 million) and one pass-through note ($27.0 million), which was formerly a structured investment vehicle ("SIV").

Held to maturity ("HTM") investments were $64.8 million as at 31 December 2011 (2010: nil) and consisted entirely of mortgage-backed securities issued by US government agencies that Management has no intention to sell before maturity.

As at 31 December 2011, 95% (2010: 98.1%) of our total investments were rated investment grade (i.e., rated 'BBB' or higher).

The Bank held two SIV-related securities at 31 December 2010.

During 2011, a SIV-related security with carrying value of $24.3 million was sold, resulting in a gain of $0.1 million. The following table shows the par value, carrying value and unrealised losses of the Bank's only remaining SIV-related security (now restructured as a pass-through note) as at 31 December 2011.

	As at 31 December	
(in $ millions)	**2011**	**2010**
Par value	**58.8**	122.2
Carrying value	**27.0**	57.6
Unrealised loss in accumulated other comprehensive income	**6.7**	5.1
Total amortised cost	**33.7**	62.7
OTTI taken during the year	**-**	(60.5)
Carrying amount (market value) / Par value	**45.9%**	47.1%
Amortised cost / Par value	**57.3%**	51.3%

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 securities, 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 equity or debt securities in an unrealised loss position, potential OTTI is considered using a variety of factors, including the length of time and extent to which the market 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.

For debt securities, Management estimates cash flows over the remaining lives of the underlying collateral to assess whether credit losses exist and to determine whether any adverse changes in cash flows have occurred. Management's cash flow estimates take into account expectations of relevant market and economic data, such as gross domestic product (GDP) and unemployment, during the cash flow cycle as of the end of the reporting period and includes, for example, underlying loan-level data, and structural features of securitisation, such as subordination, excess spread, over-collateralisation or other forms of credit enhancement. Management compares the losses projected for the underlying collateral ("pool losses") against the level of credit enhancement in the securitisation structure to determine whether these features are sufficient to absorb the pool losses, or whether a credit loss on the debt security exists. Management also performs other analyses to support its cash flow projections, such as stress scenarios. 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.

See "Note 6: Investments" in the 31 December 2011 audited Financial Statements for additional tables and information.

Loans

The loan portfolio stood at $4.2 billion at 31 December 2011, up $0.2 billion from $4.0 billion the year before, due to the net advancement of $196 million to the Government of Bermuda and an increase of $121 million in Guernsey, offset by the partial and full settlement of certain corporate loans. At 31 December 2011, the loan portfolio represented 48.1% of total assets, compared to 42.0% at 31 December 2010, whilst loans as a percentage of customer deposits were 57.4% (2010: 49.6%).

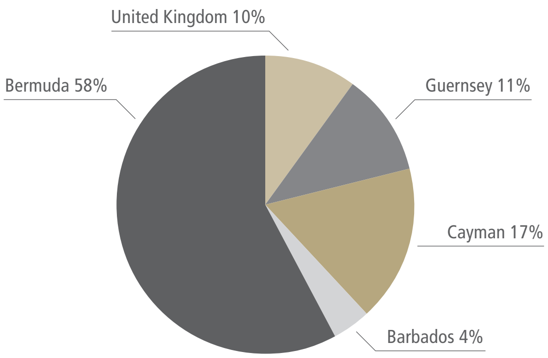
Specific and general allowances for loan losses at 2011 totalled $61.4 million at 31 December 2011, a decrease of $5.4 million from $66.8 million at year-end 2010. The movement in the allowance results from $23.8 million (2010: $107.9 million) of partial charge-offs, primarily on commercial related exposures, which the Bank deemed unrecoverable. This was offset by $4.1 million of recoveries (2010: $2.5 million) and $14.3 million (2010: $42.0 million) of incremental provisions for specific reserves, as well as enhancements to the general provisions in line with our provisioning policy that incorporates projected losses in changing economic environments.

Charge-offs were $23.8 million in 2011 compared to $107.9 million in 2010, whilst recoveries totalled $4.1 million in 2011 compared to $2.5 million in 2010. Total allowance for credit losses was $61.4 million at 31 December 2011, down from $66.8 million at 31 December 2010. Of the total allowance, the general allowance was $35.5 million (2010: $36.5 million) and the specific allowance was $25.9 million (2010: $30.3 million) and represents a total coverage ratio of 21.2% of gross non-accrual loans at 31 December 2011, compared to 19.0% at 31 December 2010.

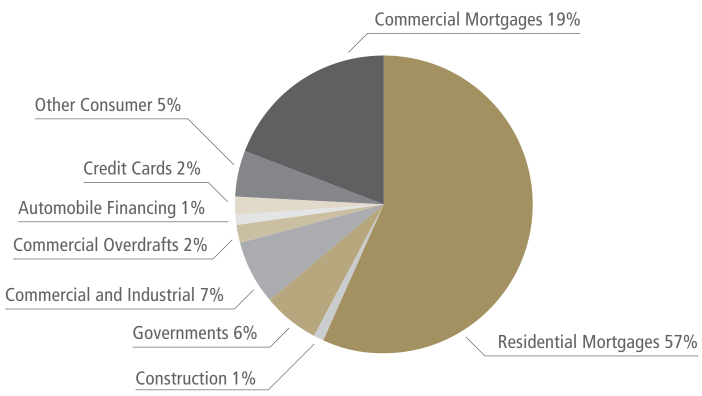
Gross non-accrual loans totalled $122.5 million at 31 December 2011, down $37.0 million from $159.5 million at 31 December 2010, and represented 2.8% of the total loan portfolio at 31 December 2011, compared to 3.9% in 2010. During 2011 the Bank recorded Other Real Estate Owned properties ("OREO") amounting to $27.4 million comprising real estate, amounting to $20.8 million, received during 2011 as settlement for a commercial mortgage loan balance and foreclosed residential properties with a fair value less cost to sell of $6.6 million.

A significant component of our credit risk relates to our loan portfolio. In addition, credit risk is inherent in certain contractual obligations such as legally binding unfunded commitments to extend credit, commercial letters of credit, and standby letters of credit. Our real estate loan portfolio comprises lending secured by commercial and residential real estate.

31 DECEMBER 2011 LENDING BY LOCATION



31 DECEMBER 2011 GROUP LOANS BY TYPE



Commercial and Industrial

Government

Loans to governments increased by $194.6 million, primarily as a result of the Bank's continued investment in the Bermuda economy. During 2011, the Bank extended the Government of Bermuda loan facility to $235 million, which was fully drawn down at the end of 2011.

Commercial and Industrial

The commercial and industrial loan portfolio includes loans and overdraft facilities advanced primarily to corporations and small and medium-sized entities, which are generally not collateralised by mortgages and where loan repayments are expected to flow from the operation of the underlying businesses.

Commercial and industrial loans decreased by $134.1 million in 2011 due to the combination of the partial settlement of a loan to BFG in the first quarter of 2011 of $40.9 million, and full settlements of corporate loans during 2011.

Commercial Mortgages

Commercial mortgages are offered to real estate investors, developers and builders domiciled primarily in Bermuda and the United Kingdom. To manage our credit exposure on such loans, the principal collateral is real estate held for commercial purposes and is supported by a registered mortgage. Cash flows from the properties, primarily from rental income, are generally supported by long-term leases to high quality international businesses. These cash flows are principally sufficient to service the loan.

Commercial mortgage financing decreased by $101.7 million, from $934.1 million at 31 December 2010 to $832.4 million at 31 December 2011, primarily due to increased pay downs, including real estate, amounting to $20.8 million, received during 2011 as settlement for a commercial mortgage loan balance, and managed reductions in commercial mortgage exposures. In addition, the Bank charged off commercial real estate loans, which in the opinion of Management, are considered uncollectible.

Residential
The residential mortgage portfolio is comprised of mortgages to clients with whom we are seeking to establish (or already have) a comprehensive financial services relationship. It includes mortgages to individuals and corporate loans secured by residential property.

At 31 December 2011, residential mortgages totalled $2.4 billion (or 56.4 % of total gross loans), an increase of $0.2 billion from 31 December 2010. The value of residential mortgages in Bermuda decreased slightly during 2011, due to the transfer of foreclosed properties to OREO at a fair value net of selling costs of $6.6 million. Our Guernsey and United Kingdom offices increased residential mortgage lending to high net worth individuals, secured by high-end properties in the London, UK area during the year, resulting in a significant increase in non-Bermuda residential mortgages in the portfolio.

All mortgages were underwritten utilising our stringent credit standards. Residential loans consist of conventional home mortgages and equity credit lines.

Other Loan Portfolios

We provide loans, as part of our normal banking business, in respect of automobile financing, consumer financing, credit cards, commercial financing, loans to financial institutions and overdrafts facilities to retail, corporate and private banking clients in the jurisdictions in which we operate.

Our loan portfolio and contractual obligations and arrangements are discussed in more detail in the Notes to the Consolidated Financial Statements.

See “Note 7: Loans” and “Note 8: Credit Risk Concentration” in the 31 December 2011 audited Financial Statements for additional tables and information.

Deposits

Deposits are our principal funding source for use in lending, investments and liquidity. Butterfield is a deposit-led Bank and does not require the use of wholesale funding to fund its loan business. During 2011, core deposits remained stable despite reductions in interest rates paid on deposits. Deposit balances at the end of reporting periods, particularly in our Bermuda and Cayman Islands operations, can fluctuate due to significant balances that flow in and out from hedge fund clients to meet quarter-end subscriptions and redemptions, and are generally paid out in the first few days of the quarter. The Bank views average customer deposits as a more representative measure of customer deposit balances.

The table below shows the average customer deposit balances by jurisdiction, comparing 2011 with 2010.

	Average balance during		
(in $ millions)	**2011**	**2010**	**$ Change**
Barbados	**3,340**	3,351	(11)
Bermuda	**259**	240	19
Cayman Islands	**1,732**	1,823	(91)
Guernsey	**1,470**	1,488	(18)
The Bahamas	**92**	129	(37)
United Kingdom	**816**	1,034	(218)
Total average deposits	**7,709**	8,065	(356)

Average customer balances were $7.7 billion, down $356 million from the prior year’s average of $8.1 billion. The decrease was primarily in the UK where the Bank made a strategic decision to exit its unprofitable Self Invested Personal Pension (“SIPP”) deposit business. In the Cayman Islands, the decrease represents lower cash balances held by institutional hedge fund clients during the year; core deposits were flat.

At year-end 2011, total customer deposits were $7.4 billion compared to $8.1 billion at 31 December 2010. The decrease primarily occurred in Bermuda, the Cayman Islands, Guernsey and the United Kingdom. The decrease in comparative year-end balances in Bermuda was primarily a result of lower hedge fund balances at 31 December 2011, as the Bank had experienced a build up of hedge fund deposits to meet the high rate of fund redemptions in the prior year. The $125.8 million decrease in Guernsey was primarily due to attrition as a result of the intense competition by European banks to attract new deposits at very high rates, as other forms of liquidity have dissipated due to the credit crisis. In the United Kingdom, deposits fell $204.1 million, primarily due to our exiting the SIPP deposit business.

Demand deposits, which include chequing accounts (both interest-bearing and non-interest-bearing), savings and call accounts, totalled $5.2 billion, or 69.7% of total customer deposits at year-end 2011, compared to $5.5 billion, or 67.9%, at year-end 2010. Term deposits decreased by 14.4% from $2.7 billion at year-end 2010 to $2.2 billion at year-end 2011 as customers moved to demand deposits given the low interest rate spread on longer-term deposits.

The cost of funds was 0.52% in 2011, down 13 basis points from the 0.65% paid in 2010, as a result of disciplined deposit pricing that contributed to the improvement in net interest income.

See "Note 11: Customer Deposits and Deposits from Banks" in the 31 December 2011 audited Financial Statements for additional tables and information.

Borrowings

We have no issuances of certificates of deposit ("CD"), commercial paper ("CP") or senior notes outstanding and have no CD or CP issuance programmes. The Bank had a $300 million committed line of credit that we cancelled in the second quarter of 2011. We are able to source funding on an uncommitted basis from a number of major banks, including our principal correspondent banks. We use funding from the inter-bank market as part of interest rate and liquidity management. At 31 December 2011, deposits from banks totalled $125.4 million, compared to $79.7 million at 31 December 2010.

Employee Future Benefits

As at 31 December 2011, the Bank had a substantial obligation for employee future benefits in the amount of $104.9 million, up $19.7 million from $85.2 million at year-end 2010. The increase is primarily the result of lower discount rates used to value the future obligations, in line with the general downward trend in interest rates, as well as lower than expected returns on plan assets.

In the second quarter of 2010, Shareholders' equity was bolstered by a combination of changes to post-retirement health care benefits. Following an independent, tri-annual actuarial review, the healthcare liability was reduced by approximately $27 million, reflecting changes in demographics and claims costs. Additionally, the Bank amended the plan for eligibility, benefits and cost sharing criteria, which resulted in a further reduction in the liability of approximately $41 million.

See "Note 12: Employee Future Benefits" in the 31 December 2011 audited Financial Statements for additional tables and information.

Subordinated Debt, Interest Payments and Maturities

We have outstanding issuances of subordinated debt with a carrying value of $267.8 million as at 31 December 2011, of which $260 million is issued in US dollars and £5 million in Great Britain pounds compared to $282.8 million as at 31 December 2010. All but $27.0 million of outstanding subordinated debt is eligible for inclusion in our Tier 2 regulatory capital base and is limited to 50% of Tier 1 capital.

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.

See "Note 19: Subordinated Capital" in the 31 December 2011 audited Financial Statements for additional tables and information.

Repurchase Agreements

We also obtain funds from time to time from the sale of securities to institutional investors under repurchase agreements. In a repurchase agreement transaction, we will generally sell an investment security, agreeing to repurchase either the same or a substantially identical security on a specified later date, generally not more than 90 days, at a price greater than the original sales price. The difference in the sale price and repurchase price is the cost of the use of the proceeds, or interest expense. The investment securities underlying these agreements may be delivered to securities dealers who arrange such transactions as collateral for the repurchase obligation. Repurchase agreements represent a cost competitive funding source and also provide liquidity on agency paper for us. However, we are subject to the risk that the borrower of the securities may default at maturity and not return the collateral. In order to minimise this potential risk when entering into such transactions, we generally deal with large, established investment brokerage firms with whom we have 'Master Repurchase' agreements. Repurchase transactions are accounted for as financing arrangements rather than as sales of such securities, and the obligation to repurchase such securities is reflected as a liability in our consolidated financial statements. No repurchase agreements were outstanding as at year-ends 2011 and 2010.

Shareholders' Equity

Shareholders' equity increased during the year ended 31 December 2011 by $20.4 million to $829.7 million, reflecting:

- $40.5 million net income for the year.
- $19.8 million from unrealised gains on AFS securities.
- $3.9 million of Share-based compensation.
- $0.8 million translation adjustments on foreign operations.

These increases were offset by:

- $23.4 million net increase in employee future benefits from the decline in interest rates used to discount the future cash flows, and lower than expected return on plan assets.
- $18.0 million Preference Share dividend and guarantee fee.
- $3.3 million cash dividends on CVCP Shares.

Capital Resources

One of Management's primary objectives is to maintain a strong capital base to promote confidence in the Bank among our clients, the investing public, bank regulators, rating agencies, and Shareholders. The Bank manages its capital both on a total Group basis and, where appropriate, on a legal entity basis. The Finance department has the responsibility for measuring, monitoring and reporting capital levels within guidelines and limits established by the Risk Policy & Compliance Committee of the Board. The management of capital will also involve regional Management when appropriate. In establishing the guidelines and limits for capital, a variety of factors are taken into consideration, including the overall risk of the business in stressed scenarios, regulatory requirements, capital levels relative to our peers, and the impact on our credit ratings.

The Bank is subject to Basel II, which is a risk-based capital adequacy framework developed by the Basel Committee on Banking Supervision and has been endorsed by the central bank governors and heads of bank supervision of the G10 countries. The Bank calculates its capital requirement on the Standardised approach under Basel II requirements. The Bank does not expect the changes being proposed to the capital adequacy ratios under Basel III to have a material impact on the Bank's capital ratios.

The Bank is fully compliant with all regulatory capital requirements and maintains capital ratios well in excess of regulatory minimums as at 31 December 2011.

As at 31 December 2011, the Bank's regulatory capital stood at $1,041.0 million with the consolidated Tier 1 total and total capital ratios being 17.7% and 23.5%, respectively (31 December 2010: 15.7% and 21.6%, respectively).

The following table sets forth our capital adequacy as at 31 December 2011 and 31 December 2010 in accordance with Basel II framework:

Year ended 31 December	2011	2010
(in $ millions)		
Capital		
Tier 1 capital	**781.4**	772.5
Tier 2 capital	**276.3**	310.3
Deductions	**(16.7)**	(15.3)
Total capital	**1,041.0**	1,067.5
Weighted Risk Assets		
Cash and cash equivalents and investments	**722.7**	957.6
Loans	**2,408.7**	2,552.2
Other assets	**401.7**	426.0
Off-Balance Sheet items	**320.2**	372.4
Operational risk charge	**572.3**	626.4
Total weighted risk assets	**4,425.6**	4,934.6
Capital Ratios (%)		
Tier 1 common	**13.1%**	11.6%
Tier 1 total	**17.7%**	15.7%
Total capital	**23.5%**	21.6%

Under Basel II Pillar III (market disclosure) the Bank is required to publish further information about the risks to which it is exposed. The Bank's Pillar III disclosures for the year ended 31 December 2011 will be published on the corporate website, www.butterfieldgroup.com, shortly after the publication of these Financials Statements.

Preference Shares

In June 2009, the Bank offered 200,000 of 8.00% Non-Cumulative Perpetual Limited Voting Preference Shares, liquidation preference of US $1,000 per share (the "Preference Shares") and $200,000,000 in the aggregate. The Preference Shares are fully and unconditionally guaranteed, with the full faith and credit of the Government of Bermuda (the "Guarantor"), as to payment of dividends for up to ten years and as to payment of the liquidation preference on, or in certain circumstances prior to, the ten-year anniversary of the date of issuance (the "Guarantee").

Dividends on the Preference Shares are payable quarterly on a non-cumulative basis, only when, as and if declared by our Board of Directors, on 15 March, 15 June, 15 September and 15 December of each year at a fixed rate equal to 8.00% per annum on the liquidation preference, commencing on 15 September 2009. In the event that, during the ten-year term of the Guarantee, the Bank does not pay full dividends in respect of any quarterly dividend period on any Preference Shares that are then issued and outstanding, the Guarantor has agreed to pay to holders of the Preference Shares an amount equal to such unpaid dividends pursuant to the Guarantee. The Bank may redeem the Preference Shares at its option, subject to approval of the Bermuda Monetary Authority ("BMA"), in whole or in part, on the tenth day prior to the ten-year anniversary of the date of issuance (the "Bank Redemption Date"), at a redemption price equal to 100% of the liquidation preference thereof plus any unpaid dividends for the then-current dividend period to the Guarantee End Date, regardless of whether any dividends are actually declared for such dividend period. In addition, the Bank may redeem the Preference Shares prior to the Bank Redemption Date, at its option, subject to approval of the BMA, in whole or in part, at any time and from time to time, at a redemption price equal to the Make-Whole Redemption Price. Unless previously redeemed, the Guarantor has agreed to purchase from the holders thereof, and such holders will be required to transfer to the Guarantor, on the ten-year anniversary of the date of issuance, all Preference Shares then issued and outstanding, at a price per Preference Share equal to the liquidation preference thereof plus any unpaid dividends for the then-current dividend period to the date of such purchase, regardless of whether any dividends are actually declared for such dividend period. In addition, upon the occurrence of a Liquidation Event at any time prior to the ten-year anniversary of the date of issuance of the Preference Shares, the Guarantor has agreed to purchase from the holders thereof, and such holders will be required to transfer to the Guarantor, all Preference Shares then issued and outstanding, at a price per Preference Share equal to the liquidation preference thereof plus any unpaid dividends for the then-current dividend period to the date of payment, regardless of whether any dividends are actually declared for such dividend period.

Capital Raise

On 2 March 2010, the Bank issued 144.8 million Common Shares of par value $1 per Share, for a consideration of $175.0 million and 281,770 Mandatorily Convertible Preference Shares of par value $0.01 per Share and 93,230 Contingent Convertible Preference Shares of par value $0.01 per Share, for a consideration of $281.8 million and $93.2 million, respectively.

Following the Bank's Annual General Meeting held on 8 April 2010, The Bank of N.T. Butterfield & Son Limited's Shareholders approved an increase in the authorised share capital to 26,000,000,000 Common Shares of par value BD$0.01. Subsequent to the increase, conversion of 281,770 Mandatorily Convertible Preference Shares into 233,157,035 Common Shares and 93,230 Contingent Convertible Preference Shares into 77,144,993 Common Shares took place.

At the Special General Meeting of Shareholders held on 14 April 2009, the Board of Directors were granted the authority to issue, allot or grant options, warrants or similar rights over or otherwise dispose of all the authorised but unissued Share capital of the Bank.

Rights Offering (See the *Rights Offering Prospectus* for details)

In March 2010, the Bank offered up to 99.3 million Common Shares and 8.3 million CVCP Shares in the form of up to 107.6 million Rights Units, each Unit consisting of 0.92038 Common Shares and 0.07692 CVCP Shares, for each Common Share held at a price of BD$1.21 per Rights Unit. Each qualifying Shareholder received 1.113 transferable rights to purchase 1 Rights Unit. Unallocated Rights Shares were available to qualifying Shareholders who exercised all the rights issued to them. Any unallocated Rights Shares remaining thereafter were available to qualifying holders of 8.0% Preference Shares.

Following the closing of the Rights Offering on 11 May 2010, the gross proceeds of $130 million were used to repurchase 107,571,361 Shares from the 2 March 2010 investors at the same price at which the investors originally subscribed for the Shares.

Contingent Value Convertible Preference Shares (See the *Rights Offering Prospectus* for details)

A holder of CVCP Shares has the option to convert any such Shares to Common Shares at any time. All CVCP Shares outstanding will automatically convert into Common Shares at the earlier of 31 March 2015 or a sale of the Bank. On such conversion, the CVCP Shares will convert into Common Shares at the Conversion Price. The initial Conversion Price shall be US$1.21 subject to any customary anti-dilution adjustments and certain downward notional adjustment based on certain loan recoveries.

