



Philippine National Bank (Europe) Plc

Pillar 3 Disclosures

31 December 2022

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INTRODUCTION

Overview – Scope and Purpose

This document sets out the Pillar 3 disclosures (the “document”) for Philippine National Bank (Europe) Plc (“PNBE” or “the Bank”) as at 31 December 2022. PNBE is a UK-registered bank authorized by the Prudential Regulation Authority (“PRA”) and regulated by the Financial Conduct Authority (“FCA”) and the PRA.

These disclosures have been prepared to give information on the basis of calculating capital requirements and on the management of risks faced by the Bank. This document has been developed in accordance with the rules laid out in Part 8 of the UK Capital Requirements Regulation (“CRR”). The Bank has also considered the Basel Committee on Banking Supervision’s Standards “Revised Pillar 3 disclosure requirements” published in January 2015.

The provision of meaningful information about common key risk metrics to market participants is an important aspect of a sound banking system. It reduces information asymmetry and helps promote comparability of bank’s risk profiles within and across jurisdiction. Pillar 3 of the Basel II framework aims to promote market discipline through regulatory disclosure requirements. These requirements enable market participants to access key information relating to bank’s regulatory capital and risk exposures in order to increase transparency and confidence about a bank’s exposure to risk and the overall adequacy of its regular capital.

The Basel II Framework is structured around three pillars:

- Pillar 1: sets the minimum capital requirements for credit, market and operational risk
- Pillar 2: requires that each bank undertakes an Internal Capital Adequacy Assessment Process (“ICAAP”) to assess its own risk profile and to determine the level of additional capital required over and above the Pillar 1 requirements, to cover risks either not covered, or not fully covered, by the Pillar 1 requirements (e.g. credit concentration risk), and factors external to the firm (e.g. external stresses).
- Pillar 3: aims to promote market discipline by enhancing the level of disclosure made by banks to their stakeholders, allowing them to assess a bank’s key risk exposures and the adequacy of bank’s risk management process to mitigate these risks.

Pillar 3 complements Pillar 1 and Pillar 2.

This disclosure document should be read in conjunction with the Bank’s Annual Report and Financial Statements for the year ended 31 December 2022 and is published on the Bank’s website: <http://www.pnb.com.ph/europe>.

The Bank has no subsidiaries and accordingly disclosures are on un-consolidated basis.

These Pillar 3 disclosures are not subject to external audit. The document has been reviewed by the Audit, Risk and Compliance (“ACR”) Committee and approved by the Board of Directors (“the Board”).

Background

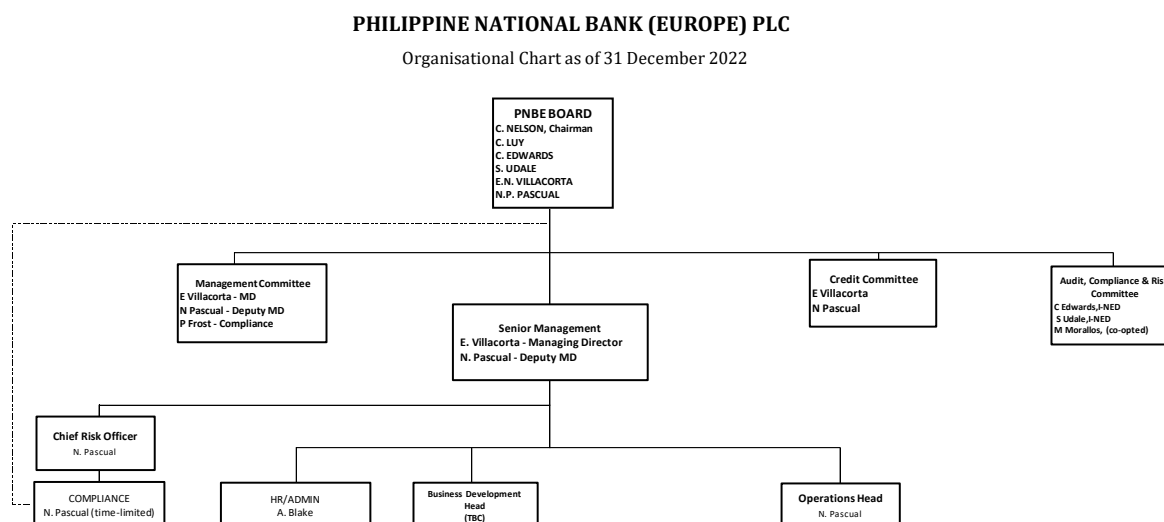
The Bank is a wholly owned subsidiary of Philippine National Bank (Manila). It was originally set up as PNB London Branch in 1976 and then converted in 1997 into a UK- registered bank with a full banking license. In April 2014, the PNBE has merged with Allied Bank Philippines (UK) Plc.

