Philippine National Bank (Europe) Plc

Pillar 3 Disclosures

31 December 2015

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OVERVIEW

Background

Philippine National Bank (Europe) Plc ("the Bank") is a UK-registered bank authorized by the Prudential Regulation Authority ("PRA") and regulated by the Financial Conduct Authority ("FCA"). It is wholly owned subsidiary of Philippine National Bank (Manila). This disclosure document should be read in conjunction with the Bank's Annual Report and Financial Statements for the year ended 31 December 2015.

Market discipline is one of the key objectives of the Basel Committee on Bank Supervision ("BCBS") and its provisions adopted throughout the European Union ("EU") under the European Union Capital Requirements Directives ("the Directive") which came into force on 1 January 2007. The Directive was implemented in the UK by rules introduced by the Financial Services Authority ("the FSA"). The Basel 2 Framework is structured around three Pillars: Pillar 1 (minimum capital requirement), Pillar 2 (supervisor review) and Pillar 3 (market discipline). The disclosure requirements of Pillar 3 are designed to promote market discipline by providing market participants with key information on a firm's risk exposure and risk management processes.

The Bank has adopted the Standardised Approach to credit risk, the Basic Indicator Approach ("BIA") to operational risk and the standard approach to market risk under Pillar 1. The Bank also became subject to Pillars 2 and 3 from 2008

Basis and Frequency of Disclosures

This disclosure document has been prepared by the Bank in accordance with the requirements of Pillar 3 as set out in Chapter 11 of BIPRU sourcebook to comply with the applicable articles of the Banking Consolidation Directive ("BCD") and the Capital Adequacy Directive ("CAD") of the EU.

These Pillar 3 disclosures have been prepared purely for explaining the basis on which the Bank has prepared and discloses certain capital requirements and information about the management of certain risks and for no other purpose. They do not constitute any form of financial statement and must not be relied upon in making any judgment on the Bank.

This report is produced on an annual basis and published as soon as practicable after the publication of the Bank's Annual Report and Financial Statements.

Scope

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

Location and Verification

This document has been reviewed by the Board of Directors and approved on 19 April 2016 and is published on the website: http://www.pillar3.eu

RISK MANAGEMENT OBJECTIVES AND POLICIES

Background

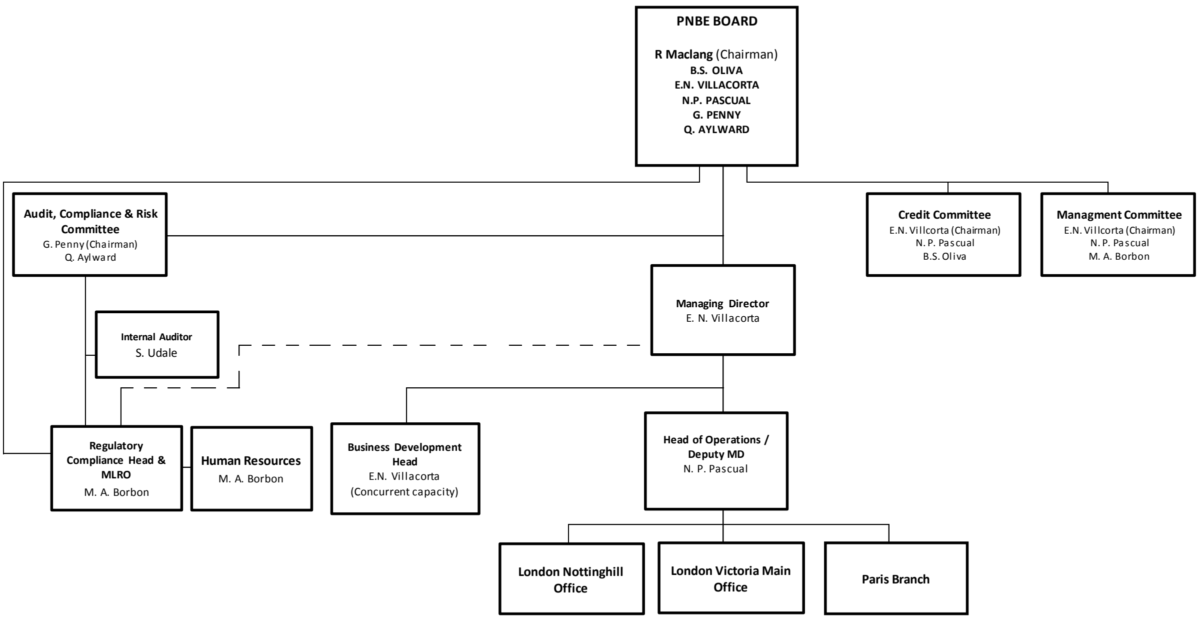
The Bank is a wholly owned subsidiary of Philippine National Bank (Manila). It was formed and registered in England and Wales (2939223) in June 1994.

Its principal activity is the provision of banking and payments services primarily to Filipino customers in the United Kingdom, France through its Paris branch as well as other European countries where the Bank has cross-border passport licences.