A holder of CVCP Shares is entitled to certain distributions in connection with certain sales or public offerings of the Bank's equity interest in BFG. On 9 February 2011, the Bank announced that it has agreed to sell its minority ownership position in BFG to a new company founded by fund industry executives Tim Calveley and Glenn Henderson and private equity firm, BV Investment Partners. The sale transaction closed during the second quarter of 2011 and generated proceeds of $3.31 million. The completion of the sale triggered a dividend of $3.27 million ($0.42 per Share) to holders of Butterfield CVCP Shares, which was paid on 16 August 2011 to Shareholders of record on 26 July 2011. Through this transaction, the Bank has fully divested itself of its minority ownership stake in BFG. BFG now operates as a subsidiary of the new company. The Bank continues to provide BFG and its clients with commercial banking, foreign exchange and custody services. BFG was originally established in 2008 through the merger of Butterfield Fund Services and the Fulcrum Group.

When, as and if declared by the Board, holders of the outstanding CVCP Shares will be entitled to receive dividends based on the number of Common Shares into which the CVCP Shares would be convertible as of the dividend record date.

In the event of any voluntary or involuntary liquidation, dissolution or winding up of the affairs of the Bank, the holders of the CVCP Shares will be entitled to receive from its assets legally available for distribution to Shareholders as a liquidation preference before any distribution of assets is made to or set aside for the holders of any junior Shares, such as the Common Shares, the greater of (1) US$1.21 per CVCP Share plus any declared but unpaid dividends with respect to the then-current dividend period and (ii) the amount per CVCP Share that would be received if such CVCP Share had converted into Common Shares immediately prior to such liquidation, dissolution or winding up.

The CVCP Shares are issued as perpetual securities subject to conversion to Common Shares and shall not be redeemable by any holders at any time.

The holders of the CVCP Shares will vote together with the holders of the Common Shares on all matters upon which the holders of the Common Shares are entitled to vote. The CVCP Shares shall be entitled to such number of votes based on the number of Common Shares into which the CVCP Shares are convertible as of the applicable record date.

The class vote of the holders of at least 66.6% of the CVCP Shares shall be required for (i) the creation or issuance of Shares that are senior to liquidation, (ii) an amendment of rights of the CVCP Shares or (iii) a reclassification, merger, amalgamation or consolidation where the holders of CVCP Shares would not receive the consideration that would be received if such CVCP Shares had converted into Common Shares immediately prior to such event.

The CVCP Shares shall be privately transferable (subject to applicable securities laws and any required regulatory consents) but shall not be listed on the Bermuda Stock Exchange or any other Stock Exchange. The CVCP Shares will not be registered under the securities laws of any jurisdiction. This will result in a limited market for the CVCP Shares.

With respect to the 8.0% Preference Shares, the CVCP Shares rank pari passu as to liquidation and pari passu as to dividends and, with respect to Common Shares, the CVCP Shares rank senior as to liquidation and pari passu as to dividends (other than dividends relating to BFG, as to which the CVCP Shares rank senior).

As at 31 December 2011, there were 7.46 million CVCP Shares outstanding with 0.325 million Shares converted to Common Shares at the holders' option during the year ended as at 31 December 2011. As at 31 December 2011 there were no loan recoveries attributable to the CVCP Shares as defined in the certificate of designation. Consequently, the conversion factor to Common Shares at 31 December 2011 remained one to one (1:1). Loan recoveries mean the amount by which the cumulative amount of collections actually received by the Bank with respect to "Covered Loans" from and after 1 January 2010 and through (and including) the Measurement Date exceeds $102.3 million. In no event shall the loan recoveries exceed US$42.0 million. As at 31 December 2011, the carrying value of the covered loans was $27.9 million (2010: $58.5 million) reflecting charge-offs during the year as approved by the Audit Committee and reviewed by an independent committee of the Board of Directors.

Warrants

Following the Capital Raise on 2 March 2010, the terms of the 4,279,601 warrants with an exercise price of $7.01 previously issued to the Government of Bermuda in conjunction with the issuance of the Preference Shares in 2009 were adjusted in accordance with the terms of the guarantee. Subsequently, the Government of Bermuda now holds 4,150,774 warrants with an exercise price of $3.614.

Dividends

No Common Share dividends were declared or paid in 2011 or 2010. Preference Share dividends declared and paid were $16.0 million during 2011 (2010: $16.6 million) in relation to the 8% dividends. In 2011, a $3.3 million dividend was paid to holders of CVCP Shares triggered by the sale of the Bank's minority interest in BFG. Guarantee fees paid to the Government of Bermuda were $2.0 million during each of 2011 and 2010.

Cash Flows

Cash and cash equivalents were $2.0 billion as at 31 December 2011, compared to $2.4 billion in the prior year. The decrease is described below by category of operating, investing and financing activities.

For the year ended 31 December 2011, net cash provided by operating activities totalled $43.7 million (2010: $67.0 million). Cash flows from operating activities are generally the cash effects of transactions and other events that enter into the determination of net income. Cash provided by operating activities decreased by $23.3 million from 2010 to 2011, due primarily from the $50 million investment of seed money in the new BNY Mellon Butterfield Income Advantage Fund, classified as "trading investments" for accounting purposes. However, cash generated from operating activities before changes in trading investments increased $23.5 million on a rebound of cash earnings compared to the prior year.

Our investing activities include capital expenditures, loan activities, investment activities, and divestiture and acquisition activities. We do not own, directly or indirectly, any shares of stock or any other equity interest or long-term debt securities of any company, corporation, firm, partnership, joint venture, association or other entity, except pursuant to the ordinary course of investment activities, the strategic investment in an associated company or as a result of the ordinary course loan structuring. Net cash provided by investing activities for the year ending 31 December 2011 totalled $235.9 million compared $197.3 million in 2010. The $38.6 million increase in 2011 over 2010 was mainly due to a $594.8 million net cash provided from proceeds from the sale or maturity of AFS investments in 2011, compared to $95.3 million in 2010, offset by the movement in loans year over year (2011: increase of $255.1 million; 2010: decrease of $104.9 million).

Net cash used in financing activities totalled $736.4 million in 2011, compared to the $121.8 million in 2010. The $858.2 million decrease reflects the net cash used to fund deposit decreases of $701.2 million in 2011, compared to the $380.8 million decrease in deposits offset by the $521.0 million net issuance of Shares and rights in 2010.

OFF BALANCE SHEET ARRANGEMENTS

Assets Under Administration and Assets Under Management

The Bank, in the normal course of business, holds assets under administration and assets under management in a fiduciary or agency capacity for our clients. In accordance with US GAAP, these assets are not assets of the Bank and are not included in our Consolidated Balance Sheet.

Credit-Related Arrangements

We enter into standby letters of credit, letters of guarantee and contractual commitments to extend credit in the normal course of business, which are not required to be recorded on the Balance Sheet. Since many commitments expire unused or only partially used, these totals do not necessarily reflect future cash requirements. Management believes there are no material commitments to extend credit that represent risks of an unusual nature.

Standby letters of credit and letters of guarantee are issued at the request of our clients in order to secure a client's payment or performance obligations to a third party. These guarantees represent our irrevocable obligation 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 client. 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.

Credit risk is the principal risk associated with these instruments. The contractual amounts of these instruments represent the credit risk should the instrument be fully drawn upon and the client defaults. To control the credit risk associated with issuing letters of credit and letters of guarantee, we subject such activities to the same credit quality and monitoring controls as our lending activities. The types and amounts of collateral security we hold for these standby letters of credit and letters of guarantee is generally represented by our deposits or a charge over assets held in mutual funds. We are obligated to meet the entire financial obligation of these agreements and in certain cases are able to recover the amounts paid through recourse against the collateral security.

The following table sets forth the outstanding financial guarantees with contractual amounts representing credit risk:

As at 31 December			2011			2010
(in $ millions)	Gross	Collateral	Net	Gross	Collateral	Net
Standby letters of credit	321.0	303.8	17.2	386.7	354.3	32.4
Letters of guarantee	13.4	9.9	3.5	14.1	8.7	5.4
Total	334.4	313.7	20.7	400.8	363.0	37.8

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

Contractual Obligations (Including Subordinated Debt)

We enter into contractual commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. These credit arrangements are subject to our normal credit standards and collateral is obtained where appropriate. Substantially all of our commitments to extend credit are contingent upon clients 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.

In the second quarter of 2011, the Bank cancelled its commitment for a $300 million line of credit with CIBC as Management deemed it was no longer necessary. Whilst outstanding, the facility fees were $200,000 per month. In 2010, the Bank had incurred non-recurring fees of $7.48 million to setup the line of credit facility. A committed line of credit to our Bank in the Cayman Islands, from one of its custodians, was allowed to expire on its maturity on 31 December 2011. Both committed lines were exited as they were no longer required as part of the Bank's liquidity management programme.

The Bank entered into an asset liability management agreement with Carlyle Investment Management LLC ("Carlyle"), an affiliated company of the Carlyle Group with an effective date of 1 October 2010. Per the agreement Carlyle has agreed to provide Balance Sheet management advisory services to the Bank for an annual fee of $4.0 million until 1 October 2013.

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 2011, $137.1 million (2010: $174.5 million) of standby letters of credit were issued under this facility.

The contractual amounts for these commitments represent the maximum payments we would have to make should the contracts be fully drawn, the counterparty default, and any collateral held prove to be of no value. Commitments, when drawn, would be funded from our free cash resources.

We enter into other contractual obligations in the normal course of business. Certain of these obligations, such as subordinated debt, are recorded as liabilities in our Consolidated Balance Sheet. Other items, such as sourcing agreements, operating leases and other purchase contracts, are not required to be recorded on the Balance Sheet. Expected cash payments associated with subordinated debt are based on principal payment dates.

See "Note 19: Subordinated Capital" for terms of subordinated debt arrangements and interest rates.

The $112.5 million contractual obligation in respect of sourcing—for Bermuda and the Cayman Islands—relates to an eight-year agreement entered into in October 2008 with global technology service provider Hewlett Packard ("HP") (previously EDS) to supply technology infrastructure and application development management, information security and technical support for our locations in Bermuda and the Cayman Islands. In 2011, working with HP, we completed the transition of all our business applications and legacy systems in these locations to a new, common platform that will be centrally managed. Under our agreement with HP, server management and maintenance, technology field support, application support and development and help desk functions are managed by HP. In addition, HP managed the installation of and conversion to our new, common core banking system in Bermuda and the Cayman Islands which went live in 2011. The transition of functional responsibility for information technology management and support, and the implementation of a new core banking system were completed in the Cayman Islands in the second quarter and in Bermuda in the fourth quarter. Under the agreement, we have the option to expand HP's service to our other locations, subject to agreement on an expansion plan and fees.

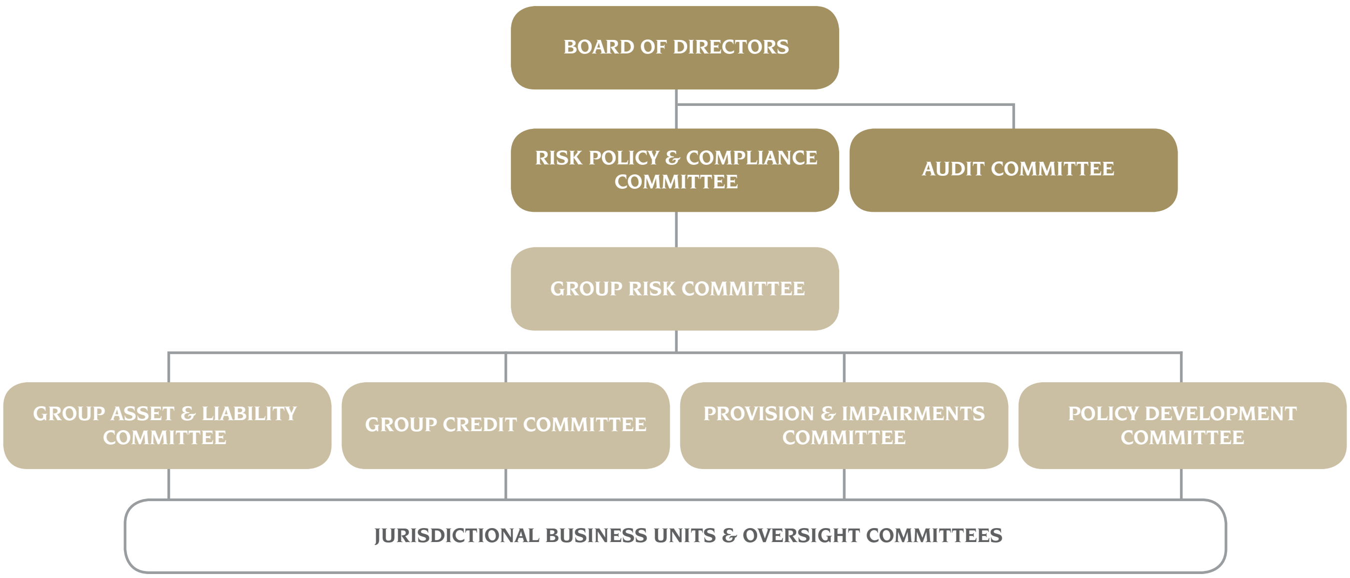
We believe that our arrangement with HP will help us optimise operations, improve productivity and enhance client service. We expect to derive synergies in the form of cost savings over time. The management and coordination of our international information technology functions will continue to be carried out from our head office in Bermuda.

We have entered into additional contractual obligations in the normal course of business which are not significant to the amounts above.

RISK MANAGEMENT

Risk Governance

The Group's risk governance and management structure is illustrated below:



The Board of Directors oversees the Group's risk management programme through the approval of the Risk Appetite Framework and supporting risk management policies. It accomplishes its mandate through the activities of two dedicated Committees:

The Risk Policy & Compliance Committee

This Committee assists the Board in fulfilling its responsibilities by overseeing the Group's risk profile and its performance against approved risk appetites and tolerance thresholds. Specifically, the Committee considers the sufficiency of the Group's policies, procedures and limits related to the identification, measurement, monitoring and control of activities that give rise to credit, market, liquidity, interest rate, operational and reputational risks, as well as overseeing its compliance with laws, regulations and codes of conduct.

The Audit Committee

This Committee reviews the overall adequacy and effectiveness of the Group's system of internal controls and the control environment, including those that are brought to bear in respect of the risk management process. It reviews recommendations arising from internal and independent audit review activities and Management's response to any findings raised.

Both the Risk Policy & Compliance Committee and the Audit Committee are supported in the execution of their respective mandates by the dedicated Audit, Compliance & Risk Policy Committees for our UK, Guernsey and Caribbean operations, which oversee the sufficiency of local risk management policies and procedures and the effectiveness of the system of internal controls that are in place. These Committees are chaired by Non-Executive Directors drawn from our jurisdictional Boards.

The Group Executive Management team, led by the President & Chief Executive Officer ("CEO") and including the members of Executive Management reporting directly to the CEO, is responsible for setting business strategy and for monitoring, evaluating and managing risks across the Group. It is supported by the following committees:

The Group Risk Committee (GRC)
This is the Senior Management Committee with responsibility for risk governance. It provides a forum for the strategic assessment of risks assumed across the Group as a whole, based on an integrated view of credit, market, liquidity, legal and regulatory compliance, operational, interest rate, investment, capital and reputational risks, ensuring that these exposures are consistent with the risk appetites and tolerances promulgated by the Board. It is responsible for reviewing, evaluating and recommending the Group's Risk Appetite Framework, the results of the Capital assessment and risk profile ("CARP") process (including all associated stress testing performed) and the Group's key risk policies to the Board of Directors for approval, for reviewing and evaluating current and proposed business strategies in the context of our risk appetites and for identifying, reviewing and advising on current and emerging risk issues and associated mitigation plans.

Its membership is drawn from the Group Executive Management team, including the CEO. The meeting is chaired by the Chief Risk Officer.

The Group Asset & Liability Committee
This Committee is responsible for liquidity, interest rate and exchange rate risk management and other Balance Sheet issues. It also oversees the execution of the Group's investment and capital management strategies and monitors the associated risks assumed. It is supported in the execution of its mandate by the work undertaken by the dedicated Asset & Liability Committees in each of the Bank's jurisdictional business units.

Its membership is drawn from the Group Executive and Senior Management teams, including the Chief Risk Officer and the CEO. The meeting is chaired by the Chief Financial Officer.

The Group Credit Committee
This Committee is responsible for a broad range of activities relating to the monitoring, evaluation and management of credit risks assumed across the Group, at both transaction and portfolio levels. It is supported in the execution of its mandate by the Financial Institutions Committee, a dedicated Sub-Committee that is responsible for the evaluation and approval of recommended inter-bank and counterparty exposures assumed in the Group's treasury and investment portfolios, and by the activities of local Credit Committees in the UK, Guernsey, and the Caribbean, which review and approve transactions within delegated authorities and recommend specific transactions outside of these limits to the Group Credit Committee for approval.

Its membership is drawn from the Group Executive and Senior Management teams. The meeting is chaired by the Chief Risk Officer.

The Provisions & Impairments Committee
This Committee is responsible for approving significant provisions and other impairment charges. It also oversees the overall credit risk profile of the Group in regard to non-accrual loans and assets. It is supported in the execution of its mandate by local Credit Committees and the Group Credit Committee, which make recommendations to this Committee.

Its membership is drawn from the Group Executive Management team, including the CEO. The meeting is chaired by the Chief Risk Officer.

The Policy Development Committee
This Committee is responsible for overseeing the design, development and maintenance of the Group's framework of operational policies. It develops recommendations regarding policy requirements, engages with nominated members of Executive Management to ensure that policies are drafted or updated on a timely basis and provides a forum through which they are debated Group-wide prior to their adoption, thereby ensuring a consistency of application and interpretation. It also ensures that all policies and any policy exception requests are reviewed and recommended prior to presentation to the Group Risk Committee or Risk Policy & Compliance Committee of the Board for approval.

Its membership is drawn from the Senior Management team across the Group. It is chaired by the Group Head of Compliance.

Risk Management
The Group manages its exposure to risk through a three "lines of defence" model. This may be summarised as follows:

The first "line of defence"
This is provided by our jurisdictional business units, which retain ultimate responsibility for the risks they assume and for bearing the cost of risk associated with these exposures.

The second "line of defence"
This is provided by the Risk Management group, which works in collaboration with our business units to identify, assess, mitigate and monitor the risks associated with our business activities and strategies. It does this by:

- Making recommendations to the Group Risk Committee regarding the constitution of the Risk Appetite Framework.
- Setting risk strategies that are designed to manage risk exposures assumed in the course of pursuing our business strategies and aligning them with agreed appetites.
- Establishing and communicating policies, procedures and limits to control risks in alignment with these risk strategies.
- Measuring, monitoring and reporting on risk levels.
- Opining on specific transactions that fall outside delegated risk limits.
- Identifying and assessing emerging risks.

The four functions within the Risk Management group that support our risk management activities are outlined below. To ensure a formal separation of duties, each reports directly to the Chief Risk Officer.

Group Market Risk – This provides independent oversight of the measurement, monitoring and control of liquidity and funding risks, interest rate and foreign exchange risks as well as the market risks associated with the Group's investment portfolios. It also monitors compliance with both regulatory requirements and the Group's internal policies and procedures relating to the management of these risks.

Credit Risk Management – This unit is responsible for the adjudication and oversight of credit risks associated with our retail and commercial lending activities and the management of risks associated with our investment portfolios and counterparty exposures. It also establishes the parameters and delegated limits within which credit risks may be assumed and promulgates guidelines on how exposures should be managed and monitored.

Compliance – This unit provides independent analysis and assurance of the Group's compliance with applicable laws, regulations, codes of conduct and recommended best practices, including those associated with anti-money laundering/counter terrorist financing requirements. It is also responsible for assessing the Group's potential exposure to upstream risks and for providing guidance on the preparations that should be made in advance of these changes coming into effect.

Group Operational Risk – This unit assesses the effectiveness of the Group's procedures and internal controls in managing its exposure to various forms of operational risk, including those associated with new business activities and processes and the deployment of new technologies. It also oversees the Group's incident management processes and reviews the effectiveness of its loss data collection activities.

The third "line of defence"
This is provided by our Group Internal Audit function, which provides ongoing review, oversight and challenge of the effectiveness of the internal controls that are executed by both the business and Risk Management communities in the management, monitoring and measurement of our exposure to risk. This includes the review of the accuracy of the underlying data and appropriateness of the stress testing methodologies that are executed as a part of our CARP process.

The Risk Appetite Framework
The Risk Appetite Framework is the cornerstone of our approach to risk management. Developed by Executive Management and approved formally by the Board of Directors, it communicates a willingness to take on certain risks in the pursuit of our strategic objectives and defines those that should be avoided. It also provides Management with a clear mandate regarding the amount and type of risk that it may accept and establishes minimum expectations regarding the practices and behaviours that should be brought to bear in managing the exposures assumed. It is aligned with the interests of our stakeholders, feeds into our business planning processes, and shapes our discussions on risk matters generally.

Our framework comprises the following elements:

(i). Nine broad categories of risk: Credit; Market; Liquidity; Legal & Regulatory; Governance; Process & Technology; People, Country & Political; and Reputational. These represent the various risks that the Group assumes across the entirety of its operations in the pursuit of its strategic goals.

(ii). For each risk category, there is a declared risk appetite. To ensure consistency in our risk conversations, these have been distilled into the three options set out in the table below, with each appetite designed to convey a clear strategic direction in terms of the risk/reward profile assumed:

APPETITE	DEFINITION	PROFILE
Averse	The Group will work to avoid exposure to this risk given its potential for financial loss, reputational damage, and/or the loss of customer and/or investor confidence.	Our processes and controls are defensive and focus on detection and prevention.
Cautions	Given the potential for financial loss, reputational damage, and the loss of customer and/or investor confidence, the Group will be very selective in the exposures assumed to this risk and will monitor it closely.	Security is favoured over reward. Exposures are only assumed when the risk can be quantified accurately and is assessed as being acceptable.
Open	The Group will consider opportunities to accept this risk and will accept those that fall within clearly defined parameters. The risk of loss or reputational damage is accepted but the exposure can be estimated reliably and can be managed to a tolerable level.	Reward is commensurate with the risk assumed. Exposures can be estimated reliably and structures, systems and processes are in place to manage it.

(iii). A statement of our governing principles relating to each risk category. This establishes the characteristics of the risks that the Bank is willing to assume and the management behaviours that we should exhibit when doing so.

Specific performance measures and tolerance thresholds in respect of each risk category, combining quantitative and qualitative targets (which are designed to reflect both forward looking as well as historical perspectives), are designed to provide Executive Management and the Board with an indication of the “direction” of our exposure relative to our declared risk appetite and an early warning of material adverse developments requiring remedial action. The metrics are monitored independently by the Group Risk function and are measured against actual results. The results of these analyses are reported to Management at all levels of the organisation and are reviewed regularly by both the Group Risk and Risk Policy & Compliance Committees in the performance of their oversight activities.