Its principal activity is the provision of banking and payments services primarily to Filipino customers in the United Kingdom.

RISK MANAGEMENT OBJECTIVES AND POLICIES

Governance

The Bank's governance policies are set by the Board and implemented by the management team. The chart below illustrates the Organization structure of the Bank.



The Board has ultimate responsibility for setting the Bank's strategy, risk appetite and control framework; and measures performance against targets. It normally meets a minimum of four times a year. The Board is also responsible for discharging the Bank's responsibilities under the remuneration policy; approving the appointment of senior executives; and agreeing authority levels and the delegation of authority. To assist it in discharging these responsibilities, the Board has instituted a number of high-level committees governed by clear term of reference.

Audit, Compliance and Risk Committee – Chaired by a Non-Executive Director. This Committee includes another Non-Executive Director and the group Chief Technology Officer also as co-opted member who was invited by the committee to represent a specific area of interest or issue of consideration like IT matters. All members of the committee have no executive responsibility for the management of the Bank. The Managing Director, the Deputy Managing Director and the Compliance Officer are invited to attend most of the meetings.

This Committee, which normally meets a minimum of four times a year, is responsible for evaluating the Bank's risk principles, risk policies, risk capacity and risk appetite and makes appropriate recommendations to the Board. It monitors the effectiveness of the Bank's risk policies in practice and evaluates the risk of new business proposals.

This Committee is also responsible for transparency in the financial performance of the Bank, including high quality and timely reporting and disclosure in line with regulatory requirements, good corporate governance and recognised best practice. The Committee also considers the nature and scope of audit reviews and the effectiveness of the system of internal control, compliance and risk management. The Bank's external auditors are also invited to attend the meetings when necessary.

Management Committee – Chaired by the Managing Director, this Committee's other members are the heads of Operations and Compliance. It is responsible for implementing Board policy and the day-to-day running of the Bank. It reviews risks and controls that mitigate the risks. This includes the identification, assessment and reporting of risks together with regular monitoring to confirm that risks are within the levels agreed by the Board. The Committee meets monthly or as required.

Credit Committee – Chaired by the Managing Director, this Committee includes the Deputy Managing Director and the Business Development Head. It operates as a working committee, accountable to the Board through the Audit, Compliance and Risk Committee and has a duty to consider all credit applications from customers and counterparties that do not exceed any delegated authority from the Board. Meetings are held as and when necessary and or according to business needs.

OWN FUNDS, CAPITAL REQUIREMENTS AND CAPITAL BUFFERS

Own Funds

Throughout 2022, the Bank complied fully with the Capital Requirements set out by the PRA. On 31 December 2022, all of the Bank's capital was comprised as follows:

Own Fund Composition		
GBP '000	As at 31 Dec 2022	% to Total Own Funds
Share capital	10,914	107.56%
Profit and loss reserve	(7,535)	-74.26%
Merger reserve	6,768	66.70%
Own Funds (Total capital)	10,147	100.00%

Tier 1 capital comprises ordinary share capital plus reserves. The Bank does not hold any Tier 2 capital.