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.

Philippine National Bank (Europe) Plc
Organization Chart



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 six 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 as member. The Internal Auditor acts as a secretary to the Committee. Senior Management to include the Managing Director, the Deputy Managing Director and the Compliance Officer are invited to attend all 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. The Committee utilises the Internal Audit function to provide assurance in this respect.

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 includes, this Committee comprises the other members of the senior management to include the heads of Operations, Business Development 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 Executive Director who is representing the Parent bank as members. 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.

CAPITAL RESOURCES

Total Capital Available

Throughout 2015, the Bank complied fully with the Capital Requirements set out in the Financial Services Handbook. On 31 December 2015, all of the Bank's capital was comprised as follows:

Composition of Capital (GBP)	
Share capital	10,914,000
Profit and loss reserve	(6,485,000)
Merger reserve	6,768,000
Total Capital	11,197,000

Tier 1 capital comprises ordinary share capital plus reserves. The Bank does not hold any Tier 2 or Tier 3 capital.

CAPITAL ADEQUACY

As referred to in Section 1, the Bank, in order to calculate the Basel Pillar 1 capital requirement, has since January 2008 adopted the Standardised Approach to credit risk, the Basic Indicator Approach to operational risk and the standard approach to market risk.

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 team 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. Prior to the approval by the PRA and FCA of the merger between Bank and Allied Bank Philippines (UK) Plc which was implemented in April 2014, the Bank had submitted to the PRA its proposed ICAAP based on post-merger scenario. The PRA had accordingly approved this ICAAP and set the Individual Capital Guidance ("ICG") for the merged Bank to which has adhered ever since.

Minimum Capital Requirements (GBP)	
Pillar 1 capital requirement	
- Basic CRR charge (8% of risk weighted assets)	546,339
- Operational risk charge	300,950
- Market risk charge (foreign currency PRR)	38,177
Total Pillar 1 capital requirement	**885,466**
Individual Capital Guidance	
157% of Pillar 1 capital requirement per (a)	1,390,182
Base capital requirement (€5m) (b)	3,682,970
Capital planning buffer (CPB) requirement	1,725,000
Minimum capital requirement (higher of (a) or (b) plus CPB	**5,407,970**
Total capital resources	**11,197,000**
Headroom over minimum Pillar 1 capital requirement	**5,789,030**

It is the Bank's policy to maintain a degree of headroom above the minimum required capital level.

The breakdown of the basic capital charge by exposure class of assets for 31 December 2015

Breakdown of Exposures by exposure class (GBP)		
Exposure class	**Risk-weighted assets**	**Basic CRR charge (8%)**
Central Government of central banks	0	0
Institutions	6,044,430	483,554
Corporate	135,450	10,836
Retail	172,165	13,773
Other Items	477,196	38,176
Total	6,829,241	546,339

SOURCES OF RISK

Credit Risk

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.

Standardised Credit Risk

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.

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 are as follows:

Breakdown of credit exposures to Institutions by geographical location, credit quality step and risk weights			
Country	Credit Quality Step	Total Exposure (GBP)	8% of Risk Weighted Exposure (GBP)
United Kingdom	1	2,696,761	43,148
	2	7,579,133	121,266
	3	3,897,164	155,887
Europe	1	213,407	3,415
	3	90,970	3,639
	Unrated	29,022	1,161
Philippines (group banks)	3	3,875,984	155,039
Totals	**-**	**18,382,441**	**483,554**

Ratings based on Moody's

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 detailed on page 26 of the 2015 Annual Report and Financial Statements. The Bank does not enter into forward or other foreign exchange instruments.

The Bank's foreign exchange position risk requirement is a follows:

Own funds requirements (GBP)	Total risk exposure amount
38,177	477,216

The Bank's exchange exposures are as follows:

Foreign Exchange Exposure (amount in GBP)	
Currency	**Exposure**
EUR	(292,842)*
USD	74,731
CHF	3,581
PHP	398,904

* Short position

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 ("ILAA") 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 legal risk, 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 immediate financial consequences 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
- 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 2015 was GBP 300,950.

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).

Other Risks

- 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 "Know Your Customer" requirements and screening of payments passing through the Bank to minimise the risk of handling 'suspicious' money.

- 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 if 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.

- 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 2013 on the defined benefit scheme and has been updated by the actuary on an FRS 102 basis as at 31 December 2015. The amount of recognized pension plan liability in said FRS 102 report was GBP 252,000.

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 other than the statutory 13th month pay given to the staff of Paris Branch which is equivalent to one month salary. 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 2015 and whose professional activities are considered to have a material impact on the bank's risk profile (Code Staff = 5) are provided below:

Total remuneration in 2015 (All forms of payments or benefits)	GBP 204,494
Number of identified Code Staff	5
Total fixed remuneration in 2015 (Salaries & other fixed benefits including pension contributions)	GBP 204, 494

Details of directors' remuneration are provided on page 22 of the 2015 Annual Report and Financial Statements.