Application Of The Risk Appetite Framework

The limits, targets and thresholds used to measure performance continue to be refined by the Group Risk Management function in an effort to express as complete a “picture” as possible of our exposure to a given risk, relative to the stated appetite. All changes proposed pass through a formal review and approval process at both the Executive Management and Board levels prior to their adoption.

Through this approach, the Risk Appetite Framework sets the tone for our risk culture across the Group as a whole, influencing behaviours at all levels of the organisation and reinforcing accountability for decisions taken. Many of our Jurisdictional offices have developed subsidiary risk appetite frameworks in conjunction with their local Risk Management functions. This ensures appropriate coverage of local risk factors and the establishment of proportional tolerance thresholds. Group Risk has reviewed these frameworks prior to their adoption and has modified any appetites proposed that are considered to be inconsistent with the overall Group approach.

Credit Ratings

Our credit ratings are provided in the table below:

	Standard & Poor’s	Moody’s	Fitch
Short-term deposits	A-2	P-1	F1
Long-term deposits and debt	A-	A2	A-
Outlook	Negative	Negative	Stable

JURISDICTION AND GROUP BUSINESS OVERVIEWS

BARBADOS

Total revenues before gains and losses in Barbados were down 6.6% year over year, primarily due to lower earnings from net interest income offset by reduced credit provisions. There was a weak demand for credit in the local market during the year, reflective of continued slowness in the Barbados economy.

Throughout 2011, tight cost management was a major strategy of Butterfield in Barbados. In line with this strategy, the Bank restructured its operations, resulting in a reduced workforce and an overall reduction in non-interest expense of 12.5% year over year.

In terms of community support, the Bank continued its title sponsorship of the Barbados Seniors' Expo.

(in $ thousands)	**2011**	**2010**	**$ change**	**% change**
Net interest income	11,485	12,917	(1,432)	(11.1)
Provision for credit losses	(1,156)	(1,707)	551	(32.3)
Non-interest income	2,896	2,948	(52)	(1.8)
Revenue before gains and losses	13,225	14,158	(933)	(6.6)
Total expenses	12,135	13,863	(1,728)	(12.5)
Net income before gains and losses	1,090	295	795	269.5
Net gains (losses)	37	(151)	188	(124.5)
Net income	**1,127**	**144**	**983**	**682.6**
As at 31 December				
(in $ millions)				
Customer deposits	269	240	29	12.1
Loans, net of allowance for credit losses	178	185	(7)	(3.8)
Total assets	**304**	**274**	**30**	**10.9**
Number of employees	**114**	**138**	**(24)**	**(17.4)**

BERMUDA

Bermuda is home to Butterfield's headquarters and remains the Bank's largest jurisdiction in terms of number of employees, Banking Centre locations and business volume. The Bank of N.T. Butterfield & Son Limited ("Butterfield") is Bermuda's first and largest independent bank, offering a full range of community banking services and wealth management, including private banking, asset management and personal trust services. Butterfield also provides services to corporate and institutional clients, which include asset management and corporate trust services.

Bermuda's revenue before gains and losses increased year over year by $38.8 million, or 24.4%, reflecting higher interest income, decreased interest expense, and decreased provisions for credit losses offset against decreased non-interest income.

The Bank has stabilised its exposure to the hospitality industry. The Bank has taken action to place two hotel properties in Bermuda in receivership, where it was deemed to be the best course of action to protect the value of assets and safeguard the interests of the Bank's Shareholders. The properties are being managed professionally with a view to selling them as going concerns as soon as appropriate arrangements can be reached.

Loans secured by commercial office buildings continue to perform well, whilst residential mortgage delinquencies have risen modestly and remain low by international standards.

Credit provisions were $25.6 million in 2010 compared to $1.2 million in 2011, primarily due to the release of provisions during the year relating to real estate received in settlement of loans outstanding. As a result, net income was up $208.9 million to $25.8 million for the year ended 31 December 2011. Total assets were $4.6 billion at 31 December 2011, down $0.6 billion from 31 December 2010. Assets under management were $3.4 billion at 31 December 2011, down from $3.6 billion at 31 December 2010, reflecting the net redemptions, whilst assets under administration for our trust and custody businesses at 31 December 2011 were $24.7 billion and $21.8 billion, respectively, compared to $22.8 billion and $19.6 billion at 31 December 2010.

Against a backdrop of economic difficulties locally, and despite the impact they had on the Bank's performance in 2011, Butterfield has reaffirmed our commitment to supporting the third sector, locally. The Bank believes that its long-term success and growth as an organisation depends on the prosperity of the communities it serves. In 2011, the Bank reduced the total amount it donated to local charities in Bermuda, but refocused its giving efforts on human services.

(in $ thousands)	2011	2010	$ change	% change
Net interest income	131,937	113,363	18,574	16.4
Provision for credit losses	(1,202)	(25,650)	24,448	(95.3)
Non-interest income	67,081	71,325	(4,244)	(6.0)
Revenue before gains and losses	197,816	159,038	38,778	24.4
Total expenses	176,726	192,174	(15,448)	(8.0)
Net income before gains and losses	21,090	(33,136)	54,226	(163.6)
Net gains (losses)	4,754	(149,940)	154,694	(103.2)
Net income (loss)	**25,844**	**(183,076)**	**208,920**	**(114.1)**
As at 31 December				
(in $ millions)				
Customer deposits	3,260	3,605	(345)	(9.6)
Loans, net of allowance for credit losses	2,507	2,505	2	0.1
Total assets	**4,578**	**5,193**	**(615)**	**(11.8)**
Assets under administration				
Custody and other administration services	21,761	19,633	2,128	10.8
Trust	24,735	22,835	1,900	8.3
Assets under management				
Butterfield Funds	2,653	2,870	(217)	(7.6)
Other assets under management	752	746	6	0.8
Total assets under management	**3,405**	**3,616**	**(211)**	**(5.8)**
Number of employees	**664**	**732**	**(68)**	**(9.3)**

CAYMAN ISLANDS

Cayman is Butterfield's second largest jurisdiction in terms of business and market presence. The Bank offers a full range of personal and corporate financial services in the Cayman Islands and is among the leaders in this highly competitive market. To complement Butterfield's strong retail banking presence, Butterfield Bank (Cayman) Limited continued to focus on developing its wealth management businesses. For the second year in a row, Butterfield's private banking service in Cayman was named "Best Private Bank in the Cayman Islands" by *Euromoney*'s Private Banking and Wealth Management Survey, considered the benchmark of excellence in international private wealth management. In April, the Bank implemented its new banking platform providing the basis for future client service offerings.

Net income before gains and losses of $9.0 million improved 28.6%, whilst the year-on-year improvement in net income in Cayman was primarily attributable to the realised gains on sale of $2.0 million in the current year compared to realised losses of $11.6 million on the sale of asset-backed securities in the Available For Sale portfolio in the prior year. Net interest income improved 30.6% year over year, to $37.3 million, whilst non-interest income declined by 5.4% to $30.6 million, resulting from decreases in net banking services revenues due to increases in credit card servicing costs, reduced asset management fees, trust fees and foreign exchange commissions. While Cayman experienced steady growth in residential mortgages in 2011, absorbing the Bahamas-based residential mortgage book and participating in several commercial lending deals with its parent led to an increase in the Bank's loan book of $114 million, or 18.8% year on year.

Total expenses were $55.0 million in 2011, up $4.8 million from $50.2 million in 2010, due to increased technology and communication costs driven by the Bank's outsourced I.T. services model and new operating systems implemented in April, including depreciation of its software fixed asset during the balance of the year. There were increases in professional and outside services costs related to asset liability management services and investment advice, along with additional cost associated with auditing the current year's system conversion. Provisions for credit losses were up 4.4% to $4.0 million on certain overseas investment mortgages, certain commercial loans and overall loan growth year over year. Total assets, at $2.0 billion, were down $63 million or 3.1%. Client assets under administration decreased by 25.6% to $3.4 billion, due primarily to declines in the value of assets relating to trust clients.

In 2011, Butterfield continued to demonstrate its commitment to the Cayman Islands by supporting high-profile economic development events and charitable causes. The Bank provides financial support and board representation to the Cayman Islands Banker's Association and Cayman Finance, the industry-led organisations that foster the ongoing development of financial services in the Cayman Islands. Butterfield also had a prominent showing at the Cayman Captive Forum conference.

Butterfield sponsored the nineteenth annual St. Patrick's Day Irish Jog, benefiting The Lighthouse School, Cayman's only school for special needs children. Butterfield Cayman continues to be a major contributor to organisations such as Cayman Hospice Care, the Cayman Heart Fund, the Cancer Society, the Cayman Islands Red Cross, Cayman Islands Little League and Junior Squash. Additionally, 2011 saw the launch of the Butterfield Education Grant, where schools compete for a grant of $20,000 to fund specific initiatives.

(in $ thousands)	**2011**	**2010**	**$ change**	**% change**
Net interest income	37,325	28,571	8,754	30.6
Provision for credit losses	(3,974)	(3,808)	(166)	4.4
Non-interest income	30,650	32,389	(1,739)	(5.4)
Revenue before gains and losses	64,001	57,152	6,849	12.0
Total expenses	54,988	50,145	4,843	9.7
Net income before gains and losses	9,013	7,007	2,006	28.6
Net gains (losses)	1,955	(11,600)	13,555	(116.9)
Net income (loss)	**10,968**	**(4,593)**	**15,561**	**(338.8)**
As at 31 December				
(in $ millions)				
Customer deposits	1,743	1,781	(38)	(2.1)
Loans, net of allowance for credit losses	722	608	114	18.8
Total assets	**1,974**	**2,037**	**(63)**	**(3.1)**
Assets under administration				
Custody and other administration services	1,226	1,187	39	3.3
Trust	2,188	3,401	(1,213)	(35.7)
Assets under management				
Butterfield Funds	211	270	(59)	(21.9)
Other assets under management	760	837	(77)	(9.2)
Total assets under management	**971**	**1,107**	**(136)**	**(12.3)**
Number of employees	**308**	**326**	**(18)**	**(5.5)**

GUERNSEY

In Guernsey, Butterfield offers private banking, lending, asset management, custody, administered banking and fiduciary services.

Net interest income increased by $6.0 million, from $12.4 million in 2010, to $18.4 million in 2011, from the purchase of higher-yielding, longer duration assets, and strong growth in our lending book. Non-interest income decreased by $1.3 million from $23.0 million in 2010 to $21.7 million in 2011, from the loss of two administered bank mandates and lower foreign exchange revenues, compensated in part, by increases in asset management revenues. Total expenses increased by $2.6 million to $30.2 million for the year ended 31 December 2011, due to increases in professional and advisory fees in 2011 coupled with a non-recurring expense recovery in 2010. Total assets at 31 December 2011 were $1.5 billion, down from $1.6 billion at 31 December 2010, due to customer deposit balances reducing by $128 million, offset by year-on-year exchange translation variances. Loans increased $120 million to $453 million from $333 million at 31 December 2010 as a direct result of our strategy to increase our lending balances with high net worth clients investing in high end residential prime property. Client assets under administration were $16.7 billion at 31 December 2011, up from $16.4 billion a year earlier.

Butterfield in Guernsey has continued to support initiatives and its profile in the local community through sponsorships of the Guernsey Volleyball Junior Development Programme, the Guernsey Squash Rackets Association's Racketball coaching programme and Guernsey Annual Squash Open, The Guernsey Sinfonietta, as well as the Classic Yacht Regatta, which was hosted on the island.

To build upon the Group's reputation and profile in the area of fiduciary services, sponsorship was provided for the Society of Trust and Estate Practitioner's Asia conference held in Singapore. Support for promotional initiatives led by Guernsey Finance was also provided with a secondary sponsorship at the 2011 Guernsey Funds Forum held in London.

(in $ thousands)	2011	2010	$ change	% change
Net interest income	18,379	12,384	5,995	48.4
Non-interest income	21,664	23,003	(1,339)	(5.8)
Revenue before gains and losses	39,406	35,387	4,019	11.4
Total expenses	30,245	27,625	2,620	9.5
Net income before gains and losses	9,161	7,762	1,399	18.0
Net gains (losses)	242	(1,433)	1,675	(116.9)
Net income	**9,403**	**6,329**	**3,074**	**48.6**
As at 31 December				
(in $ millions)				
Customer deposits	1,334	1,462	(128)	(8.8)
Loans, net of allowance for credit losses	453	333	120	36.0
Total assets	**1,480**	**1,618**	**(138)**	**(8.5)**
Assets under administration				
Custody and other administration services	6,714	5,694	1,020	17.9
Trust	9,944	10,754	(810)	(7.5)
Assets under management				
Butterfield Funds	141	180	(39)	(21.7)
Other assets under management	447	512	(65)	(12.7)
Total assets under management	**588**	**692**	**(104)**	**(15.0)**
Number of employees	**165**	**166**	**(1)**	**(0.6)**

UNITED KINGDOM

In the UK, Butterfield Private Bank provides a range of exclusive banking, lending, treasury and investment management services. This includes family office services to high net worth international clients and their advisers from offices in London.

The UK's net loss of $3.3 million in 2011 was a result of credit provisions relating to historical non-core private banking business. These specific loan loss provisions generated a realised loss, net of tax, of $4.7 million. Total revenues before gains and losses were $16.9 million, up $4.6 million from $12.3 million as a result of an increase in UK residential lending and a higher return the Bank achieved on its debt securities in 2011. At 31 December 2011, total assets were $1.0 billion, down $129 million due to the decrease in customer deposits, mainly reflecting the strategic decision to exit non-core private banking business.

During 2011, Butterfield re-focused its business on providing exclusive private banking and wealth management services to wealthy clients and their families through the exit of non-core business. As part of a re-focused private banking strategy, the Bank enhanced its credit offering through the recruitment of a specialist team of experienced relationship managers to meet the demand of its clients. The Bank's lending focus is on providing lending services to wealthy clients at modest loan-to-value ratios secured on prime Central London residential property.

The Bank made a number of small donations to a range of charities connected with private clients during the year.

(in $ thousands)	**2011**	**2010**	**$ change**	**% change**
Net interest income	12,688	9,381	3,307	35.3
Provision for credit losses	(6,724)	(7,136)	412	(5.8)
Non-interest income	10,929	10,027	902	9.0
Revenue before gains and losses	16,893	12,272	4,621	37.7
Total expenses	20,253	16,088	4,165	25.9
Net income before gains and losses	(3,360)	(3,816)	456	(11.9)
Gains and losses	45	(9,964)	10,009	(100.5)
Net loss	**(3,315)**	**(13,780)**	**10,465**	**(75.9)**
As at 31 December				
(in $ millions)				
Customer deposits	735	939	(204)	(21.7)
Loans, net of allowance for credit losses	434	415	19	4.6
Total assets	**976**	**1,105**	**(129)**	**(11.7)**
Assets under administration				
Custody and other administration services	**1,276**	**1,263**	**13**	**1.0**
Assets under management				
Butterfield Funds	330	331	(1)	(0.3)
Other assets under management	309	296	13	4.4
Total assets under management	**639**	**627**	**12**	**1.9**
Number of employees	**101**	**109**	**(8)**	**(7.3)**

GROUP ASSET MANAGEMENT

Butterfield Asset Management focuses on fulfilling the financial needs of those who demand the highest level of service and expertise. Clients have direct access to their portfolio managers who are, in turn, supported by a Group investment discipline designed to leverage resources from across the organisation, including a Core Strategy & Research Team based in London.

The Group provides a broad range of investment services to institutional and private clients in Bermuda, the Cayman Islands, Guernsey, and the United Kingdom. Principal services include discretionary investment management and managed portfolio services. Advisory and self-directed brokerage offerings are available to clients in Bermuda and the Cayman Islands. The Group also offers money market and mutual funds to both client bases. Institutional clients consist primarily of captive insurance companies in Bermuda and the Cayman Islands. High net worth private clients and their fiduciary vehicles are served from all four jurisdictions. Retail and mass affluent clients are served out of Bermuda and the Cayman Islands as part of the Bank's community banking platform.

Group Asset Management revenues increased by $0.3 million in 2011, largely attributable to a change in the mix of services favouring higher margin offerings.

Assets under management decreased by $0.4 billion (7.1%) to $5.6 billion in 2011, largely due to a fall in money market balances in Cayman and particularly Bermuda as clients sought better yielding alternatives for short-term investments. In addition, Cayman institutional assets under management declined as insurance captives moved to manage more of their assets onshore. Private client asset growth was strong in the first half of the year, especially in the UK. In the second half of the year, private clients were increasingly reluctant to invest in correcting and volatile markets and select large trust mandates concluded as scheduled in Guernsey.

Non-interest income		**Asset Management**	
(in $ thousands)	**2011**	**2010**	**$ change**
Bermuda	8,858	9,396	(538)
Cayman Islands	4,150	4,407	(257)
Guernsey	4,255	3,784	471
UK	5,679	5,078	601
Total	**22,942**	**22,665***	**277**

*Excludes non-interest income of $1.9 million attributable to the Hong Kong subsidiary disposed on 8 September 2010.

Note: *the above amounts quoted are net of inter-jurisdiction eliminations.*

Total assets under management ("AUM") at 31 December:

		2011			**2010**	
	Butterfield	**Other**		**Butterfield**	**Other**	
(in $ millions)	**Funds**	**assets**	**Total AUM**	**Funds**	**assets**	**Total AUM**
Bermuda	2,653	752	3,405	2,870	746	3,616
Cayman Islands	211	760	971	270	837	1,107
Guernsey	141	447	588	180	512	692
The Bahamas	40	1	41	26	9	35
UK	330	309	639	331	296	627
Total	**3,375**	**2,269**	**5,644**	**3,677**	**2,400**	**6,077**

GROUP TRUST

Our trust and corporate services specialists deliver fiduciary solutions to meet a range of client needs, including estate and succession planning, administration of complex asset holdings, and tax-efficient co-ordination for the affairs of international families, the pension and employee benefit planning requirements of multi-national corporations and institutions.

We provide both personal and institutional trust services from our operations in Bermuda, The Bahamas, the Cayman Islands, Guernsey and Switzerland, with our multi-jurisdictional capability therefore spanning the world's leading international trust and fiduciary centres.

Alongside our traditional strengths in providing services to families and institutions with links to the United Kingdom, North America and Europe, our business increasingly supports clients connected to the Asian and Latin American regions.

Our goal is to develop long-term relationships with our clients, based on consistently reliable service and underpinned by the technical expertise and competencies of our team. To this end, training and continual professional development for our staff remained a key priority in 2011. Following our selection as The Society of Trust and Estates Professional's (STEP) Institutional Trust Company of the Year in 2009/10, we were pleased to be recognised as one of *Private Client Practitioner*'s Top 25 Trust Companies in 2011. Butterfield Trust (Switzerland) Limited also received a nomination as Swiss Trust Company of the Year for *Citywealth*'s 2012 Offshore Awards.

Trust revenues are derived from a combination of fixed fees, fees based on the market values of assets held in trust and fees based on time spent in relation to the range of personal trust and company administration services and pension and employee benefit trust services we provide.

In 2011, trust revenues totalled $30.0 million, almost 2% higher than the $29.5 million recorded in 2010, excluding $1.0 million in revenue related to the Malta business that was sold in 2010. Revenue increases were seen in four of our five trust operations: The Bahamas was up 4.3%, Bermuda increased 3.6% and Guernsey rose 1.7%, while in Switzerland revenues were up 38.2% year on year. In December 2010, a restructuring of our Bahamas operations to focus predominantly on trust activities was announced. In September 2010, the Bank concluded the sale of its trust operations located in Malta, which did not contribute significantly to this line of business. Total Trust assets under administration were $40.7 billion as at 31 December 2011, compared to $40.5 billion the prior year.

The tables below shows trust revenues by jurisdiction, followed by assets under administration.

Non-interest income		Trust	
(in $ thousands)	**2011**	**2010**	**$ change**
Bermuda	13,166	12,704	462
Cayman Islands	4,879	5,263	(384)
Guernsey	6,549	6,437	112
Switzerland	677	490	187
The Bahamas	4,180	4,009	171
UK	544	607	(63)
Total	**29,995**	**29,510***	**485**

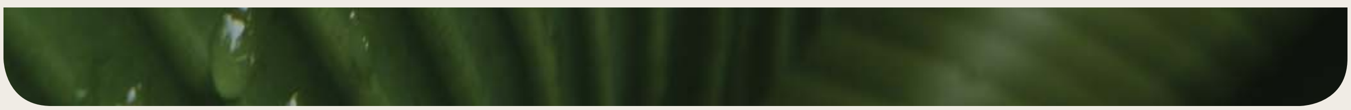
*Excludes non-interest income of $1.0 million attributable to the Malta subsidiary disposed on 8 September 2010.

Note: *the above amounts quoted are net of inter-jurisdiction eliminations.*

Total Trust assets under administration ("Trust AUA") at 31 December:

(in $ millions)	**2011**	**2010**
Bermuda	24,735	22,835
Cayman Islands	2,188	3,401
Guernsey	9,944	10,754
Switzerland	386	349
The Bahamas	3,439	3,172
UK	-	-
Total	**40,692**	**40,511**

Financials



MANAGEMENT'S FINANCIAL REPORTING RESPONSIBILITY

The Management of The Bank of N.T. Butterfield & Son Limited is responsible for the preparation of the Consolidated Financial Statements contained in this Report, which covers all of the interests of the Bank. Management has fully disclosed its income, assets, liabilities and off Balance Sheet commitments. These Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America and, where appropriate, are based on the best estimates and judgement of Management.

Management has established and maintains a system of financial reporting and internal controls to provide reasonable assurance that transactions are properly authorised and recorded, assets are protected against unauthorised use or disposition and liabilities are recognised. These procedures include the careful selection and training of qualified staff, the establishment of organisational structures providing an appropriate and well-defined division of responsibilities, and the communication of policies and standards of business conduct throughout the Bank.

The system of internal controls is further supported by a professional staff of internal auditors who conduct periodic inspections of all aspects of the Bank's operations. In addition, the Bank's Head of Group Internal Audit reports to, and has full and free access to the Audit Committee of the Board of Directors.

The Audit Committee, composed entirely of Directors who are not employees of the Bank, reviews the Financial Statements before such Statements are approved by the Board of Directors and submitted to the Bank's Shareholders. The Committee meets and consults regularly with Management, the internal auditors and our external independent auditors to review the scope and results of their work.