Capital Requirements

Overall responsibility for capital management rests with the Board of Directors. Responsibility for oversight on a day-to-day basis has been delegated to the Managing Director who has, in turn, delegated responsibility for the management, review and reporting and capital management to the Deputy Managing Director who is in charge of Financial Control of the Bank. The use of Bank's capital to support current and future activities is monitored on a continuous basis through daily management information produced by Financial Control and sent to the senior management and also reported during the regular meetings of the Audit, Compliance and Risk Committee and the Board.

The Bank produces an ICAAP. It includes an assessment of the Bank's capital needs based upon the minimum regulatory requirements and additional capital charges that the Bank deems prudent to include. These additional capital charges take account of factors such as: the current quality of the credit exposures; the risks associated with any existing concentrations in particular geographical areas or industry sectors; risk identified from stress testing and scenario analysis particularly in the area of the Bank's view of how potential economic changes may affect the banking industry or its customers; and capital charges for planned business projects.

The ICAAP represents Bank's views on the necessary Pillar 2A capital requirement which are the Banks' capital requirements for the risks that are not covered, or fully covered, under Pillar 1. In completing the ICAAP assessment PNBE considers as Pillar 2A capital requirement the higher of its own Pillar 2A and the Individual Capital Guidance ("ICG") set by regulators.

The Bank's Capital Requirements are determined in accordance with the CRR relevant articles, the related EBA Technical Standards and the rules defined in the prudential guidelines by the PRA.

The Bank has adopted the Standard Approach ("SA") to Credit Risk and Market Risk and the Basic Indicator Approach ("BIA") to Operational Risk for the calculation of Pillar 1 capital requirements.

The Bank's Pillar 1 capital requirements are presented in the table below:

GBP '000	As at 31 Dec 2022	
	RWAs	Capital Requirements
Credit and counterparty credit risk	5,075	380
Market risk	41	3
Operational risk	3,045	244
Total Pillar 1 capital requirements	<u>8,161</u>	<u>627</u>
<i>100% Base capital requirement (equivalent of €5m)</i>		<u>4,401</u>

The Bank has considered the higher of total Pillar 1 plus Pillar 2A capital requirements based on the ICG and the initial (base) capital requirement of equivalent to €5 million as its minimum capital requirement.

Capital Buffers

The Bank calculates the CET1 capital ratio as per CRR requirements. As shown in table below, the Bank is compliant with the regulatory limits set in Article 92.

	31 December 2022
	RWAs
CET1 capital ratio ^{1/}	124.34%

^{1/}Being CET1 capital the same as Tier 1 capital and Total capital, the CET1 capital ratio is equal to Tier 1 capital ratio and Total capital ratio.

In addition to capital requirement, the Bank is compliant with the following capital buffers:

- PRA buffer, the amount of capital firms should maintain to absorb losses that may arise under a severe scenario, while avoiding duplication with the combined buffers. The PRA buffer of PNBE was computed at 1.78% of total RWAs.
- Combined buffer comprising the Capital Conservation Buffer (CCB) and the Countercyclical Buffer (CCyB):
 - CCB is intended to ensure that firms build up buffers of capital outside any periods of stress and is designed to avoid breaches of minimum capital requirements. This capital buffer can then be drawn upon in times when losses are incurred. Since its introduction in 2016 on a phased-in implementations, the CCB rate has now been fully implemented from 2019 and being computed at 2.5% of the total RWAs.
 - CCyB requires firms to build up capital when aggregate credit growth is judged to be associated with a build-up of system-wide risk to ensure the banking system has a buffer of capital to protect it against future losses. The buffer can then be drawn down to absorb losses during stressed periods. The UK CCyB rate of 1.0% is applicable from 13 December 2022 and computed at 1.0% of the total RWAs.

CREDIT RISK

Qualitative Disclosure

Credit risk is the risk that financial institutions and other counterparties will be unable to meet their obligations to the Bank which may result in financial losses. The Bank's credit risk exposure arises out of its short-term deposit held with its correspondent banks.

Counterparty risks with correspondent banks relate to spot delivery of currency arising out of the Bank's remittance business and reimbursements under trade related letters of credit.

The Bank does not provide material credit facilities to its customers.

The Bank manages credit risk by establishing individual counterparty limits with which it undertakes business within the terms of Bank's Business Risk and Risk Appetite policies.

Quantitative Disclosure

The Bank adopts the Simplified Method of calculating risk weight under Standardised Credit Risk which is considered to be the most appropriate for its business given the nature and size of its activity.

Standardised Approach – credit risk exposure as at 31 December 2022

Asset classes (GBP '000)	On-balance sheet amount	Off-balance sheet amount	RWAs
Exposures to central governments or central banks	2,289	0	0
Exposures to regional governments or local authorities	10	0	2
Exposures to institutions	11,725	0	3,488
Exposures to corporates	1,151	0	1,151
Exposures to retail	13	0	10
Other items	511	0	424
Total	15,699	0	5,075

Standardised Approach – exposures by asset classes and risk weights as at 31 December 2022

Asset classes (GBP '000)	Assets split by the risk weight to be applied to them						
	0%	20%	50%	75%	100%	Total	RWAs
Exposures to central governments or central banks	2,289					2,289	0
Exposures to regional governments or local authorities		10				10	2
Exposures to institutions		7,915	3,810			11,725	3,488
Exposures to corporates					1,151	1,151	1,151
Exposures to retail				13		13	10
Other items	87				424	511	424
Total	2,376	7,925	3,810	13	1,575	15,699	5,075

Geographic distribution by Exposure Class

The table below shows the Bank's geographic concentration risk as at 31 December 2022:

(GBP '000)	UK	Europe	Philippines	Total
Exposures to central governments or central banks	2,289			2,289
Exposures to regional governments or local authorities	10			10
Exposures to institutions	11,308	417		11,725
Exposures to corporates	45	1	1,105	1,151
Exposures to retail	13			13
Other items	511			511
Total	14,176	418	1,105	15,699

Exposures to Institutions by geographic distribution and risk weights

Considered the main credit risk, the Bank's exposure to financial institutions and counterparty correspondent banks broken down by geographical location and risk weights associated with each credit quality step as at 31 December 2022 are as follows:

(GBP '000)	Credit Quality Step	Exposures	RWAs
United Kingdom	2	11,308	3,405
Europe	2	155	31
	unrated	262	52
Philippines (group banks)	3	1,105	1,105
Totals		12,830	4,593

Ratings based on Moody's and Fitch.

MARKET RISK

Market risk is the risk that changes in interest rate, foreign exchange rates, or other prices and volatilities will have an adverse effect on the Bank's financial condition or results.

Foreign Exchange Risk

The Bank does not actively trade in foreign currency on its own account but maintains working balances with its correspondent banks to facilitate its remittance business and the foreign currency assets and liabilities are presented in the note to the 2022 Annual Report and Financial Statements. The Bank does not enter into forward or other foreign exchange instruments.

Senior management is responsible for the management of market risk.

Liquidity Risk

The principal objective is to ensure that at all times there are sufficient liquid assets to satisfy the Bank's payment obligations and potential obligations to the depositors, together with other business liabilities, as they fall due, without incurring unacceptable shortfalls.

Under the PRA's liquidity rules, the Bank is regarded as a stand-alone entity and prepares an Individual Liquidity Adequacy Assessment Process ("ILAAP") annually to determine the amount of liquidity resources required. A buffer of highly liquid government securities is held to mitigate the Bank's liquidity risk.

Liquidity risk is monitored daily to ensure it remains within the FCA/PRA guidelines and the Bank's own limits.

Senior management is responsible for the management of liquidity risk.

OPERATIONAL RISK

Definition and source of risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, employees and IT systems, or from external events, including outsourcing and legal risks, but excluding strategic and reputational risk. It is a pervasive risk that involves all aspects of the business as well as other people with whom the Bank deals. When such risks materialise, they have not only an immediate financial consequence for the Bank but also an effect on its business objectives, customer services and regulatory responsibilities.