Under the provisions of the Bermuda Monetary Authority Act 1969, the Bermuda Monetary Authority is charged with the supervision of the Bank. Such supervision is in line with international practices and combines a comprehensive system of statistical returns, providing a detailed breakdown of the Balance Sheet and Statement of Income accounts of the Bank, and regular meetings with the senior Management of the Bank. Such regular reviews are intended to satisfy the Authority that the safety and interests of the depositors, creditors and Shareholders of the Bank are being duly observed and that the Bank is in a sound financial condition.

The accounting firm of PricewaterhouseCoopers, the Shareholders' independent auditors, has examined the Consolidated Financial Statements of the Bank in accordance with auditing standards generally accepted in the United States of America and have expressed their opinion in their report to the Shareholders. The auditors have unrestricted access to, and meet periodically with, the Audit Committee to review their findings regarding internal controls over the financial reporting process, auditing matters and financial reporting issues. Management has made available to PricewaterhouseCoopers all of the Bank's financial records and related data, as well as the minutes of Shareholders' and Directors' meetings.

Bradford Kopp
President & Chief Executive Officer
29 February 2012

Bradley Rowse
Executive Vice President & Chief Financial Officer
29 February 2012

pwc

February 29, 2012

To the 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 changes in shareholders' equity and comprehensive income (loss), 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 2011 and 2010, 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 Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements 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.

PricewaterhouseCoopers

Chartered Accountants

PricewaterhouseCoopers, Chartered Accountants, P.O. Box HM 1171, Hamilton HM EX, Bermuda
T: +1 (441) 295 2000, F: +1 (441) 295 1242, www.pwc.com/bermuda

CONSOLIDATED BALANCE SHEET

As at 31 December (in thousands of Bermuda dollars)

	2011	2010
Assets		
Cash and demand deposits with banks	413,213	300,865
Cash equivalents	1,566,245	2,128,834
Total cash and cash equivalents	1,979,458	2,429,699
Short-term investments	34,814	26,392
Debt and equity securities		
Trading	62,591	18,088
Available for sale	1,962,346	2,611,056
Held to maturity	64,789	-
Total investments in debt and equity securities	2,089,726	2,629,144
Loans, net of allowance for credit losses	4,247,260	4,043,360
Premises, equipment and computer software	276,114	261,955
Accrued interest	25,259	17,691
Goodwill	15,937	16,017
Intangible assets	33,247	38,946
Investments in affiliates	32,582	33,534
Receivable from investments sold	-	50,817
Other real estate owned	27,354	-
Other assets	62,358	75,505
Total assets	8,824,109	9,623,060
Liabilities		
Deposits		
Non-interest bearing	961,002	977,417
Interest bearing		
Customers	6,439,076	7,170,963
Banks	125,362	79,679
Total deposits	7,525,440	8,228,059
Employee future benefits	104,913	85,209
Accrued interest	8,905	9,647
Preference Share dividends payable	715	715
Payable for investments purchased	-	112,663
Other liabilities	86,656	94,680
Total other liabilities	201,189	302,914
Subordinated capital	267,755	282,799
Total liabilities	7,994,384	8,813,772
Shareholders' equity		
Common Share capital (BMD 0.01 par; authorised Shares 26,000,000,000 (2010: BMD 0.01 par; authorised Shares 26,000,000,000) issued and outstanding: 549,468,349 (2010: 549,143,448)	5,494	5,491
Preference Share capital (USD 0.01 par; USD 1,000 liquidation preference) issued and outstanding: 200,000 (2010: 200,000)	2	2
Contingent Value Convertible Preference Share capital (USD 0.01 par) issued and outstanding: 7,464,186 (2010: 7,789,087)	75	78
Additional paid-in capital	1,377,556	1,376,037
Accumulated deficit	(490,377)	(509,579)
Less: Treasury Common Shares: 2,163,958 Shares (2010: 2,401,593 Shares)	(21,723)	(24,127)
Accumulated other comprehensive loss	(41,302)	(38,614)
Total Shareholders' equity	829,725	809,288
Total liabilities and Shareholders' equity	8,824,109	9,623,060

The accompanying notes are an integral part of these Consolidated Financial Statements.

Robert A. Mulderig
Chairman of the Board

Robert Steinhoff
Vice Chairman

Bradford B. Kopp

Bradford Kopp
President & Chief Executive Officer

CONSOLIDATED STATEMENTS OF OPERATIONS

For the year ended 31 December (in thousands of Bermuda dollars, except per Share data)

	2011	2010
Non-interest income		
Asset management	22,942	24,544
Banking	33,302	33,941
Foreign exchange revenue	31,519	32,479
Trust	29,995	30,534
Custody and other administration services	11,780	13,574
Other non-interest income	5,708	8,348
Total non-interest income	135,246	143,420
Interest income		
Loans	202,473	198,008
Investments	45,640	28,330
Deposits with banks	10,846	11,047
Total interest income	258,959	237,385
Interest expense		
Deposits	34,736	45,988
Subordinated capital	10,486	12,455
Securities sold under repurchase agreement	2	-
Total interest expense	45,224	58,443
Net interest income before provision for credit losses	213,735	178,942
Provision for credit losses	(14,326)	(41,970)
Net interest income after provision for credit losses	199,409	136,972
Net realised / unrealised (losses) gains on trading investments	(919)	971
Net realised gains (losses) on available for sale investments	2,059	(107,047)
Other-than-temporary impairment losses on available for sale investments	-	(60,522)
Realised loss on disposal of subsidiaries	-	(7,430)
Net other gains (losses)	3,135	(6,489)
Total net revenue	338,930	99,875
Non-interest expense		
Salaries and other employee benefits	150,752	159,082
Technology and communications	55,037	54,037
Property	29,316	27,469
Professional and outside services	18,762	13,811
Non-income taxes	14,500	15,405
Amortisation of intangible assets	5,799	5,711
Marketing	5,257	5,002
Other expenses	19,068	28,948
Total non-interest expense	298,491	309,465
Net income (loss) before income taxes	40,439	(209,590)
Income tax benefit	33	1,975
Net income (loss)	40,472	(207,615)
Cash dividends declared on Contingent Value Convertible Preference Shares	(3,270)	-
Cash dividends declared on Preference Shares	(16,000)	(16,000)
Preference Shares guarantee fee	(2,000)	(2,000)
Net income (loss) attributable to Common Shareholders	19,202	(225,615)
Income (loss) per Common Share		
Basic	0.03	(0.47)
Diluted	0.03	(0.47)

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)

For the year ended 31 December (in thousands of Bermuda dollars)

	2011	2010
Common Share capital issued and outstanding		
Balance at beginning of year (2011: 549,143,448 Shares; 2010: 99,060,111 Shares)	**5,491**	99,060
Issuance (2011: nil Shares; 2010: 147,703,758 Shares)	-	144,836
Reduction in par value of Shares	-	(241,429)
Repurchased (2011: nil Shares; 2010: 107,571,361 Shares)	-	(1,076)
Rights conversion (2011: nil Shares; 2010: 99,173,842 Shares)	-	992
Conversion of Mandatorily and Contingent Convertible Preference Shares (2011: nil Shares; 2010: 310,302,028 Shares)	-	3,103
Conversion of Contingent Value Convertible Preference Shares (2011: 324,901 Shares; 2010: 475,070 Shares)	3	5
Balance at end of year (2011: 549,468,349 Shares; 2010: 549,143,448 Shares)	**5,494**	5,491
Preference Shares		
Balance at beginning of year (2011: 200,000 Shares; 2010: 200,000 Shares)	**2**	2
Issuance (2011: nil Shares; 2010: nil Shares)	-	-
Balance at end of year (2011: 200,000 Shares; 2010: 200,000 Shares)	**2**	2
Mandatorily Convertible Preference Shares		
Balance at beginning of year (2011: nil Shares; 2010: nil Shares)	-	-
Issuance (2011: nil Shares; 2010: 281,770 Shares)	-	3
Conversion to Common Shares (2011: nil Shares; 2010: 281,770 Shares)	-	(3)
Balance at end of year (2011: nil Shares; 2010: nil Shares)	-	-
Contingent Convertible Preference Shares		
Balance at beginning of year (2011: nil Shares; 2010: nil Shares)	-	-
Issuance (2011: nil Shares; 2010: 93,230 Shares)	-	1
Conversion to Common Shares (2011: nil Shares; 2010: 93,230 Shares)	-	(1)
Balance at end of year (2011: nil Shares; 2010: nil Shares)	-	-
Contingent Value Convertible Preference Shares		
Balance at beginning of year (2011: 7,789,087 Shares; 2010: nil Shares)	**78**	-
Rights conversion (2011: nil Shares; 2010: 8,264,157 Shares)	-	83
Conversion to Common Shares (2011: 324,901 Shares; 2010: 475,070 Shares)	(3)	(5)
Balance at end of year (2011: 7,464,186 Shares; 2010: 7,789,087 Shares)	**75**	78
Additional paid-in capital		
Balance at beginning of year	**1,376,037**	764,206
Stock option plan expense	3,567	4,019
Reduction of additional paid-in capital on transfer and sale of Treasury Shares	(2,048)	(6,939)
Issuance of Common Shares	-	30,192
Issuance of Mandatorily Convertible Preference Shares	-	281,767
Issuance of Contingent Convertible Preference Shares	-	93,229
Reduction of par value of Common Shares	-	241,429
Conversion of Mandatorily and Contingent Convertible Preference Shares	-	(3,103)
Cost of capital raise and rights offering	-	(28,763)
Balance at end of year	**1,377,556**	1,376,037
Accumulated deficit		
Balance at beginning of year	**(509,579)**	(283,964)
Net income (loss) for year	40,472	(207,615)
Cash dividends declared on Contingent Value Convertible Preference Shares	(3,270)	-
Cash dividends declared on Preference Shares	(16,000)	(16,000)
Preference Shares guarantee fee	(2,000)	(2,000)
Balance at end of year	**(490,377)**	(509,579)

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS) *(Continued)*

For the year ended 31 December (in thousands of Bermuda dollars)

	2011	2010
Treasury Common Shares		
Balance at beginning of year (2011: 2,401,593 Shares; 2010: 3,426,106 Shares)	**(24,127)**	(34,660)
Share-based compensation	**356**	3,593
Net purchases, sales and transfers of Treasury Shares	**2,048**	6,940
Balance at end of year (2011: 2,163,958 Shares; 2010: 2,401,593 Shares)	**(21,723)**	(24,127)
Accumulated other comprehensive loss		
Balance at beginning of year	**(38,614)**	(189,184)
Net change in unrealised gains (losses) on translation of net investment in foreign operations	**823**	(4,494)
Net change in unrealised gains on available for sale investments	**19,845**	38,809
Net change in unrealised non-credit losses on held to maturity investments	**-**	58,557
Net change in employee future benefits liability	**(23,356)**	57,698
Balance at end of year	**(41,302)**	(38,614)
Total Shareholders' equity	**829,725**	809,288
Comprehensive income (loss)		
Net income (loss)	**40,472**	(207,615)
Other comprehensive (loss) income	**(2,688)**	150,570
Total comprehensive income (loss)	**37,784**	(57,045)
Components of accumulated other comprehensive loss		
Cumulative unrealised losses on translation of investment in foreign operations	**(11,321)**	(12,144)
Cumulative unrealised gains (losses) on available for sale investments	**1,663**	(18,182)
Cumulative change in employee future benefits liability	**(31,644)**	(8,288)
Balance at end of year	**(41,302)**	(38,614)

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the year ended 31 December (in thousands of Bermuda dollars)

	2011	2010
Cash flows from operating activities		
Net income (loss)	40,472	(207,615)
Adjustments to reconcile net income (loss) to operating cash flows:		
Depreciation and amortisation	39,084	25,216
Write down of computer software in development	-	3,831
Decrease in carrying value of investments in affiliates	952	1,959
Share-based payments	3,923	7,612
Loss on sale of premises and equipment	-	63
Net (gain) loss on sale of affiliate / subsidiaries	(3,178)	7,430
Net gain on repayment of sub-debt	(1,125)	-
Net realised (gains) losses of available for sale securities	(2,059)	107,047
Other-than-temporary impairments on available for sale investments	-	60,522
Provision for credit losses	14,326	41,970
Changes in operating assets and liabilities:		
Increase in accrued interest receivable	(7,769)	(1,520)
Decrease in other assets	12,918	23,259
Decrease in accrued interest payable	(731)	(2,707)
Decrease in other liabilities	(8,716)	(2,441)
	88,097	64,626
Net change in trading investments	(44,422)	2,371
Cash provided by operating activities	43,675	66,997
Cash flows from investing activities		
Net (increase) decrease in short-term investments	(8,668)	20,802
Net proceeds on sale of affiliate	3,178	-
Additions to premises, equipment and computer software	(33,476)	(39,611)
Net (increase) decrease in loans	(255,145)	104,878
Held to maturity investments: proceeds from maturities	-	20,584
Held to maturity investments: purchases	(64,789)	-
Available for sale investments: proceeds from sale and maturities	2,383,659	2,181,165
Available for sale investments: purchases	(1,788,827)	(2,085,825)
Cash and demand deposits held by subsidiaries at time of sale	-	(4,657)
Cash provided by investing activities	235,932	197,336
Cash flows from financing activities		
Net decrease in demand and term deposit liabilities	(701,240)	(380,828)
Repayment of subordinated capital	(13,875)	-
Issuance of Common Share capital	-	295,000
Issuance of Preference Share capital	-	385,001
Cost of issuing Share capital and rights	-	(28,763)
Common Shares repurchased	-	(130,000)
Cash dividends paid on Contingent Value Convertible Preference Shares	(3,270)	-
Cash dividends paid on Preference Shares	(16,000)	(16,622)
Preference Shares guarantee fee paid	(2,000)	(2,000)
Cash (used in) provided by financing activities	(736,385)	121,788
Net effect of exchange rates on cash and cash equivalents	6,537	(21,597)
Net (decrease) increase in cash and cash equivalents	(450,241)	364,524
Cash and cash equivalents at beginning of year	2,429,699	2,065,175
Cash and cash equivalents at end of year	1,979,458	2,429,699
Supplemental disclosure of cash flow information		
Cash interest paid	47,268	58,770
Cash income tax paid	871	468
Non-cash item		
Transfer to Other Real Estate Owned and other repossessed assets	27,354	-

The accompanying notes are an integral part of these Consolidated Financial Statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Bermuda dollars)

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 license 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 and a provider of specialised wealth management services. Services offered include retail, private & corporate banking, treasury, custody, asset management and personal & institutional trust services. The Bank provides such services from seven jurisdictions: Bermuda, Barbados, Cayman, Guernsey, Switzerland, The Bahamas and the United Kingdom. The Bank holds all applicable licenses 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 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 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:

- i. Allowance for credit losses
- ii. Fair value of financial instruments
- iii. Impairment of long-lived assets
- iv. Impairment of goodwill
- v. Employee future benefits
- vi. Share-based payments
- vii. Concentrations of credit risk & customers
- viii. Commitments and contingencies

b. Basis of Consolidation

The Consolidated Financial Statements include the accounts of the Company and its majority-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 consolidates VIEs where it is considered to be the primary beneficiary. 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. 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 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 Statement of Operations.

The assets and liabilities of foreign currency-based subsidiaries are translated at the rate of exchange prevailing on the Balance Sheet date, whilst 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 income (loss) ("AOCI"). Gains and losses on foreign currency-based subsidiaries are recorded in the Consolidated Statement of Operations only when realised.

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 Sheet because the Bank is not the beneficiary of these assets.

e. Investments

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

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 Sheet with unrealised gains and losses reported as a net increase or decrease to accumulated other comprehensive income (loss). Debt and equity securities classified as trading investments are carried at fair value in the Consolidated Balance Sheet, with unrealised gains and losses included in the Consolidated Statement of Operations as net realised / unrealised gains (losses) on trading investments.

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 Sheet. Unrecognised gains and losses on HTM securities are disclosed in the notes to the 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 Statement 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 Statement 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 a closed ended fund and private equity companies for which the Bank does not have sufficient rights or ownership interests to follow the equity method of accounting. With respect to the closed ended fund, the Bank uses the net assets value as a practical expedient for fair value. 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.

Investments in affiliates includes 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

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 qualitative determination. 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 and for AFS investments, the decrease in fair value relating to factors other than credit losses are recognised in Other Comprehensive Income (Loss) ("OCI"). In determining whether credit losses exist, Management considers 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. 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 valuation process. The valuation process 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.

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.

Losses projected for the underlying collateral ("pool losses") are compared against the level of credit enhancement in the securitisation structure to determine whether these features are sufficient to absorb the pool losses, or whether a credit loss on the debt security exists. As at 31 December 2011, Management's cash flow forecasts for its Pass-through note investment ("PTN") was created in conjunction with a specialist in analytical cash flow modelling. Management also performs other analyses to support its cash flow projections to assess the reasonability. 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.

Management's 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 valuations change, the Bank may experience additional OTTI or realised losses or gains, and the period-to-period changes in value could vary significantly.

f. Loans

Loans are reported as the principal amount outstanding, net of allowance for credit losses, unearned income 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.

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 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 immediately 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 restored to accrual status only when interest and principal payments are brought current and future payments are reasonably assured.

Loans Modified in a Troubled Debt Restructuring
A modification of a loan constitutes a TDR when a borrower is experiencing financial difficulty and the modification constitutes a concession. If a restructuring is considered a TDR, the Bank is required to make certain disclosures in the notes of the 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.

Loans modified in a TDR are typically already on non-accrual status and partial charge-offs have, in some cases, already been taken against the outstanding loan balance.

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.

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 30 days or more 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 written off and reported as charge-offs.

g. 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 Allowance
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, internal risk ratings, and 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 installment, 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.

h. Cash and Cash Equivalents
Cash and cash equivalents 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. See Note 3.

i. Business Combinations, Goodwill and Intangible Assets
All business combinations are accounted for using the purchase method. Identifiable intangible assets (mostly customer relationships) are recognised separately from goodwill and are initially valued using discounted cash flow calculations and other recognised valuation techniques. Goodwill represents the excess of the price paid for the acquisition of a business over the fair value of the net assets acquired.

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.

j. Premises, Equipment and Computer Software

Land, 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 3 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 5 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.

k. Other Real Estate Owned ("OREO")

OREO comprise 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 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. Subsequent decreases in the property's fair value and operating expenses of the property are recognised through charges to non-interest expense.

l. Derivatives

All derivatives are recognised on the Consolidated Balance Sheet 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); or an instrument that is held for trading or non-hedging purposes (a trading or non-hedging 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. When the hedge is highly effective, 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 income, until earnings are affected by the variability of cash flows of the hedged transaction. Any hedge ineffectiveness is recorded in current year 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 other comprehensive income, depending on whether the hedging relationship satisfies the criteria for a fair value or cash flow hedge when the hedge is highly effective. 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 account within other comprehensive income. Changes in the fair value of derivative trading and non-hedging 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 objective and strategy 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 Sheet 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. When it is determined that a derivative has ceased to be highly effective as a hedge, the Bank discontinues hedge accounting prospectively.

For those hedge relationships that are terminated, hedge designations that are removed, or forecasted transactions that are no longer expected to occur, 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 account. For fair value hedges, any changes to the hedged item remain as part of the basis of the asset or liability and are ultimately reflected as an element of the yield. For cash flow hedges, any changes in fair value of the end-user derivative remain in other comprehensive income and are included in retained earnings of future periods when earnings are also affected by the variability of the hedged cash flows. If the forecasted transaction is no longer likely to occur, any changes in fair value of the end-user derivatives are recognised in net income.

m. Employee Future Benefits

The Bank maintains trusteed 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 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 (liability) recognised for accounting purposes is reported in other assets and employee future benefits, respectively. The actuarial gains and losses, transition obligation and past service costs of the defined pension plans and post-retirement medical benefits plan are recognised in OCI net of tax and amortised to net income over the average service period.

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.

n. 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 Statement 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 Statement 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).

o. Revenue Recognition

Trust and investment 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 fee.

Banking services fees primarily include fees for certain loan origination, letters of credit, other financial guarantees, compensating balances and other financial services-related products. Certain loan origination fees are primarily overdraft and other revolving lines of credit fees. These fees are recognised as revenue over the period of the underlying facilities. Letters of credit fees are recognised as revenue over the period in which the related service is provided. All other fees are recognised as revenue in the period in which the service is provided.

Loan interest income includes the amortisation of non-refundable loan origination and commitment fees. These fees are deferred (except for certain retrospectively determined fees meeting specified criteria) and recognised as an adjustment of yield over the life of the related loan. These loan origination and commitment fees are offset by their related direct cost 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 Statement 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.

p. 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 available for sale, and derivative assets and liabilities are recognised in the Consolidated Balance Sheet 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 price 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 and cash equivalents
The carrying amount of cash and demand deposits with banks, being short term in nature, is deemed to equate to the fair value.

Cash equivalents include unrestricted term deposits, certificates of deposit 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 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.

Investments and employee future benefits plans' assets
The fair values of investments and pension plan assets are determined based on observable quoted prices for identical assets or liabilities in active markets when available. If unavailable, observable inputs from similar items in active markets or identical/similar items with inactive markets are used. In the absence of observable quoted prices, unobservable inputs are used.

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.

Other real estate owned ("OREO")
OREO assets are carried at the lower of cost or fair value less estimated costs to sell. Fair value is based on third-party appraisals adjusted to reflect Management's judgment as to the realisable value of the properties. 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.

Subordinated capital
The fair value of the subordinated capital has been estimated by discounting the contractual cash flows, using current market interest rates.

Derivatives
Fair value of exchange-traded derivatives is based on quoted market prices. Over-the-counter (OTC) derivative contracts may include forward, swap and option contracts relating to interest rates or foreign currencies. Depending on the product and the terms of the transaction, the fair value of the OTC derivative products are modelled taking into account the counterparties' creditworthiness and using a series of techniques. Many pricing models do not entail material subjectivity because the methodologies employed do not necessitate significant judgements and the pricing inputs are observed from actively quoted markets, as is the case for interest rate swap and option contracts.

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

q. 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.
- Documentary and commercial letters of credit, primarily related 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 13) 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.

r. Income Taxes

The Bank uses the asset and liability method whereby income taxes reflect the expected future tax consequences of temporary differences between the 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. Income taxes on the Consolidated Statement of Operations include the current and deferred portions of the income taxes. Income taxes applicable to items charged or credited directly to Shareholders' equity are included in such items.

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.

The Bank initially recognises the financial statement effects of a tax position when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. The Bank recognises interest accrued and penalties related to unrecognised tax benefits in operating expenses.

s. Consolidated Statement of Cash Flows

For the purposes of the Consolidated Statement of Cash Flows, cash and cash equivalents 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.

t. 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.

u. 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 costs of sale.

v. Charitable Trust

In July 2000, the Bank established a charitable trust with the irrevocable purpose to make charitable donations to persons ordinarily resident in Bermuda (the "Charitable Trust"). As a not-for-profit organisation, the Charitable Trust is not consolidated in the Bank's financial statements. As the Charitable Trust's trustees are representatives of the Bank, the Bank's endowment donations to the Charitable Trust are recognised at their recoverable amount in Other assets in the Consolidated Balance Sheet until dispersed by the Charitable Trust, at which time donations are recognised in Other expenses in the Consolidated Statement of Operations.

w. New Accounting Pronouncements

The following accounting developments were issued during the year ending 31 December 2011:

Financing receivables and the allowance for credit losses disclosures

In July 2010, the Financial Accounting Standards Board ("FASB") issued an accounting standards update about additional "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses". The new disclosure guidance significantly expanded the existing requirements and were effective for the Bank on 1 January 2011. The prior-period figures for loan disclosures have been reclassified to conform to the current enhanced note disclosures required by the Standard. The Standard did not affect the Bank's consolidated financial condition or results of operations.

Troubled debt restructurings

During March 2011, the FASB issued an accounting standards update, "A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring" to assist creditors in determining whether a loan modification is a TDR. The new guidance was effective for public companies in interim and annual periods beginning on or after 15 June 2011 and must be applied retrospectively to restructurings occurring on or after the beginning of the year. The Bank applied the provisions of this update retrospectively to all modifications and restructurings occurring on or after 1 January 2011. As a result of the retrospective application, the Bank classified $33.6 million loan modifications as TDRs that, in previous periods, had not been classified as TDRs. These newly identified TDRs did not have a significant impact on the specific allowance or provision expense. At 31 December 2011, these amounts included $20.9 million of performing loans that were not previously considered to be impaired loans.

Fair value measurements

In May 2011, the FASB issued accounting standard update, "Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure requirements in US GAAP and IFRS". The amendments clarify the application of the highest and best use and valuation premise concepts, preclude the application of blockage factors in the valuation of all financial instruments and include criteria for applying the fair value measurement principles to portfolios of financial instruments. The amendments additionally prescribe enhanced financial statement disclosures for Level 3 fair value measurements. The new amendments will be effective for first interim or annual period beginning on or after 15 December 2011. The new guidance will require prospective application. The impact of this additional accounting guidance is expected to be primarily on disclosures.

Repurchase agreements

During May 2011, the FASB issued an accounting standard update, "Reconsideration of Effective Control for Repurchase Agreements". The amendments in this update remove from the assessment of effective control the criterion relating to the transferor's ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. The amendments in this update also eliminate the requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets.

The guidance in this update is effective for the first interim or annual period beginning on or after 15 December 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted.

Other comprehensive income

In June 2011, the FASB issued an accounting standards update, "Presentation of Comprehensive Income", which eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. The amendments are effective for fiscal years, and interim periods within those years, beginning after 15 December 2011 and should be applied retrospectively. Early adoption is permitted but the Bank elected not to early adopt. These amendments do not require any transition disclosures. The impact of these amendments is primarily on disclosures on the face of the Consolidated Statement of Operations.

Goodwill impairment test

During September 2011, the FASB issued an accounting standards update, "Testing Goodwill for Impairment (the revised standard)" that permits an entity to make a qualitative assessment of whether it is more likely than not that a reporting unit's fair value is less than its carrying amount before applying the two-step goodwill impairment test. The update is effective for annual and interim goodwill impairment tests performed in fiscal years beginning after 15 December 2011. Early adoption is permitted. The Bank is assessing the impact of these amendments.

NOTE 3: CHANGE IN ACCOUNTING POLICY

Effective 1 January 2011, the Bank changed its accounting policy with respect to cash and cash equivalents for the purposes of the Consolidated Statement of Cash Flows. The Bank defines cash and cash equivalents to 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, treasury bills and securities purchased under agreements to resell. Previously cash and demand deposits with banks only included cash and demand deposits, vault cash and cash in transit for the purposes of the Consolidated Statement of Cash Flows. The Bank believes the new policy is preferable as it more closely reflects the manner in which the Bank manages its liquid assets.

The impact of this voluntary change in accounting policy on the Consolidated Financial Statements since the Bank's adoption of the change in accounting policy is shown in the table below:

	As reported 2010	Adjustments 2010	Restated 2010
Consolidated Balance Sheet			
Cash and demand deposits with banks	325,367	(24,502)	300,865
Cash equivalents			
Term deposits with banks	1,950,179	(1,890)	1,948,289
Certificates of deposit and treasury bills	-	180,545	180,545
Total cash equivalents	1,950,179	178,655	2,128,834
Total cash and cash equivalents	2,275,546	154,153	2,429,699
Short-term investments	-	26,392	26,392
Debt and equity securities			
Trading	18,088	-	18,088
Available for sale	2,791,601	(180,545)	2,611,056
Total investments in debt and equity securities	2,809,689	(180,545)	2,629,144

	As reported 2010	Adjustments 2010	Restated 2010
Extract of Consolidated Cash Flow Statement			
Cash flows from investing activities			
Net increase in term deposits with banks	(536,208)	536,208	-
Net decrease in short-term investments	-	20,802	20,802
Available for sale securities: proceeds from sale and maturities	6,264,970	(4,083,805)	2,181,165
Available for sale securities: purchases	(6,224,605)	4,138,780	(2,085,825)
Net effect of exchange rates on cash and cash equivalents	(14)	(21,583)	(21,597)
Net (decrease) increase in cash and cash equivalents	**(225,882)**	**590,406**	**364,524**
Cash and cash equivalents at beginning of year	**551,249**	**1,513,926**	**2,065,175**
Cash and cash equivalents at end of year	**325,367**	**2,104,332**	**2,429,699**

NOTE 4: CASH AND CASH EQUIVALENTS

	2011			2010		
	Bermuda	Non-Bermuda	Total	Bermuda	Non-Bermuda	Total
Unrestricted						
Non-interest earning						
Cash and demand deposits	176,091	30,847	206,938	118,155	42,895	161,050
Interest earning						
Demand deposits	49	206,226	206,275	44	139,771	139,815
Cash equivalents	489,391	1,076,854	1,566,245	602,135	1,526,699	2,128,834
Sub-total - Interest earning	489,440	1,283,080	1,772,520	602,179	1,666,470	2,268,649
Total cash and cash equivalents	665,531	1,313,927	1,979,458	720,334	1,709,365	2,429,699

NOTE 5: SHORT-TERM INVESTMENTS

	2011			2010		
	Bermuda	Non-Bermuda	Total	Bermuda	Non-Bermuda	Total
Unrestricted						
Interest earning						
Term deposits maturing between three to six months	-	4,630	4,630	-	392	392
Term deposits maturing between six to twelve months	-	2,900	2,900	-	1,215	1,215
Total unrestricted short-term investments	-	7,530	7,530	-	1,607	1,607
Affected by drawing restrictions related to minimum reserve and derivative margin requirements						
Non-interest earning						
Demand deposits	-	12,394	12,394	-	6,156	6,156
Interest earning						
Demand deposits	12,641	2,249	14,890	18,157	472	18,629
Total restricted short-term investments	12,641	14,643	27,284	18,157	6,628	24,785
Total short-term investments	12,641	22,173	34,814	18,157	8,235	26,392

NOTE 6: INVESTMENTS

Amortised cost, carrying amounts and estimated fair value

The amortised cost, carrying amounts and fair values are as follows:

	2011				2010			
	Amortised cost	Gross unrealised gains	Gross unrealised losses	Carrying amount / Fair value	Amortised cost	Gross unrealised gains	Gross unrealised losses	Carrying amount / Fair value
Trading								
Debt securities issued by non-US governments	5,788	419	(236)	5,971	6,553	150	(192)	6,511
Mutual funds (1)	56,964	224	(568)	56,620	11,981	273	(677)	11,577
Total trading	62,752	643	(804)	62,591	18,534	423	(869)	18,088
Available for sale								
Certificates of deposit	354,847	2,411	(765)	356,493	854,273	4,885	(12)	859,146
US government and federal agencies	778,387	14,419	(2,002)	790,804	927,598	398	(10,502)	917,494
Debt securities issued by non-US governments	111,172	1,966	(106)	113,032	131,028	1,675	(11)	132,692
Corporate debt securities guaranteed by non-US governments	122,987	38	(1,377)	121,648	149,948	76	(304)	149,720
Corporate debt securities	412,285	421	(3,744)	408,962	352,960	14	(5,504)	347,470
Asset-backed securities - Student loans	149,759	-	(5,413)	144,346	152,434	-	(5,623)	146,811
Pass-through note	33,696	-	(6,705)	26,991	62,762	-	(5,116)	57,646
Equity securities	120	-	(50)	70	77	-	-	77
Total available for sale	1,963,253	19,255	(20,162)	1,962,346	2,631,080	7,048	(27,072)	2,611,056

(1) The Bank invested $50 million of seed money in the BNY Mellon Butterfield Income Advantage Fund during September 2011.

2011	Amortised cost	Non-credit impairments recognised in AOCI	Carrying amount	Gross unrecognised gains	Gross unrecognised losses	Fair values
Held to maturity						
US government and federal agencies	64,789	-	64,789	228	(429)	64,588
Total held to maturity	64,789	-	64,789	228	(429)	64,588

There were no held to maturity investments as at 31 December 2010.

Unrealised loss positions

The following tables show the fair value and gross unrealised losses of the Bank's available for sale and held to maturity investments with unrealised losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealised loss position. Debt securities are categorised as being in a continuous loss position for "Less than 12 months" or "12 months or more" based on the point in time that the fair value declined below the cost basis.

2011	Less than 12 months		12 months or more			
	Fair value	Gross unrealised losses	Fair value	Gross unrealised losses	Total fair value	Total gross unrealised losses
Available for sale						
Certificates of deposit	48,623	(765)	-	-	48,623	(765)
US government and federal agencies	144,364	(1,585)	72,600	(417)	216,964	(2,002)
Debt securities issued by non-US governments	9,493	(54)	2,198	(52)	11,691	(106)
Corporate debt securities guaranteed by non-US governments	30,179	(3)	47,267	(1,374)	77,446	(1,377)
Corporate debt securities	217,612	(2,859)	125,101	(885)	342,713	(3,744)
Asset-backed securities - Student loans	-	-	144,346	(5,413)	144,346	(5,413)
Pass-through note	-	-	26,992	(6,705)	26,992	(6,705)
Equity securities	70	(50)	-	-	70	(50)
Total available for sale securities with unrealised losses	450,341	(5,316)	418,504	(14,846)	868,845	(20,162)
Held to maturity						
US government and federal agencies	30,034	(429)	-	-	30,034	(429)
Total held to maturity securities with unrealised losses	30,034	(429)	-	-	30,034	(429)

2010	Less than 12 months		12 months or more			
	Fair value	Gross unrealised losses	Fair value	Gross unrealised losses	Total fair value	Total gross unrealised losses
Available for sale						
Certificates of deposit	128,619	(12)	-	-	128,619	(12)
US government and federal agencies	775,157	(10,459)	23,337	(43)	798,494	(10,502)
Debt securities issued by non-US governments	3,239	(11)	-	-	3,239	(11)
Corporate debt securities guaranteed by non-US governments	108,611	(304)	-	-	108,611	(304)
Corporate debt securities	8,075	(46)	322,995	(5,458)	331,070	(5,504)
Asset-backed securities - Student loans	-	-	146,811	(5,623)	146,811	(5,623)
Pass-through note	33,304	(2,589)	24,342	(2,527)	57,646	(5,116)
Total available for sale securities with unrealised losses	1,057,005	(13,421)	517,485	(13,651)	1,574,490	(27,072)

There were no held to maturity investments as at 31 December 2010.

The following is a description of the Bank's main investments.

Certificates of deposit
As of 31 December 2011, gross unrealised losses on the Bank's holdings of certificates of deposit ("CDs") were $0.8 million, all of which related to CDs that have been in an unrealised loss position for less than 12 months. Management assesses the credit quality of the issuers, which includes assessments of credit ratings (the Bank only purchases CDs that are rated investment grade or above) and credit worthiness of the issuer and concluded that the CDs do not have any credit losses.

US government and federal agencies
As of 31 December 2011, gross unrealised losses on securities related to United States ("US") government and federal agencies were $2.0 million, $0.4 million of which related to investments that were in an unrealised loss position for longer than 12 months. Overall, Management believes that all the securities in this class do not have any credit losses, given the explicit and implicit guarantees provided by the US federal government.

Debt securities issued by non-US governments
As of 31 December 2011, gross unrealised losses on debt securities issued by non-US governments were $0.1 million, $0.05 million of which related to investments that were in an unrealised loss position for greater than 12 months. All securities in this category were issued by governments of the United Kingdom and Caribbean jurisdictions. Management believes that these securities do not have any credit losses, given the explicit guarantees provided by the non-US governments.

Corporate debt securities guaranteed by non-US governments
As of 31 December 2011, gross unrealised losses related to corporate debt securities guaranteed by non-US governments were $1.4 million, all of which related to investments that were in an unrealised loss position for greater than 12 months. All the bank-issued securities acquired are explicitly guaranteed by the following governments: United Kingdom, Australia, Denmark and Germany. One security is jointly and explicitly guaranteed by three European Governments: Belgium, France and Luxembourg. Management believes that these securities do not have any credit losses, given the guarantees provided by the non-US governments.

Corporate debt securities
As of 31 December 2011, gross unrealised losses related to corporate debt securities were $3.7 million, of which $0.9 million related to investments that were in an unrealised loss position for longer than 12 months. Management estimates of cash flows are based on observable market data, issuer-specific information and credit ratings. Management believes these securities do not have any credit losses.

Asset-backed securities - Student loans
As of 31 December 2011, gross unrealised losses on student loan asset-backed securities were $5.4 million, all of which related to securities that have been in an unrealised loss position for longer than 12 months. All of these securities are "AAA" rated and Management believes these securities do not have any credit losses. All student loan asset-backed securities are backed by loans that fall within the US federally guaranteed Federal Family Education Loan Program ("FFELP"). The unrealised losses were due to maturity profiles that were longer than was initially estimated.

Pass-through note ("PTN")
During 2010, the Bank's investment in its remaining structured investment vehicle ("SIV") was legally amended to a pass-through note structure whereby the Bank maintained the identical beneficial interest in the same underlying securities of the SIV.

As of 31 December 2011, the PTN was in an unrealised loss position amounting to $6.7 million (2010: $5.1 million) for a period exceeding 12 months. Unrealised losses have increased since 31 December 2010 as a result of general risk aversion in the market with regards to distressed assets. The net present value of expected cash flows, or the intrinsic value, to be generated from the underlying assets of the PTN, calculated on both a stressed and severely-stressed environment, is in excess of the amortised cost of the PTN and Management believes that these securities do not have any credit losses. Residential housing prices in the United States, a key driver of the underlying intrinsic value, have performed better than assumed in the models supporting the intrinsic value, which confirms that the unrealised loss is primarily attributable to market risk appetite and not to fundamental valuations.

The following table presents securities by remaining term to earlier of expected or contractual maturity:

2011	Remaining term to earlier of expected or contractual maturity						
	Within 3 months	3 to 12 months	1 to 5 years	5 to 10 years	Over 10 years	No specific maturity	Carrying amount
Trading							
Debt securities issued by non-US governments	-	811	2,026	2,106	1,028	-	5,971
Mutual funds	-	-	-	-	-	56,620	56,620
Total trading	-	811	2,026	2,106	1,028	56,620	62,591
Available for sale							
Certificates of deposit	105,318	174,302	76,873	-	-	-	356,493
US government and federal agencies	-	4,740	622,559	149,245	14,258	2	790,804
Debt securities issued by non-US governments	7,749	66,056	17,905	20,349	971	2	113,032
Corporate debt securities guaranteed by non-US governments	-	90,882	30,766	-	-	-	121,648
Corporate debt securities	27,514	106,639	260,755	14,054	-	-	408,962
Asset-backed securities - Student loans	-	-	58,183	74,999	11,164	-	144,346
Pass-through note	-	-	-	26,991	-	-	26,991
Equity securities	-	-	-	-	-	70	70
Total available for sale	140,581	442,619	1,067,041	285,638	26,393	74	1,962,346
Held to maturity							
US government and federal agencies	-	-	-	24,854	39,935	-	64,789
Total held to maturity securities	-	-	-	24,854	39,935	-	64,789
Total investments	140,581	443,430	1,069,067	312,598	67,356	56,694	2,089,726
Total by currency							
Bermuda dollars	-	-	-	-	-	181	181
US dollars	-	186,614	990,571	300,714	65,358	55,226	1,598,483
Other	140,581	256,816	78,496	11,884	1,998	1,287	491,062
Total investments	140,581	443,430	1,069,067	312,598	67,356	56,694	2,089,726

2010	Remaining term to earlier of expected or contractual maturity						
	Within 3 months	3 to 12 months	1 to 5 years	5 to 10 years	Over 10 years	No specific maturity	Carrying amount
Trading							
Debt securities issued by non-US governments	-	728	2,968	533	2,282	-	6,511
Mutual funds	-	-	-	-	-	11,577	11,577
Total trading	-	728	2,968	533	2,282	11,577	18,088
Available for sale							
Certificates of deposit	582,783	198,362	78,001	-	-	-	859,146
US government and federal agencies	660	23,575	803,851	67,803	21,605	-	917,494
Debt securities issued by non-US governments	-	31,770	80,384	18,298	2,240	-	132,692
Corporate debt securities guaranteed by non-US governments	-	-	149,720	-	-	-	149,720
Corporate debt securities	39,365	121,878	185,160	1,067	-	-	347,470
Asset-backed securities - Student loans	-	-	5,872	129,760	11,179	-	146,811
Pass-through note	-	-	57,646	-	-	-	57,646
Equity securities	-	-	-	-	3	74	77
Total available for sale	622,808	375,585	1,360,634	216,928	35,027	74	2,611,056
Total investments	622,808	376,313	1,363,602	217,461	37,309	11,651	2,629,144

2010	Remaining term to earlier of expected or contractual maturity						
	Within 3 months	3 to 12 months	1 to 5 years	5 to 10 years	Over 10 years	No specific maturity	Carrying amount
Total by currency							
Bermuda dollars	-	-	-	-	-	169	169
US dollars	257,887	112,939	1,241,066	209,736	32,786	5,273	1,859,687
Other	364,921	263,374	122,536	7,725	4,523	6,209	769,288
Total investments	622,808	376,313	1,363,602	217,461	37,309	11,651	2,629,144

Gains and losses on investments

The following table presents gains and losses on investments:

Year ended	2011				2010			
	Trading	Available for sale	Held to maturity	Total	Trading	Available for sale	Held to maturity	Total
Gains (losses) other than OTTI recognised in net income	(919)	2,059	-	1,140	971	(107,047)	-	(106,076)
Total impairment applied against carrying amount	-	-	-	-	-	36,844	-	36,844
Less: change in non-credit related impairments recognised in OCI	-	-	-	-	-	(97,366)	-	(97,366)
OTTI impairments recognised in net income	-	-	-	-	-	(60,522)	-	(60,522)
Net gains (losses) recognised in net income	(919)	2,059	-	1,140	971	(167,569)	-	(166,598)
Gross unrealised gains (losses) recorded in OCI	-	21,904	-	21,904	-	(70,203)	-	(70,203)
Realised (gains) losses transferred to net income	-	(2,059)	-	(2,059)	-	167,569	-	167,569
Total net gains recognised in OCI	-	19,845	-	19,845	-	97,366	-	97,366
Non-credit related impairments recognised in OCI	-	-	-	-	-	-	-	-
Effect of transfer of HTM to AFS	-	-	-	-	-	(58,557)	58,557	-
Net change in gains (losses) recognised in AOCI	-	19,845	-	19,845	-	38,809	58,557	97,366

Sale proceeds and realised gains (losses)

During the year ended 31 December 2011, the Bank disposed of:

- Certificates of deposit totalling $580.2 million in sale proceeds, resulting in a gross realised gain of $0.8 million and a gross realised loss of $0.4 million;
- US agency securities totalling $302.8 million in sale proceeds, resulting in a gross realised gain of $1.8 million; and
- Corporate bonds totalling $88.3 million in sale proceeds, resulting in a gross realised loss of $0.2 million.

During the year ended 31 December 2010, the Bank disposed of:

- SIV investments totalling $87.0 million in sale proceeds, resulting in a gross realised gain of $4.7 million; and
- Asset-backed securities totalling $820.1 million in sale proceeds, resulting in a gross realised loss of $113.8 million.

NOTE 7: LOANS

The composition of the loan portfolio by collateral exposure at each of the indicated dates was as follows:

	2011			2010		
		Non-			Non-	
	Bermuda	Bermuda	Total	Bermuda	Bermuda	Total
Commercial loans						
Banks	-	-	-	276	81	357
Government	256,442	4,230	260,672	61,739	4,365	66,104
Commercial and industrial	103,922	186,715	290,637	249,965	191,699	441,664
Commercial overdrafts	64,733	28,209	92,942	35,539	40,491	76,030
Total commercial loans	425,097	219,154	644,251	347,519	236,636	584,155
Less specific allowance for credit losses on commercial loans	(1,222)	(1,655)	(2,877)	(313)	(264)	(577)
Total commercial loans after specific allowance for credit losses	423,875	217,499	641,374	347,206	236,372	583,578
Commercial real estate loans						
Commercial mortgage	502,110	330,286	832,396	567,776	366,366	934,142
Construction	37,178	2,814	39,992	44,093	13,047	57,140
Total commercial real estate loans	539,288	333,100	872,388	611,869	379,413	991,282
Less specific allowance for credit losses on commercial real estate loans	(9,225)	(2,829)	(12,054)	(16,400)	(5,134)	(21,534)
Total commercial real estate loans after specific allowance for credit losses	530,063	330,271	860,334	595,469	374,279	969,748
Consumer loans						
Automobile financing	23,964	5,862	29,826	37,296	6,025	43,321
Credit card	59,469	25,073	84,542	58,582	25,035	83,617
Overdrafts	9,147	5,731	14,878	4,995	5,241	10,236
Other consumer	87,889	144,002	231,891	94,756	139,450	234,206
Total consumer loans	180,469	180,668	361,137	195,629	175,751	371,380
Less specific allowance for credit losses on consumer loans	(160)	(388)	(548)	(118)	(1,411)	(1,529)
Total consumer loans after specific allowance for credit losses	180,309	180,280	360,589	195,511	174,340	369,851
Residential mortgage loans	1,348,606	1,082,308	2,430,914	1,341,461	821,857	2,163,318
Less specific allowance for credit losses on residential mortgage loans	(3,184)	(7,262)	(10,446)	(1,710)	(4,962)	(6,672)
Total residential mortgage loans after specific allowance for credit losses	1,345,422	1,075,046	2,420,468	1,339,751	816,895	2,156,646
Total gross loans	2,493,460	1,815,230	4,308,690	2,496,478	1,613,657	4,110,135
Less specific allowance for credit losses	(13,791)	(12,134)	(25,925)	(18,541)	(11,771)	(30,312)
Less general allowance for credit losses	(23,474)	(12,031)	(35,505)	(26,038)	(10,425)	(36,463)
Net loans	2,456,194	1,791,066	4,247,260	2,451,899	1,591,461	4,043,360

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, credit card, business and government loans are generally repayable over terms not exceeding five years. The effective yield on total loans as at 31 December 2011 is 4.90% (2010: 4.81%).