Operational risk is one of the principal risks in the overall Risk Management Framework. There are many major types of operational risks faced by the Bank, including internal fraud, external fraud, clients, products, business practice, execution, delivery and process management, employment system and workplace safety, damage to physical assets, and IT events.

Risk management and monitoring

As operational risk is inherent in the Bank's processes, the objective of operational risk management is not to remove operational risk altogether but to manage and control operational risk in a cost-effective manner consistent with the Bank's risk appetite. In achieving this we:

- Seek to minimise the impact of losses suffered in the normal course of business (expected losses) and avoid or reduce the likelihood of suffering a large extreme (or unexpected) loss; and

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- Seek to improve the effective management of operations and thus strengthen the Bank's reputation.

The Bank's operational risk management framework consists of the following key components:

- Identification and categorisation of the key operational risks faced by the business areas, including defining risk appetites;
- Risk assessments, including financial and non-financial impact assessment for each of the key risks to which the business is exposed;
- Control assessments, evaluating the effectiveness of the control framework covering each of the key risks to which the business is exposed;
- Loss and incidental management;
- The development of Key Risk Indicators for management;
- Scenarios for estimation potential loss exposures for material risks;
- Purchases of insurance to mitigate certain operational risk events.

Under the Basel II rules, the Bank has adopted the Basic Indicator Approach to operational risk; therefore, the Bank's operational risk capital requirement ("ORCR") is equal to 15% of the three-year average of the sum of the Bank's net interest income; and the Bank's net non-interest income. The Bank's operational risk charge at 31 December 2022 was GBP 236.3k.

OTHER RISKS

- **Business Risk** - The business income source is dependent on one product (remittances) which is subject to competitive pricing it being noted that remitters have strong connections to only one geographical location (Philippines).
- **Reputational Risk** – This is a key area of risks for banks. The Bank ensures compliance with regulatory rules through a strong compliance culture and seeks to minimise complaints by providing its customers with high level of service. Particular attention is paid to anti-money laundering requirements with comprehensive "Customer Due Diligence" requirements and screening of payments passing through the Bank to minimise the risks of handling the proceeds of crime and dealing with sanctioned parties.
- **Litigation Risk** – The Bank takes care to avoid disputes by ensuring that all documentation comprehensively covers the risks involved. Where appropriate, it seeks specialist legal advice. Systems and procedures are reviewed regularly to safeguard the Bank against any legal or regulatory lapses.
- **Professional Conduct Risk** – The Bank is aware of the risks it faces from the improper professional conduct of its employees. The Conduct of Business Policy as well as other relevant Bank policies detail the measure in place to protect the Bank from risks arising

from bribery, gifts and hospitality, conflicts of interests and market abuse. The staff are required to certify, at least annually, that they agree to adhere to the letter and the spirit of the policy

- Pension Liability Risk – The Bank operated a defined pension benefit scheme whose assets are independent of the Bank’s finances. From 01 March 2005, the directors have closed the defined benefit scheme to future accrual. Rights earned by members up to that date have been preserved and are defined for each member by their salary on that date. A full actuarial valuation was carried out on 01 October 2019 on the defined benefit scheme and has been updated by the actuary on an FRS 102 basis as at 31 December 2022. The amount of recognized net defined benefit liability of the scheme in said FRS 102 report was a surplus of GBP 2.0m.

REMUNERATION

The Bank has no Remuneration Committee and remuneration arrangements such as bonus are reviewed and determined by the Board of Directors.

The Bank does not provide incentives or compensation schemes to reward Staff for performance. The Bank provides all permanent employees with a non-contributory pension scheme based on salary.

The aggregate quantitative data on remuneration for those members of staff in employment at the end of 2022 whose professional activities are considered to have a material impact on the bank’s risk profile and all members of the senior management (Code Staff = 3) are provided below:

Total remuneration in 2022 (All forms of payments or benefits)	GBP 139k
Number of identified Code Staff	3
Total fixed remuneration in 2022 (Salaries & other fixed benefits including pension contributions)	GBP 139k