The table below presents information about the loan delinquencies:

	2011				
	30-59 days	60-89 days	90 days or more	Total delinquent loans	Loans past due 90 days and still accruing interest
Commercial loans					
Commercial and industrial	2,297	210	6,136	8,643	-
Commercial overdrafts	-	26	4,810	4,836	-
Total commercial loans	2,297	236	10,946	13,479	-
Commercial real estate loans					
Commercial mortgage	9,866	1,280	47,032	58,178	8
Construction	16,680	1,629	-	18,309	-
Total commercial real estate loans	26,546	2,909	47,032	76,487	8
Consumer loans					
Automobile financing	611	299	633	1,543	-
Credit card	3,944	1,722	1,272	6,938	1,272
Overdrafts	6	9	76	91	11
Other consumer	2,776	839	3,351	6,966	173
Total consumer loans	7,337	2,869	5,332	15,538	1,456
Residential mortgage loans	68,173	37,238	52,983	158,394	17,589
Total loans	104,353	43,252	116,293	263,898	19,053

	2010				
	30-59 days	60-89 days	90 days or more	Total delinquent loans	Loans past due 90 days and still accruing interest
Commercial loans					
Commercial and industrial	1,219	205	6,639	8,063	-
Commercial overdrafts	-	49	8,660	8,709	5
Total commercial loans	1,219	254	15,299	16,772	5
Commercial real estate loans					
Commercial mortgage	2,971	99	87,908	90,978	-
Construction	-	8,068	-	8,068	-
Total commercial real estate loans	2,971	8,167	87,908	99,046	-
Consumer loans					
Automobile financing	197	322	340	859	-
Credit card	3,720	400	659	4,779	659
Overdrafts	10	-	390	400	8
Other consumer	1,718	1,689	6,762	10,169	104
Total consumer loans	5,645	2,411	8,151	16,207	771
Residential mortgage loans	21,285	10,966	61,098	93,349	29,361
Total loans	31,120	21,798	172,456	225,374	30,137

The table below sets forth information about the Bank's non-accrual loans:

2011

	Current	30-90 days past due	90 days past due	Non-accrual gross recorded investments
Commercial loans				
Commercial and industrial	1,590	45	6,136	7,771
Commercial overdrafts	873	-	4,810	5,683
Total commercial loans	2,463	45	10,946	13,454
Commercial real estate loans	8,148	-	47,024	55,172
Consumer loans				
Automobile financing	89	261	633	983
Overdrafts	-	-	65	65
Other consumer	46	144	3,178	3,368
Total consumer loans	135	405	3,876	4,416
Residential mortgage loans	3,149	10,907	35,394	49,450
Total loans	13,895	11,357	97,240	122,492

2010

	Current	30-90 days past due	90 days past due	Non-accrual gross recorded investments
Commercial loans				
Commercial and industrial	-	-	6,639	6,639
Commercial overdrafts	-	22	8,655	8,677
Total commercial loans	-	22	15,294	15,316
Commercial real estate loans	-	2,151	87,908	90,059
Consumer loans				
Automobile financing	130	519	340	989
Overdrafts	-	-	382	382
Other consumer	164	843	6,658	7,665
Total consumer loans	294	1,362	7,380	9,036
Residential mortgage loans	2,483	10,870	31,737	45,090
Total loans	2,777	14,405	142,319	159,501

The table below presents information about the credit quality of the Bank's loan portfolio:

31 December 2011	**Pass**	**Special mention**	**Substandard**	**Non-accrual**	**Total gross recorded investments**
Commercial loans					
Banks	-	-	-	-	-
Government	260,672	-	-	-	260,672
Commercial and industrial	267,499	10,716	4,651	7,771	290,637
Commercial overdrafts	84,131	3,128	-	5,683	92,942
Total commercial loans	612,302	13,844	4,651	13,454	644,251
Commercial real estate loans					
Commercial mortgage	625,770	109,678	41,766	55,172	832,396
Construction	38,363	1,629	-	-	39,992
Total commercial real estate loans	664,133	111,307	41,776	55,172	872,388
Consumer loans					
Automobile financing	28,843	-	-	983	29,826
Credit card	83,159	-	1,383	-	84,542
Overdrafts	14,741	72	-	65	14,878
Other consumer	219,959	987	7,577	3,368	231,891
Total consumer loans	346,702	1,059	8,960	4,416	361,137
Residential mortgage loans	2,293,083	46,087	42,294	49,450	2,430,914
Total loans	3,916,220	172,297	97,681	122,492	4,308,690

31 December 2010	Pass	Special mention	Substandard	Non-accrual	Total gross recorded investments
Commercial loans					
Banks	357	-	-	-	357
Government	66,104	-	-	-	66,104
Commercial and industrial	421,306	12,929	790	6,639	441,664
Commercial overdrafts	58,704	8,311	338	8,677	76,030
Total commercial loans	546,471	21,240	1,128	15,316	584,155
Commercial real estate loans					
Commercial mortgage	773,351	59,905	10,827	90,059	934,142
Construction	40,549	16,591	-	-	57,140
Total commercial real estate loans	813,900	76,496	10,827	90,059	991,282
Consumer loans					
Automobile financing	42,095	159	78	989	43,321
Credit card	83,079	-	538	-	83,617
Overdrafts	9,286	437	131	382	10,236
Other consumer	215,087	11,375	79	7,665	234,206
Total consumer loans	349,547	11,971	826	9,036	371,380
Residential mortgage loans	2,071,185	38,260	8,783	45,090	2,163,318
Total loans	3,781,103	147,967	21,564	159,501	4,110,135

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

Quality classification definitions

Pass:
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.

Special Mention:
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.

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.

Non-accrual:
Either where 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 loans which are not well secured and in the process of collection.

The table below presents the impairment methodology applied to the Bank's loan portfolio:

	2011		2010	
Total gross loans evaluated for impairment	**Individually evaluated**	**Collectively evaluated**	Individually evaluated	Collectivelly evaluated
Commercial loans	**644,251**	**-**	583,080	-
Commercial real estate loans	**872,388**	**-**	991,849	-
Consumer loans	**4,416**	**356,721**	9,035	362,345
Residential mortgage loans	**56,832**	**2,374,082**	45,598	2,118,228
Total gross loans	**1,577,887**	**2,730,803**	1,629,562	2,480,573

The table below presents the changes in the allowance for credit loan losses:

Loan Allowances	2011					2010
	Commercial loans	**Commercial real estate loans**	**Consumer loans**	**Residential mortgage loans**	**Total**	Total
Allowances at beginning of year	**7,725**	**28,099**	**9,120**	**21,831**	**66,775**	130,317
Provision taken during the year	**2,259**	**1,482**	**3,882**	**6,703**	**14,326**	41,970
Recoveries	**546**	**634**	**2,890**	**13**	**4,083**	2,456
Charge-offs	**(1,360)**	**(12,280)**	**(6,730)**	**(3,412)**	**(23,782)**	(107,935)
Other	**11**	**(10)**	**6**	**21**	**28**	(33)
Allowances at end of year	**9,181**	**17,925**	**9,168**	**25,156**	**61,430**	66,775
Ending balance: individually evaluated for impairment	**2,877**	**12,054**	**548**	**10,446**	**25,925**	30,312
Ending balance: collectively evaluated for impairment	**6,304**	**5,871**	**8,620**	**14,710**	**35,505**	36,463

The table below presents information about the Bank's impaired loans:

2011	Impaired loans with an allowance			Impaired loans without an allowance		
	Gross recorded investments	Specific allowance	Net loans	Gross recorded investments	Specific allowance	Net loans
Commercial loans						
Commercial and industrial	4,007	(2,208)	1,799	6,611	-	6,611
Commercial overdrafts	669	(669)	-	6,056	-	6,056
Total commercial loans	4,676	(2,877)	1,799	12,667	-	12,667
Commercial real estate loans	41,697	(12,054)	29,643	23,178	-	23,178
Consumer loans						
Automobile financing	240	(75)	165	743	-	743
Credit cards	-	-	-	-	-	-
Overdrafts	-	-	-	65	-	65
Other consumer	861	(473)	388	2,507	-	2,507
Total consumer loans	1,101	(548)	553	3,315	-	3,315
Residential mortgage loans	30,206	(10,446)	19,760	26,626	-	26,626
Total impaired loans	77,680	(25,925)	51,755	65,786	-	65,786

2010	Impaired loans with an allowance			Impaired loans without an allowance		
	Gross recorded investments	Specific allowance	Net loans	Gross recorded investments	Specific allowance	Net loans
Commercial loans						
Commercial and industrial	2,730	(520)	2,210	3,909	-	3,909
Commercial overdrafts	57	(57)	-	8,620	-	8,620
Total commercial loans	2,787	(577)	2,210	12,529	-	12,529
Commercial real estate loans	53,849	(21,534)	32,315	36,210	-	36,210
Consumer loans						
Automobile financing	-	-	-	989	-	989
Overdrafts	314	(314)	-	68	-	68
Other consumer	3,807	(1,215)	2,592	3,858	-	3,858
Total consumer loans	4,121	(1,529)	2,592	4,915	-	4,915
Residential mortgage loans	18,372	(6,672)	11,700	26,718	-	26,718
Total impaired loans	79,129	(30,312)	48,817	80,372	-	80,372

2011	Impaired loans	
	Average recorded investment	Interest income recognised
Commercial loans		
Commercial and industrial	9,284	86
Commercial overdrafts	7,314	5
Total commercial loans	16,598	91
Commercial real estate loans	79,801	520
Consumer loans		
Automobile financing	1,167	-
Credit cards	78	-
Overdrafts	95	-
Other consumer	4,273	-
Total consumer loans	5,613	-
Residential mortgage loans	36,359	273
Total impaired loans	138,371	884

During the year ended 31 December 2011, the amount of gross interest income that would have been recorded had impaired loans been current was $6.9 million (2010: $10.8 million).

The table below presents information about the Bank's loans modified in a troubled debt restructuring as of 31 December 2011:

2011	Number of contracts	Recorded investment	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment	Effect of modification on recorded investment: Changes in the timing of principal or interest payments	Effect of modification on recorded investment: Interest capitalisation
Commercial loans						
Commercial and industrial	4	2,847	2,777	2,777	-	-
Commercial overdrafts	1	1,042	1,142	1,142	-	-
Total commercial loans	5	3,889	3,919	3,919	-	-
Commercial real estate loans	5	22,279	23,121	23,183	-	61
Residential mortgage loans	11	7,382	7,146	7,336	9	180
Total loans	21	33,550 (1)	34,186	34,438	9	241

(1) The amount comprised $12.6 million of non-accrual loans and $20.9 million of loans on accrual status.

The table below presents information about the Bank's loans modified in a troubled debt restructuring from 1 January 2011 to 31 December 2011 that subsequently became 90 days or more past due following a modification:

	Number of contracts	Recorded investment
Commercial real estate loans	1	1,519

NOTE 8: 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 primarily evaluated by industry and also by geographic region. In the consumer portfolio, concentrations are primarily evaluated by products. Credit exposures include loans, guarantees and acceptances, letters of credit and commitments for undrawn lines of credit. Unconditionally cancellable credit cards, overdrafts and 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 as disclosed in Note 13: Commitments and Credit Related Arrangements.

	2011			2010		
	On-Balance Sheet	Off-Balance Sheet	Total credit exposure	On-Balance Sheet	Off-Balance Sheet	Total credit exposure
Banks and financial services	331,726	496,753	828,479	355,215	423,295	778,510
Commercial and merchandising	278,614	137,023	415,637	439,429	250,927	690,356
Governments	258,479	-	258,479	68,250	-	68,250
Individuals	2,301,823	100,500	2,402,323	2,218,136	59,979	2,278,115
Primary industry and manufacturing	226,030	2,692	228,722	70,212	42,376	112,588
Real estate	779,450	94,029	873,479	789,155	25,960	815,115
Hospitality industry	97,340	-	97,340	128,724	2,804	131,528
Transport and communication	9,303	-	9,303	10,702	200	10,902
Sub-total	4,282,765	830,997	5,113,762	4,079,823	805,541	4,885,364
General allowance	(35,505)	-	(35,505)	(36,463)	-	(36,463)
Total	4,247,260	830,997	5,078,257	4,043,360	805,541	4,848,901

The following table summarises the credit exposure of the Bank by region:

	2011			2010		
	On-Balance Sheet	Off-Balance Sheet	Total credit exposure	On-Balance Sheet	Off-Balance Sheet	Total credit exposure
Bermuda	2,479,669	406,094	2,885,763	2,477,937	441,485	2,919,422
Barbados	181,325	8,563	189,888	188,938	8,127	197,065
Cayman	728,572	177,846	906,418	595,425	227,023	822,448
Guernsey	454,039	149,387	603,426	332,827	106,556	439,383
The Bahamas	4,742	90	4,832	69,321	1,734	71,055
United Kingdom	434,418	89,017	523,435	415,375	20,616	435,991
Sub-total	4,282,765	830,997	5,113,762	4,079,823	805,541	4,885,364
General allowance	(35,505)	-	(35,505)	(36,463)	-	(36,463)
Total	4,247,260	830,997	5,078,257	4,043,360	805,541	4,848,901

NOTE 9: PREMISES, EQUIPMENT AND COMPUTER SOFTWARE

The following table summarises land, buildings, equipment and computer software:

	2011			2010		
	Cost	Accumulated depreciation	Net carrying amount	Cost	Accumulated depreciation	Net carrying amount
Land	13,371	-	13,371	13,371	-	13,371
Buildings	184,943	(53,306)	131,637	185,335	(46,524)	138,811
Equipment	56,585	(44,545)	12,040	55,383	(41,588)	13,795
Computer software in use	168,738	(52,525)	116,213	60,202	(43,796)	16,406
Computer software in development	2,853	-	2,853	79,572	-	79,572
Total	426,490	(150,376)	276,114	393,863	(131,908)	261,955

	2011	2010
Depreciation		
Buildings (included in property expense)	6,819	5,257
Equipment (included in property expense)	2,876	3,207
Computer hardware and software (included in technology & communications expense)	9,559	8,070
Total depreciation charged to non-interest expense	19,254	16,534
Impairment		
Write off of computer software in development (included in net other losses)	-	3,831

NOTE 10: GOODWILL AND OTHER INTANGIBLE ASSETS

The following table presents goodwill and other intangible assets by business segment:

Goodwill

Business segment	Guernsey	United Kingdom	Total
Balance as at 31 December 2009	6,917	9,795	16,712
Foreign exchange translation adjustment	(245)	(450)	(695)
Balance as at 31 December 2010	6,672	9,345	16,017
Foreign exchange translation adjustment	(38)	(42)	(80)
Balance as at 31 December 2011	6,634	9,303	15,937

Customer relationship intangible assets	2011				2010			
	Cost	Accumulated impairment	Accumulated amortisation	Net carrying amount	Cost	Accumulated impairment	Accumulated amortisation	Net carrying amount
Bermuda - Wealth Management	8,342	-	(4,034)	4,308	8,342	-	(3,479)	4,863
Barbados	6,681	-	(3,597)	3,084	6,681	-	(3,152)	3,529
Cayman	1,211	(180)	(593)	438	1,211	-	(511)	700
Guernsey	41,010	-	(27,542)	13,468	41,242	-	(24,924)	16,318
The Bahamas	5,234	-	(2,867)	2,367	5,204	-	(2,517)	2,687
United Kingdom	19,036	-	(9,454)	9,582	19,153	-	(8,304)	10,849
Total	81,514	(180)	(48,087)	33,247	81,833	-	(42,887)	38,946

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. The 31 December 2011 fair value of customer relationship intangible assets is based on the present value of net cash flows expected to be derived solely from the recurring customer base existing as at 31 December 2011. The discount rate used for testing is the discount rate implied in the initial purchase price acquisition.

During 2011 and 2010, the Bank did not acquire new customer relationship intangible assets. Intangible asset impairment loss for the year ended 31 December 2011 of $0.02 million was recognised. During 2011, the amortisation expense amounted to $5.8 million (2010: $5.7 million) and the foreign exchange translation adjustment increased the net carrying amount by $0.07 million (2010: increased by $0.05 million). The estimated aggregate amortisation expense for each of the succeeding five years (until 31 December 2016) is $5.5 million.

NOTE 11: CUSTOMER DEPOSITS AND DEPOSITS FROM BANKS

a) By Maturity

	2011			2010		
	Customers	Banks	Total	Customers	Banks	Total
Demand deposits						
Demand deposits - Non-interest bearing	961,002	-	961,002	977,417	-	977,417
Demand deposits - Interest bearing	4,202,728	118,449	4,321,177	4,558,249	10,793	4,569,042
Sub-total - demand deposits	5,163,730	118,449	5,282,179	5,535,666	10,793	5,546,459
Term deposits						
Term deposits maturing within six months	2,005,446	6,410	2,011,856	2,353,217	64,133	2,417,350
Term deposits maturing between six to twelve months	131,932	382	132,314	132,359	4,753	137,112
Term deposits maturing after twelve months	98,970	121	99,091	127,138	-	127,138
Sub-total - term deposits	2,236,348	6,913	2,243,261	2,612,714	68,886	2,681,600
Total	7,400,078	125,362	7,525,440	8,148,380	79,679	8,228,059

b) By Type and Location

	31 December 2011			31 December 2010		
	Payable on demand	Payable on a fixed date	Total	Payable on demand	Payable on a fixed date	Total
Bermuda						
Customers	2,237,849	1,021,747	3,259,596	2,458,003	1,146,796	3,604,799
Banks	109,923	-	109,923	-	44,988	44,988
Barbados						
Customers	171,705	97,378	269,083	159,255	80,686	239,941
Cayman						
Customers	1,319,357	423,436	1,742,793	1,348,636	432,140	1,780,776
Banks	5,692	6,074	11,766	8,587	22,387	30,974
Guernsey						
Customers	1,018,084	316,172	1,334,256	1,010,897	450,895	1,461,792
Banks	2,834	388	3,222	1,516	-	1,516
The Bahamas						
Customers	55,350	3,968	59,318	84,357	37,606	121,963
United Kingdom						
Customers	361,385	373,647	735,032	474,518	464,591	939,109
Banks	-	451	451	690	1,511	2,201
Total Customers	5,163,730	2,236,348	7,400,078	5,535,666	2,612,714	8,148,380
Total Banks	118,449	6,913	125,362	10,793	68,886	79,679
Total	5,282,179	2,243,261	7,525,440	5,546,459	2,681,600	8,228,059

NOTE 12: EMPLOYEE FUTURE BENEFITS

The Bank maintains trusteed 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 final 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 an independent actuary.

The following table presents the expense constituents of the Bank's defined benefit pension plans and the Bank's post-retirement medical benefits:

For the year ended	2011		2010	
	Pension plans	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
Accumulated benefit obligation at year end	146,897	-	131,177	-
Change in projected benefit obligation				
Opening projected benefit obligation	140,874	81,114	125,470	141,645
Service cost	2,638	740	2,366	2,466
Employee contributions	245	-	248	-
Interest cost	7,355	4,428	7,424	6,521
Benefits paid	(9,377)	(2,047)	(5,727)	(2,452)
Settlement and curtailment of liability	(1,800)	-	-	-
Plan amendment	-	(3,704)	-	(40,641)
Actuarial loss (gain)	13,124	11,349	12,959	(26,425)
Foreign exchange translation adjustment	(587)	-	(1,866)	-
Closing projected benefit obligation	152,472	91,880	140,874	81,114
Change in plan assets				
Opening fair value of plan assets	143,978	-	135,986	-
Actual return on plan assets	5,458	-	10,931	-
Employer contribution	5,559	2,047	4,557	2,452
Employee contributions	245	-	248	-
Benefits paid	(9,377)	(2,047)	(5,727)	(2,452)
Foreign exchange translation adjustment	(540)	-	(2,017)	-
Closing fair value of plan assets	145,323	-	143,978	-

For the year ended	2011		2010	
	Pension plans	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
Amounts recognised in the Balance Sheet consist of:				
Prepaid benefit cost included in other assets	5,861	-	7,199	-
Accrued pension benefit cost included in employee future benefits liability	(13,010)	(91,880)	(4,095)	(81,114)
(Deficit) surplus of plan assets over projected benefit obligation at measurement date	(7,149)	(91,880)	3,104	(81,114)
Amounts recognised in accumulated other comprehensive income (loss) consist of:				
Net actuarial loss	(40,460)	(26,195)	(29,405)	(15,781)
Past service credit	-	35,066	-	37,520
Net amount recognised in accumulated other comprehensive income (loss)	(40,460)	8,871	(29,405)	21,739

Effective 31 December 2011, the Bank's post-retirement medical benefits were amended to freeze credited service and final average earnings for remaining active members. The benefits amendment resulted in a further reduction in the post-retirement medical liability of $1.8 million as at 31 July 2011. The benefits amendment is being amortised to the Statement of Operations over the expected average remaining service lifetime of the active employees in the plan.

The following table presents the expense constituents of the Bank's defined benefit pension plans and the Bank's post-retirement medical benefit plan:

For the year ended	2011		2010	
	Pension plans	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
Annual benefit expense				
Service cost	2,638	740	2,366	2,466
Interest cost	7,355	4,428	7,424	6,521
Expected return on plan assets	(9,173)	-	(8,617)	N/A
Amortisation of past service credit	-	(6,158)	-	(3,121)
Amortisation of net actuarial loss	4,027	935	3,386	1,634
Defined benefit expense	4,847	(55)	4,559	7,500
Defined contribution expense	5,496	-	5,043	-
Total benefit expense	10,343	(55)	9,602	7,500
Other changes recognised in other comprehensive income (loss)				
Net (loss) gain arising during the year	(15,082)	(11,349)	(10,645)	26,425
Past service credit arising during the year	-	3,704	-	40,641
Amortisation of past service credit	-	(6,158)	-	(3,121)
Amortisation of net actuarial loss	4,027	935	3,386	1,634
Total changes recognised in other comprehensive income (loss)	(11,055)	(12,868)	(7,259)	65,579

The estimated portion of the net actuarial loss for the pension plans that will be amortised from accumulated other comprehensive loss into benefit expense over the next fiscal year is $5.8 million. The estimated portion of the net actuarial loss and the past service credit for the post-retirement medical benefit plan that will be amortised from accumulated other comprehensive loss into benefit expense over the next fiscal year is $2.1 million for the net actuarial loss and a credit of $6.7 million for the past service credit.

	2011		2010	
	Pension plans	Post-retirement medical benefit plan	Pension plans	Post-retirement medical benefit plan
Actuarial assumptions used to determine annual benefit expense				
Weighted average discount rate	5.30%	5.50%	5.85%	6.10%
Weighted average rate of compensation increases	3.75%	N/A	3.80%	N/A
Weighted average expected long-term rate of return on plan assets	6.35%	N/A	6.45%	N/A
Weighted average annual medical cost increase rate	N/A	7.5% to 4.5% in 2027	N/A	7.5% to 4.5% in 2027
Actuarial assumptions used to determine benefit obligations at end of year				
Weighted average discount rate	4.65%	4.60%	5.30%	5.50%
Weighted average rate of compensation increases	1.70%	N/A	3.75%	N/A
Weighted average annual medical cost increase rate	N/A	7.5% to 4.5% in 2027	N/A	7.5% to 4.5% in 2027

For 2011, 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 a $1.0 million increase (2010: $2.1 million) and a $0.8 million decrease (2010: $1.6 million), respectively, and on the benefit obligation a $17.2 million increase (2010: $13.7 million) and a $13.8 million decrease (2010: $11.1 million), respectively.

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 funds. 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. The weighted average annual medical cost increase rate remained unchanged in 2011 at 7.5% to 4.5%.

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 & Investment Policy. The asset allocation is diversified and any use of derivatives is limited to hedging purposes only.

The weighted average actual and target asset allocations of the pension plans by asset category are as follows:

	2011		2010	
	Actual allocation	Target allocation	Actual allocation	Target allocation
Asset category				
Debt securities (including debt mutual funds)	45%	40%	46%	46%
Equity securities (including equity mutual funds)	50%	47%	52%	47%
Other	5%	13%	2%	7%
Total	100%	100%	100%	100%

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.

	2011				2010			
	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	-	5,890	-	5,890	-	8,242	-	8,242
Corporate debt securities	-	51,295	-	51,295	-	47,912	-	47,912
Debt securities issued by non-US governments	-	10,143	-	10,143	-	9,696	-	9,696
Equity securities and mutual funds	-	74,089	385	74,474	-	74,794	377	75,171
Other	-	3,521	-	3,521	-	2,957	-	2,957
Total fair value of plans' assets	-	144,938	385	145,323	-	143,601	377	143,978

At 31 December 2011, 26.3% (2010: 28.7%) 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 2011, 0.2% and 1.6% (2010: 0.4% and 1.6%) 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 2011 Bank contribution to, and estimated benefit payments for the next ten years under, the pension and post-retirement medical benefit plans are as follows:

2011	Pension Plans	Post-retirement medical benefit plan
Estimated Bank contributions for 2012	3,588	2,807
Estimated benefit payments by year:		
2012	5,700	2,807
2013	6,000	3,034
2014	6,400	3,271
2015	7,000	3,555
2016	6,900	3,791
2017 - 2021	35,600	22,876

The projected benefit obligation and fair value of plan assets for pension plans with projected benefit obligations in excess of plan assets were $127.5 million and $114.5 million as at 31 December 2011.

NOTE 13: CREDIT RELATED ARRANGEMENTS AND COMMITMENTS

Commitments

The Bank was committed to expenditures under contract for sourcing and leases of $112.5 million and $30.2 million, respectively, as at 31 December 2011 (2010: $133.2 million and $29.5 million, respectively). Rental expense for premises leased on a long-term basis for the year ended 31 December 2011 amounted to $5.7 million (2010: $5.8 million). The expenditures committed under the other agreements relate to the Balance Sheet Management Advisory Agreement entered into with Carlyle as disclosed in Note 26: Related Party transactions.

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

2011	Sourcing	Leases	Other agreements	Total
2012	24,886	5,971	4,000	34,857
2013	23,665	5,030	3,000	31,695
2014	22,746	4,941	-	27,687
2015	22,566	4,424	-	26,990
2016	18,671	3,645	-	22,316
2017 & thereafter	-	6,210	-	6,210
Total commitments	112,534	30,221	7,000	149,755

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 with contractual amounts representing credit risk as follows:

	2011			2010		
	Gross	Collateral	Net	Gross	Collateral	Net
Standby letters of credit	321,059	303,769	17,290	386,728	354,310	32,418
Letters of guarantee	13,388	9,876	3,512	14,115	8,655	5,460
Total	334,447	313,645	20,802	400,843	362,965	37,878

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 with contractual amounts representing credit risk as follows:

	2011	2010
Commitments to extend credit	491,251	402,567
Commitments to extend credit with terms modified by troubled debt restructuring	779	-
Documentary and commercial letters of credit	4,520	2,131
Total	**496,550**	404,698

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 2011, $137.1 million (2010: $174.5 million) of standby letters of credit were issued under this facility.

Legal Proceedings

There are a number of 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 not be material to the consolidated financial position of the Bank.

NOTE 14: INTEREST INCOME

Loans

The following table presents the components of loan interest income:

	2011	2010
Mortgages	95,885	97,667
Other loans	104,393	93,958
	200,278	191,625
Amortisation of loan premium / discount	-	53
Amortisation of fair value hedge	(2,498)	-
Amortisation of loan origination fees (net of amortised costs)	4,693	6,330
Total loan interest income	**202,473**	198,008
Balance of unamortised fair value hedge as at 31 December	**(11,656)**	-
Balance of unamortised loan fees as at 31 December	**7,951**	7,764

NOTE 15: SEGMENTED INFORMATION

At 31 December 2011, for management reporting purposes, the operations of the Bank are grouped into the following seven business segments based upon the geographic location of the Bank's operations: Bermuda, Barbados, 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 telephone banking, Internet 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 Barbados segment provides a range of community and commercial banking services through four branch locations, ATMs and debit cards. Services include deposit services, commercial banking, consumer and mortgage lending and credit cards.

The Cayman Islands segment provides a comprehensive range of community and commercial banking services to private and corporate customers through five locations and through Internet banking, ATMs and debit cards. Wealth management and fiduciary services are also provided.

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 institutional, corporate and private clients with a range of wealth management & fiduciary 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.

Total Assets by Segment

	2011	2010
Bermuda	4,577,775	5,192,585
Barbados	303,960	273,797
Cayman	1,974,338	2,036,512
Guernsey	1,479,901	1,617,976
Switzerland	1,118	1,191
The Bahamas	77,565	146,069
United Kingdom	976,451	1,104,946
	9,391,108	10,373,076
Less: inter-segment eliminations	(566,999)	(750,016)
Total	8,824,109	9,623,060

For the year ended 2011	Net interest income								
	Customer	Inter-segment	Provision for credit losses	Non-interest income	Revenue before gains and losses	Total expense	Net income (loss) before gains and losses	Gains and losses	Net income (loss)
Bermuda	131,056	881	(1,202)	67,081	197,816	176,726	21,090	4,754	25,844
Barbados	11,485	-	(1,156)	2,896	13,225	12,135	1,090	37	1,127
Cayman	36,568	757	(3,974)	30,650	64,001	54,988	9,013	1,955	10,968
Guernsey	18,396	(17)	(637)	21,664	39,406	30,245	9,161	242	9,403
Switzerland	1	-	-	663	664	2,075	(1,411)	-	(1,411)
The Bahamas	1,041	264	(633)	5,114	5,786	5,787	(1)	3	2
United Kingdom	14,573	(1,885)	(6,724)	10,929	16,893	20,253	(3,360)	45	(3,315)
Total before eliminations	213,120	-	(14,326)	138,997	337,791	302,209	35,582	7,036	42,618
Add / (less) inter-segment eliminations / transactions	615	-	-	(3,751)	(3,136)	(3,751)	615	(2,761)	(2,146)
Total	213,735	-	(14,326)	135,246	334,655	298,458	36,197	4,275	40,472

For the year ended 2010	Net interest income								
	Customer	Inter-segment	Provision for credit losses	Non-interest income	Revenue before gains and losses	Total expense	Net income (loss) before gains and losses	Gains and losses	Net income (loss)
Bermuda	113,259	104	(25,650)	71,325	159,038	192,174	(33,136)	(149,940)	(183,076)
Barbados	12,921	(4)	(1,707)	2,948	14,158	13,863	295	(151)	144
Cayman	26,590	1,981	(3,808)	32,389	57,152	50,145	7,007	(11,600)	(4,593)
Guernsey	12,521	(137)	-	23,003	35,387	27,625	7,762	(1,433)	6,329
Hong Kong*	1	-	-	2,119	2,120	1,730	390	(3,639)	(3,249)
Malta*	5	-	-	886	891	861	30	(3,790)	(3,760)
Switzerland	2	-	-	489	491	2,159	(1,668)	-	(1,668)
The Bahamas	2,270	48	(3,669)	5,201	3,850	7,812	(3,962)	-	(3,962)
United Kingdom	11,373	(1,992)	(7,136)	10,027	12,272	16,088	(3,816)	(9,964)	(13,780)
Total before eliminations	178,942	-	(41,970)	148,387	285,359	312,457	(27,098)	(180,517)	(207,615)
Add / (less) inter-segment eliminations / transactions	-	-	-	(4,967)	(4,967)	(4,967)	-	-	-
Total	178,942	-	(41,970)	143,420	280,392	307,490	(27,098)	(180,517)	(207,615)

* Disposed of the subsidiaries on 8 September 2010; disclosed in the 2010 annual financial statements.

NOTE 16: ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

The Bank uses derivatives in the asset and liability management ("ALM") of positions and to meet the needs of its customers with their risk management objectives. The Bank's derivative contracts principally involve over the counter 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 Sheet 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 Statement 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 Sheet 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, such that previously contracted derivative transactions have become more or less favourable than what can be negotiated under current market conditions for contracts with the same remaining period to maturity. 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 primarily enters into 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 interest rate 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 derivative instruments to hedge its exposure to interest rate risk and foreign currency risk. Certain hedging relationships are formally designated and qualify for hedge accounting as fair value or cash flow hedges. Other derivatives that are entered into for risk management purposes as economic hedges are not formally designated as hedges and, therefore, are accounted for as if they were trading instruments. In order to qualify for hedge accounting, a formal assessment is performed on a calendar quarter basis to verify that derivatives used in designated hedging transactions continue to be highly effective as offsets to changes in fair value or cash flows of the hedged item. If a derivative ceases to be highly effective, or if the hedged item matures, is sold, or is terminated, hedge accounting is terminated and the derivative is treated as if it were a trading instrument.

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 six months ended 30 June 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 will be amortised to net income over the remaining life of each individual loan using the effective interest method.

Cash flow hedges

Derivatives are designated as cash flow hedges in order to minimise the variability in cash flows of interest earning assets caused by movements in interest rates. The effective portion of changes in the fair value of such derivatives is recognised in accumulated other comprehensive income, a component of Shareholders' equity. When the hedged item impacts earnings, balances in other comprehensive income are reclassified to the same income or expense classification as the hedged item. The Bank applies the "shortcut" method of accounting for cash flow hedges of held to maturity investments, in assessing whether these hedging relationships are highly effective at inception and on an ongoing basis. Any ineffectiveness in cash flow hedge is recognised in earnings.

As of 31 December 2011 and 2010, there were no cash flow hedges in place and there were no deferred net gains or losses on derivative instruments accumulated in other comprehensive income in relation with cash flow hedges.

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 with banks and foreign exchange risk of the Bank's non-USD investments in subsidiaries. Changes in the fair value of derivative instruments not formally designated as hedges are recognised in 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 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 divided 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 Sheet 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.

2011	Derivative instrument	Notional amounts	Positive fair value	Negative fair value	Net fair value
Risk management derivatives					
Fair value hedges					
Fixed-rate loans	Interest rate swaps	11,436	-	(227)	(227)
Investments	Interest rate swaps	18,613	18	-	18
Sub-total fair value hedges		30,049	18	(227)	(209)
Not designated as hedging instruments					
	Currency swaps	346,453	1,031	(105)	926
	Foreign currency options	65,335	3,160	(651)	2,509
Sub-total not designated as hedges		411,788	4,191	(756)	3,435
Sub-total risk management derivatives		441,837	4,209	(983)	3,226
Client services derivatives					
	Spot and forward foreign exchange	5,775,477	44,207	(43,756)	451
	Interest rate caps	37,225	89	(89)	-
Sub-total client services derivatives		5,812,702	44,296	(43,845)	451
Total derivative instruments		6,254,539	48,505	(44,828)	3,677

2010	Derivative instrument	Notional amounts	Positive fair value	Negative fair value	Net fair value
Risk management derivatives					
Fair value hedges					
Fixed-rate loans	Interest rate swaps	175,858	47	(17,151)	(17,104)
Investments	Interest rate swaps	34,316	228	-	228
Customer deposits	Interest rate swaps	5,447	-	(26)	(26)
Sub-total fair value hedges		215,621	275	(17,177)	(16,902)
Not designated as hedging instruments					
	Interest rate swaps	360,000	1,481	(555)	926
	Currency swaps	264,843	4,028	(1)	4,027
Sub-total not designated as hedges		624,843	5,509	(556)	4,953
Sub-total risk management derivatives		840,464	5,784	(17,733)	(11,949)
Client services derivatives					
	Spot and forward foreign exchange	4,842,989	39,774	(39,755)	19
	Interest rate caps	37,435	389	(389)	-
Sub-total client services derivatives		4,880,424	40,163	(40,144)	19
Total derivative instruments		5,720,888	45,947	(57,877)	(11,930)

The following table shows the location and amount of gains (losses) recorded in the Consolidated Statement of Operations.

		For the year ended	
Derivative Instrument	**Consolidated Statement of Operations line item**	**2011**	2010
Interest rate swaps	Net other gains (losses)	**(906)**	1,154
Forward foreign exchange	Foreign exchange revenue	**699**	1,076
Foreign currency options	Foreign exchange revenue	**1,092**	-
Total net gains recognised in net income		**885**	2,230

NOTE 17: FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the financial assets and liabilities that are measured at fair value on a recurring basis and classifies such fair value based on the type of input used in the related valuations, as described in Note 2.

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 in Note 2.

Financial instruments in Level 1 include listed equity shares and 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 and forward foreign exchange contracts, and mutual funds not actively traded.

Financial instruments in Level 3 include non-redeemable private equity shares, corporate bonds, mortgage-backed securities and other asset-backed securities for which the market is relatively illiquid and for which information about actual trading prices is not readily available.

Items that are recognised at fair value on a recurring basis

	2011 Fair value				2010 Fair value			
	Level 1	Level 2	Level 3	Total carrying amount / Fair value	Level 1	Level 2	Level 3	Total carrying amount / Fair value
Financial assets								
Trading								
Debt securities issued by non-US governments	-	5,971	-	5,971	-	6,511	-	6,511
Mutual funds	5,368	51,252	-	56,620	10,021	1,556	-	11,577
Total Trading	5,368	57,223	-	62,591	10,021	8,067	-	18,088
Available for sale								
Certificates of deposit	-	356,493	-	356,493	-	859,146	-	859,146
US government and federal agencies	-	790,804	-	790,804	-	917,494	-	917,494
Debt securities issued by non-US governments	-	113,032	-	113,032	-	132,692	-	132,692
Corporate debt securities guaranteed by non-US governments	-	121,648	-	121,648	-	149,720	-	149,720
Corporate debt securities	-	408,962	-	408,962	-	347,470	-	347,470
Asset-backed securities - Student loans	-	133,182	11,164	144,346	-	135,632	11,179	146,811
Pass-through note	-	-	26,991	26,991	-	24,342	33,304	57,646
Equity securities	-	70	-	70	-	77	-	77
Total Available for sale	-	1,924,191	38,155	1,962,346	-	2,566,573	44,483	2,611,056
Other assets - Derivatives	-	48,505	-	48,505	-	45,947	-	45,947
Other assets - Closed ended real estate fund	-	-	6,199	6,199	-	-	9,044	9,044
Financial liabilities								
Other liabilities – Derivatives	-	(44,828)	-	(44,828)	-	57,877	-	57,877

Consistent with the significant accounting policy in Note 2, the current carrying value of other real estate owned will be adjusted to fair value only when there is a devaluation below cost.

Transfers of securities	2011		2010	
	Trading investments	Available for sale investments	Trading investments	Available for sale investments
Transfers out of Level 1	(50,035)	-	-	-
Transfers into Level 2	50,035	-	-	1,002,803

The transfer out of Level 1 and into Level 2 represents transfers of mutal funds classified at measurement date based on the level of trading.

Level 3 reconciliation	2011		2010		
	Available for sale investments	Closed ended property fund	Trading investments	Available for sale investments	Closed ended property fund
Carrying amount at beginning of year	44,483	9,044	296	382,452	8,307
Purchases	290	1,185	151	-	-
Proceeds from sale / Capital distributions	(3,973)	(3,765)	(447)	(103,064)	-
Accretion recognised in net income	1,776	-	-	(3,245)	1,020
Realised and unrealised losses recognised in other comprehensive income	(4,421)	(251)	-	(137,093)	-
Transfers in and out of Level 3	-	-	-	(94,567)	-
Foreign exchange translation adjustment	-	(14)	-	-	(283)
Carrying amount at end of year	38,155	6,199	-	44,483	9,044

Items other than those recognised at fair value on a recurring basis

	2011 Carrying amount	2011 Fair value	2011 Appreciation / (depreciation)	2010 Carrying amount	2010 Fair value	2010 Appreciation / (depreciation)
Financial assets						
Cash and cash equivalents	1,979,458	1,979,458	-	2,429,699	2,429,699	-
Short-term investments	34,814	34,814	-	26,392	26,392	-
Investments held to maturity	64,789	64,588	(201)	-	-	-
Loans, net of allowance for credit losses	4,247,260	4,241,040	(6,220)	4,043,360	4,043,360	-
Financial liabilities						
Customer deposits						
Demand deposits	5,163,730	5,163,730	-	5,535,666	5,535,666	-
Term deposits	2,236,348	2,232,570	3,778	2,612,714	2,621,188	(8,474)
Deposits from banks	125,362	125,362	-	79,679	79,679	-
Subordinated capital	267,755	225,019	42,736	282,799	244,606	38,193

NOTE 18: INTEREST RATE RISK

The following table sets 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 this table 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 pre-pay earlier, and certain term deposits, which are shown at contractual maturity but which may be withdrawn before their contractual maturity. Investments are shown based on expected duration, which the Bank believes is more representative of maturity date than actual contractual maturity.

2011	Earlier of maturity or repricing date						
(in $ millions)	Within 3 months	3 to 6 months	6 to 12 months	1 to 5 years	After 5 years	Non-interest bearing funds	Total
Assets							
Cash and cash equivalents	1,772	-	-	-	-	207	1,979
Short-term investments	15	5	3	-	-	12	35
Investments	450	209	128	993	253	57	2,090
Loans	3,534	121	53	368	117	54	4,247
Premises, equipment and computer software	-	-	-	-	-	276	276
Other assets	-	-	-	-	-	197	197
Total assets	5,771	335	184	1,361	370	803	8,824
Liabilities and Shareholders' equity							
Shareholders' equity	-	-	-	-	-	830	830
Demand deposits	4,321	-	-	-	-	961	5,282
Term deposits	1,712	300	132	99	-	-	2,243
Other liabilities	-	-	-	-	-	201	201
Subordinated capital	98	-	-	145	25	-	268
Total liabilities and Shareholders' equity	6,131	300	132	244	25	1,992	8,824
Interest rate swaps	2	8	(2)	(8)	-	-	-
Interest rate sensitivity gap	(358)	43	50	1,109	345	(1,189)	-
Cumulative interest rate sensitivity gap	(358)	(315)	(265)	844	1,189	-	-

2010	Earlier of maturity or repricing date						
(in $ millions)	Within 3 months	3 to 6 months	6 to 12 months	1 to 5 years	After 5 years	Non-interest bearing funds	Total
Assets							
Cash and cash equivalents	2,269	-	-	-	-	161	2,430
Short-term investments	19	-	1	-	-	6	26
Investments	1,139	14	200	1,115	92	69	2,629
Loans	3,588	63	48	138	109	97	4,043
Premises, equipment and computer software	-	-	-	-	-	262	262
Other assets	-	-	-	-	-	233	233
Total assets	7,015	77	249	1,253	201	828	9,623
Liabilities and Shareholders' equity							
Shareholders' equity	-	-	-	-	-	809	809
Demand deposits	4,569	-	-	-	-	977	5,546
Term deposits	2,042	376	137	126	1	-	2,682
Other liabilities	-	-	-	-	-	303	303
Subordinated capital	90	-	-	168	25	-	283
Total liabilities and Shareholders' equity	6,701	376	137	294	26	2,089	9,623
Interest rate swaps	448	-	(339)	(48)	(61)	-	-
Interest rate sensitivity gap	762	(299)	(227)	911	114	(1,261)	-
Cumulative interest rate sensitivity gap	762	463	236	1,147	1,261	-	-

NOTE 19: SUBORDINATED CAPITAL

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 pay a fixed coupon of 5.15% until 27 May 2013 when they become 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 2 April 2004, in conjunction with the acquisition of Leopold Joseph, the Bank assumed a subordinated debt of £5 million which is included in the Balance Sheet in the amount of $7.8 million. The issuance was by way of private placement in the United Kingdom and pays a fixed coupon of 9.29% until February 2012 when it becomes redeemable in whole at the option of the Bank and 10.29% thereafter until February 2017.

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 $60 million in Series B notes due 2020. The issuance was by way of private placement with US institutional investors. The notes are listed on the BSX in the specialist debt securities category. The notes issued under Series A paid a fixed coupon of 4.81% until 2 July 2010 after which the coupon rate became floating and the principal became redeemable in whole at the Bank's option. At 31 December 2011, the Bank has not redeemed any of the Notes issues under Series A and effective 2 July 2010 the coupon rate became floating at 3 months US$ LIBOR + 1.095%. 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 5-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.

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 pay a fixed coupon of 7.59% until 27 May 2013 when they become redeemable in whole at the option of the Bank. 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 A notes were priced at a spread of 4.34% over the 5-year US Treasury yield and the Series B notes were priced at a spread of 4.51% over the 10-year US Treasury yield.

Interest capitalised during 2011 amounted to $2.8 million (2010: $3.0 million) and is excluded from interest expense in the Consolidated Statement of Operations.

The following table presents the contractual maturity and interest payments for subordinated capital issued by the Bank as at 31 December 2011. The interest payments are calculated until contractual maturity using the current LIBOR rates.

The following table presents for the remaining subordinated capital issued by the Bank as at 31 December 2011.

Subordinated capital	Earliest date redeemable	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
Bermuda								
2003 issuance - Series B	27 May 2013	27 May 2018	5.15%	3 months US$ LIBOR + 2.000%	47,000	2,421	5,464	1,815
2005 issuance - Series A	2 July 2010	2 July 2015	4.81%	3 months US$ LIBOR + 1.095%	90,000	1,470	4,029	-
2005 issuance - Series B	2 July 2015	2 July 2020	5.11%	3 months US$ LIBOR + 1.695%	45,000	2,300	8,184	3,841
2008 issuance - Series A	27 May 2013	27 May 2018	7.59%	3 months US$ LIBOR + 4.185%	53,000	4,023	10,870	3,779
2008 issuance - Series B	27 May 2018	27 May 2023	8.44%	3 months US$ LIBOR + 4.929%	25,000	2,110	8,440	10,056
Subsidiary	8 February 2012	8 February 2017	9.29%	10.29%	7,755	759	3,192	399
Total					267,755	13,083	40,179	19,890

NOTE 20: EARNINGS PER SHARE

Earnings per Share has 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. Diluted earnings per Common Share include the dilutive effect resulting from the conversion of Treasury stock. Numbers of Shares are expressed in thousands.

	2011	2010
Basic earnings per Share		
Net income (loss) for the year	40,472	(207,615)
Less: Preference dividends declared and guarantee fee	(21,270)	(18,000)
Net income (loss) attributable to Common Shareholders	19,202	(225,615)
Weighted average number of participating Shares[1]	556,933	479,882
Weighted average number of Common Shares held as Treasury stock	(2,283)	(2,657)
Adjusted weighted average number of Common Shares	554,650	477,225
	0.03	(0.47)
Diluted earnings per Share		
Net income (loss) attributable to Common Shareholders	19,202	(225,615)
Weighted average number of participating Shares [1]	556,933	479,882
Weighted average number of Common Shares held as Treasury stock	(2,283)	(2,657)
Weighted average number of dilutive Share-based awards	965	-
Adjusted weighted average number of diluted Common Shares	555,615	477,225
	0.03	(0.47)

[1] The Contingent Value Convertible Preference Shares are classified as participating securities as they are entitled to dividends declared to Common Shareholders on a 1:1 basis and are therefore included in the basic earnings per Share calculation.

During 2011, weighted-average options to purchase 34.5 million (2010: 26.5 million) Shares of Common stock (see Note 21), were outstanding but were anti-dilutive and, therefore, not included in the computation of diluted earnings per Share. Each of these options was considered anti-dilutive because the sum of the option's expense that will be recognised in the future and its exercise price was greater than the average market price of the Bank's Common stock.

During 2011, the weighted-average number of outstanding awards of unvested Common Shares (see Note 21) was 3.28 million (2010: nil). All unvested awards of Common Shares were considered dilutive because each award's unrecognised expense was lower than the average market price of the Bank's Common stock. The awards' yet unrecognised expense is considered to be the proceeds the employees would need to pay to purchase accelerated vesting of the awards. For purpose of calculating dilution, such proceeds are assumed to be used by the Bank to buy-back Shares at the average market price. The weighted-average number of outstanding awards net of the assumed weighted-average number of 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 $3.61 for 4.15 million Shares of Common stock were not included in the computation of earnings per Share in 2011 and 2010 because the exercise price was greater than the average market price of the Bank's Common stock.

NOTE 21: SHARE-BASED PAYMENTS

The following table presents the Share-based compensation cost that has been charged against net income and the value of Share-based settlements.

	For the year ended					
	2011			2010		
	Stock option plans	EDIP and ELTIP	Total	Stock option plans	EDIP and ELTIP	Total
Share-based compensation plans						
Awards granted in years 2009 and prior				2,655	3,381	6,036
Awards granted in years 2010 and 2011	1,703	1,876	3,579	1,305	-	1,305
Total Share-based compensation	1,703	1,876	3,579	3,960	3,381	7,341
Share-based settlement plans						
Directors Shares and retainers settlement plans			344			271
Total Share-based payments			3,923			7,612

Unrecognised expense	For the year ended 2011
2010 Stock Option Plan	
Time Vesting Options	5,731
Performance Vesting Options	9,169
2011 EDIP	915
2011 ELTIP	
Time Vesting Shares	952
Performance Vesting Shares	961
	17,728

On 22 February 2011, the Board approved the 2010 Employee deferred incentive plan and the 2011 Executive long-term incentive Share plan.

2010 Employee Deferred Incentive Plan ("EDIP")

Under the Bank's 2010 EDIP Plan, Shares were awarded to Bank employees and Executive Management based on time vesting condition, which states that the Shares will vest equally over a three-year period from the effective grant date, subject to the employee's continued employment.

	2011 Number of Shares transferable upon vesting (thousands)
Outstanding at beginning of year	-
Granted	1,361
Vested	(11)
Forfeited / cancelled	(74)
Outstanding unvested at end of year	1,276

2011 Executive long-term incentive Share plan ("ELTIP")

Under the Bank's 2011 ELTIP Plan, Shares were awarded to Bank employees and Executive Management, based on predetermined vesting conditions. The ELTIP Plan comprises two types of vesting conditions upon which the Shares will be awarded, i.e.,:

Time Vesting Condition – 50% of each Share award is granted in the form of Time Vested Shares, vesting over a three-year period from the effective grant date, subject to the employee's continued employment; and

Performance Vesting Condition – 50% of each Share award is granted in the form of Performance Shares, vesting upon the achievement of certain performance targets.

	2011 Number of Shares transferable upon vesting (thousands)
Outstanding at beginning of year	-
Granted	2,560
Vested	(10)
Forfeited / cancelled	(35)
Outstanding unvested at end of year	2,515

2010 Stock Option Plan

Under the Bank's 2010 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 last traded Common Share price when granted and have a term of 10 years. The Plan comprises two types of vesting conditions upon which the options will be awarded, i.e.,:

Time Vesting Condition – 50% of each option award is granted in the form of Time Vested Options and vests 25% on the 2nd, 3rd, 4th and 5th anniversary of the effective grant date, subject to the employee's continued employment; and

Performance Vesting Condition – 50% of each option award is granted in the form of Performance Options and vests on a "Valuation Event" date (date any of the 2 March 2010 Investors transfers at least 5% of total number of Shares or the date that there is a change in control) and any of the New Investors achieve a Multiple of Invested Capital ("MOIC") based on predetermined MOICs. In the event of a Valuation Event and the MOIC reaching 200%, all options would vest.

No options were exercised during the year ended 31 December 2011.

	Time Vested Options	Performance Options
Weighted average fair value of stock options granted in the year ended 31 December 2011	**$0.41**	**$0.43**
Weighted average fair value of stock options granted in the year ended 31 December 2010	$0.62	$0.66

The weighted average fair value of stock options granted in the year ended 31 December 2011 was calculated using the Black-Scholes-Merton option-pricing model for the Time Vested Options and the Monte Carlo method for the Performance Options using the following weighted average assumptions:

	Time Vested Options	Performance Options
	0% for 2010-2012	0% for 2010-2012
	1.0% for 2013	1.0% for 2013
	2.0% for 2014	2.0% for 2014
Projected dividend yield	3.5% for 2015 and later years	3.5% for 2015 and later years
Risk-free interest rate	2.0% to 2.2%	0.0% to 3.6%
Projected volatility	36%	36%
Expected life (years)	6.75 years	8 to 9 years

The projected dividend yield is based on the Bank's estimate, as the Bank has suspended dividend payments, but expects to start paying dividends in 2013. The projected volatilities are based on the historical trading prices of the Bank's Common Shares. The risk-free interest rate for periods within the expected life of the option is based on the US Treasuries yield curve in effect at the time of grant. As the time vested options granted are "plain vanilla" options, the Bank uses one-half of the time between the average vesting date and the full option term to estimate the expected option life; separate groups of employees that have similar historical exercise behaviour are considered separately for valuation purposes.

	2011			
	Number of Shares transferable upon exercise (thousands)	**Weighted average exercise price ($)**	**Weighted average life remaining (years)**	**Aggregate intrinsic value ($ thousands)**
Outstanding at beginning of year	**34,308**	**3.26**		
Granted	**1,260**	**1.24**		
Forfeited / cancelled	**(1,936)**	**6.79**		
Outstanding at end of year	**33,632**	**3.02**	**5.91**	**-**
Vested and exercisable at end of year	**5,431**	**12.41**	**4.95**	

	2010			
	Number of Shares transferable upon exercise (thousands)	Weighted average exercise price ($)	Weighted average life remaining (years)	Aggregate intrinsic value ($ thousands)
Outstanding at beginning of year	12,428	11.72		
Granted	28,137	1.21		
Forfeited / cancelled	(6,257)	11.04		
Outstanding at end of year	34,308	3.26	8.68	1,069
Vested and exercisable at end of year	6,275	12.38	5.61	

Directors' Compensation
The Bank's Non-Executive Directors received their annual retainer compensation in the form of cash or fully vested and unrestricted Bank Shares, or a combination of the two.

During 2010, a Bank Non-Executive Director received additional compensation in the form of a one-time Shares grant vesting over a two-year period amounting to $0.25 million. The Bank has recognised $0.2 million compensation expense for the year ended 31 December 2011 related to the time vesting Shares granted.

NOTE 22: SHARE BUY-BACK PLANS
During the years 2011 and 2010, no Common Shares were purchased.

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 the programme, but under BSX regulations such trades must not be pre-arranged and all repurchases must be made in the open market. Prices paid by the Bank must not, according to BSX regulations, be higher than the last independent trade for a 'round lot', defined as 100 Shares or more.

The BSX must be advised monthly of Shares repurchased and cancelled by the Bank and Shares purchased by both the Bank's Stock Option Trust and the Bank's Charitable Trust.

NOTE 23: CAPITAL STRUCTURE
Authorised capital
The Bank's total authorised Share capital as of 31 December 2011 consisted of (i) 26 billion Ordinary 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 2 March 2010, the Bank issued 144.8 million Common Shares of par value $1 per Share, for a consideration of $175 million.

Following the Bank's Annual General Meeting held on 8 April 2010, The Bank of N.T. Butterfield & Son Limited's Shareholders approved an increase in the authorised Share capital to 26,000,000,000 Common Shares of par value BD$0.01. Subsequent to the increase, conversion of 281,770 Mandatorily Convertible Preference Shares into 233,157,035 Common Shares and 93,230 Contingent Convertible Preference Shares into 77,144,993 Common Shares took place.

At the Special General Meeting of Shareholders held on 14 April 2009, the Board of Directors were granted the authority to issue, allot or grant options, warrants or similar rights over or otherwise dispose of all the authorised but unissued Share capital of the Bank.

On 11 May 2010, the rights were over subscribed with the maximum allowable number of rights of 107,438,016 were exercised and subsequently converted on the ratio of 0.92308 Common Shares for each right unit exercised, amounting to 99,173,842 Common Shares issued.

Following the closing of the Rights Offering on 11 May 2010, the gross proceeds of $130 million were used to repurchase 107,571,361 Shares from the 2 March 2010 investors at the same price at which the investors originally subscribed for the Shares.

As part of the cost of the Capital Raise, the Bank's investment adviser was compensated $10 million in cash and $3.5 million in Common Shares at the same prices as the New Investors. On 12 May 2010, in settlement of the aforementioned, the Bank issued 2,896,152 Common Shares to the Bank's investment adviser.

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 principal and dividend payments are guaranteed by the Government of Bermuda.

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 $1,000 per Preference Share payable quarterly in arrears.

At any time after the expiry of the guarantee offered by the Government of Bermuda, and subject to the approval of the Bermuda Monetary Authority, 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.

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.

On 2 March 2010, the Bank issued 281,770 Mandatorily Convertible Preference Shares of par value $0.01 per Share and 93,230 Contingent Convertible Preference Shares of par value $0.01 per Share, for a consideration of $281.8 million and $93.2 million, respectively. Subsequent to the Bank's Annual General Meeting held on 8 April 2010, the 281,770 Mandatorily Convertible Preference Shares and 93,230 Contingent Convertible Preference Shares were converted into 233,157,035 and 77,144,993 Common Shares, respectively.

As stated above, on 11 May 2010, 107,438,016 rights were exercised and subsequently converted on the ratio of 0.07692 Contingent Value Convertible Preference Share for each right unit exercised amounting to 8,264,157 Contingent Value Convertible Preference Shares ("CVCP") issued. The Contingent Value Preference Shares have specific rights and conditions attached which is explained in detail in the Prospectus of The Rights Offering.

Following the Capital Raise on 2 March 2010 under the terms of the 4,279,601 warrants with an exercise price of $7.01 previously issued to the Government of Bermuda in conjunction with the issuance of 200,000 Government guaranteed 8% Non-Cumulative Perpetual Limited Voting Preference Shares in 2009 were adjusted in accordance with the terms of the guarantee. Subsequently, the Government of Bermuda now holds 4,150,774 warrants with an exercise price of $3.61.

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 Bermuda Monetary Authority 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.

The Bank is fully compliant with all regulatory capital requirements and maintains capital ratios well in excess of regulatory minimums as at 31 December 2011. As at 31 December 2011, the Bank's regulatory capital stood at $1,041 million (2010: $1,067 million) with the consolidated Tier 1 total and Total Capital ratios being 17.7% and 23.5%, respectively (2010: 15.7% and 21.6%, respectively).

NOTE 24: VARIABLE INTEREST ENTITIES

The Bank had no investments in variable interest entities for which it was deemed the primary beneficiary for the years ended 31 December 2011 and 2010.

The Bank has an equitable mortgage in a hospitality related company that has been placed under Receivership and as the Bank is an equity holder at risk, the hospitality related company was considered to be a variable interest entity. As the Bank did not have the legal power to direct the activities of the company that most significantly impact the company's economic performance it was considered not to be the primary beneficiary.

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, Barbados and Switzerland are subject to the tax laws of those jurisdictions and the jurisdictions in which they operate.

For the years ended 31 December 2011 and 2010, the Bank did not record any unrecognised tax benefits or expenses and has no uncertain tax positions as at 31 December 2011.

The Bank records income taxes based on the enacted tax laws and rates applicable in the relevant jurisdictions for each of the years ended 31 December 2011 and 2010. For the year ended 31 December 2011, the Bank recorded net interest received of $0.03 million and penalties payable of $0.02 million.

The components of income taxes attributable to the Bank's subsidiaries' operations for the years ended 31 December 2011 and 2010 were as follows:

31 December	2011	2010
Income taxes in Consolidated Statement of Operations		
Current	1,006	(3,676)
Deferred	(1,039)	1,701
Total tax (benefit) expense	(33)	(1,975)
Deferred income tax asset		
Tax loss carried forward	6,755	5,797
Pension liability	747	515
Fixed assets	738	676
Allowance for compensated absence	27	30
Onerous leases	11	115
Other	532	490
Total asset	8,810	7,623
Deferred income tax liability		
Other	(444)	-
Net deferred income tax asset	8,366	7,623

Management believes it is more likely than not that the tax benefit of the remaining net deferred tax assets will be realised.

NOTE 26: RELATED PARTY TRANSACTIONS

Butterfield Fulcrum Group Limited ("BFG")

On 8 February 2011, the Bank entered into an agreement with an investor group (comprised of BV Investor Partners, Glen Henderson and Tim Calveley, (the "BV Investor Group")) to dispose of its 36% equity interest on a diluted basis in BFG. The sale was completed in the second quarter of 2011 and resulted in a gain on sale of $3.1 million.

Under the terms of the agreement, the BV Investor Group paid down BFG's existing debt and revolving credit facility with the Bank and combined their overall funding requirements with another related entity, FORS Limited ("FORS"), whereby the total loan facilities post-disposition, on commercial market terms as to interest rate, repayment terms and security, is $45.1 million. A Bank Non-Executive Director is a minority shareholder of less than 1% of BFG.

As a result of the sale, the Bank paid a dividend of $3.3 million during the third quarter to Contingent Value Convertible Preference Shareholders of record on 26 July 2011.

In addition, the Bank has guaranteed to purchase services from BFG, on normal commercial market terms, for three years at minimum agreed revenue levels of $5.5 million, $5.0 million and $4.5 million per annum. In the event there is a shortfall, the Bank is required to pay 38% of the shortfall.

Renegotiations of agreements occurred during the third and fourth quarter of 2011, resulting in an expected shortfall from the revenue guarantees over the three-year period, whereby the resultant fair value of the liability is estimated at approximately $0.5 million as at 31 December 2011.

Employee loan programme

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 2011 amount to $251.9 million (2010: $219.0 million) resulting in an interest rate benefit to employees of $6.5 million (2010: $6.2 million).

Interested and Director transactions

The Bank provides loans and other banking services to the Bank's Directors, as well as their immediate family members and companies with which they are affiliated, as described in Section 96 of the Companies Act 1981, in the ordinary course of business the Bank provides these services on normal commercial terms in respect of interest rates, repayment terms and security.

During the third quarter of 2011, the Bank provided a loan to a trust company controlled by a Bank Non-Executive Director, amounting to $2.45 million. The terms of the loan are market related including comprehensive security provided.

Charitable Trust

The Bank has historically provided a loan facility to the Charitable Trust. At 31 December 2011 and 2010, the carrying value of the loan was $1.2 million. The Charitable Trust used the Loan to purchase Shares in the Bank: 772,971 of the Bank's Common Shares and 6,223 of the Bank's Contingent Value Preference Shares at 31 December 2011 and 2010.

Financing transactions

Capital transaction

Canadian Imperial Bank of Commerce ("CIBC") and funds associated with the Carlyle Group each hold approximately 18% of the Bank's equity voting power, along with the right to each designate two persons for nomination for election by the Shareholders as member of the Bank's Board of Directors.

Liquidity Facility Agreement

During 2010, the Bank entered into a commitment letter for a $500 million line of credit at market rates with CIBC, which was subsequently reduced to $300 million. The Bank cancelled the credit facility effective 1 March 2011.

Balance Sheet Management Advisory Agreement

The Bank entered into a Balance Sheet management advisory agreement with Carlyle Investment Management LLC, an affiliated company of the Carlyle Group with an effective date of 1 October 2010. Per the agreement the Carlyle Group has agreed to provide Balance Sheet management advisory services to the Bank, including advisory services on valuation assessments, for an annual fee of $4 million for a three-year period.

Financial instruments with related parties

At 31 December 2011, the Bank held $15.9 million in cash and cash equivalents with CIBC and CIBC held $1 million in deposits with the Bank. For the year ended 31 December 2011, the Bank held forward exchange contracts with CIBC with a notional amount of $295.8 million and a net realised loss amount of $5.7 million. As noted in Note 16, the Bank enters into client service forward exchange contracts to meet the foreign exchange needs of its customers.

NOTE 27: COMPARATIVE INFORMATION

Certain prior period figures have been reclassified to conform to current period presentation.

NOTE 28: SUBSEQUENT EVENTS

The Financial Statements were available to be issued and subsequent events have been evaluated up to 29 February 2012.

SHAREHOLDER INFORMATION

DIRECTORS' AND EXECUTIVE OFFICERS' SHARE INTERESTS AND DIRECTORS' SERVICE CONTRACTS

Pursuant to Regulation 6.8(3) of Section IIA of the Bermuda Stock Exchange Listing regulations, the ownership of Common Shares and Contingent Value Convertible Preference Shares of the Bank by all Directors and Executive Officers as at 31 December 2011 was 7,750,255 Shares. In addition, this group owns 140 Non-Cumulative Perpetual Limited Voting Preference Shares. As of 31 December 2011, Executive Officers also owned 23,470,000 stock options pursuant to the 2010 Stock Option Plan to vest in accordance with timelines established by the Plan. In 2010, a Non-Executive Director received additional compensation in the form of a one-time Share grant of 172,413 Shares to vest over a two-year period. None of the Directors or Executive Officers had any interest in any debt securities issued by the Bank or its subsidiaries as at 31 December 2011.

There are no service contracts with Directors, except for that of Bradford Kopp, President & Chief Executive Officer, whose contract expires on 1 March 2013.

Save for the foregoing contract, and those arrangements described in Note 26 to the Bank's Financial Statements, there are no other contracts of significance subsisting during or at the end of the financial year ended 31 December 2011 in which a Director of the Bank is or was materially interested, either directly or indirectly.

EXCHANGE LISTING

The Bank's Shares are listed on the Bermuda Stock Exchange (BSX) and the Cayman Islands Stock Exchange (CSX), which are located at:

BERMUDA STOCK EXCHANGE

(Primary Listing)
30 Victoria Street
Hamilton, HM 12
P.O. Box HM 1369
Hamilton HM FX
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Tel: (441) 292 7212
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CAYMAN ISLANDS STOCK EXCHANGE

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SHARE PRICE

Published daily in *The Royal Gazette* in Bermuda and available on *Bloomberg Financial Markets* (symbol: NTB BH).

Also available on the BSX and CSX websites.

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WRITTEN NOTICE OF SHARE REPURCHASE PROGRAMME — BSX REGULATION 6.38

No Shares were purchased under any Share repurchase programme in 2011.

LARGE SHAREHOLDERS

At 31 December 2011, the following were registered holders of 5% or more of the issued Share capital:

Canadian Imperial Bank of Commerce, 18.64%
Carlyle Global Financial Services Partners LP, 18.64%
Wellcome Trust Investments, 6.88%
Ithan Creek Master Investor (Cayman) LP, 6.71%
Rosebowl Western, 6.71%

PRINCIPAL OFFICES & SUBSIDIARIES

This list does not include all companies in the Group.

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Group Parent Company, Community Banking, Private Banking, Credit and Treasury Services

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BERMUDA

Country Head: Michael Collins,
Senior Executive Vice President

Butterfield Asset Management Limited
Investment Management

Managing Director: Michael Neff
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Grosvenor Trust Company Limited
Personal Trust and Corporate Trust

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GUERNSEY

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Fiduciary Services

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