

	under the Merged Bank.	
Trust Committee	Push of the Wealth Management Program of Trust Banking Group through Estate Planning targeting the retirees of the LT Group of Companies	
Board Oversight Committee – Domestic & Foreign Subsidiaries and Affiliates	<p>Expanded review & monitoring of monthly performance of oversea and domestic offices. Approved new strategic programs to further strengthen its operations to achieve long-term profitable operations via:</p> <ul style="list-style-type: none"> - New marketing programs, tools & strategies to sell PNB products & services supported by aggressive advertising. - Retention programs were approved to win back lost clients and deepen relationship with existing valued customers. - New distribution channels for remittances through new technology i.e. web-based. 	Rolled-out revenue generating programs and effectively reduced overhead expenses to achieve desired rate of return.
Board Oversight RPT Committee	<ol style="list-style-type: none"> 1. Enhance existing RPT policy manual to align with the new regulatory issuances. 2. Ensures proper monitoring of RPTs and such RPT dealings are approved by the Board through BORC per Board approved policy guidelines. 3. Conduct training and increase awareness of RPT policies and procedures of bank employees. 4. Conduct regular monthly meetings or as necessary to review, approve and endorse RPT proposals to the Board for final approval. 	<p>Bank has fully adhered with the SEC/BSP/PSE regulations and enhanced practices to align with global best practices.</p> <p>Established a robust RPT framework and modified/codified existing policies to provide clearer RPT policy guidelines based on regulatory requirements.</p> <p>Officers attended trainings on RPT Policy Guidelines conducted by BSP thru Baiphil to increase awareness on RPT policy guidelines.</p> <p>Bank's RPT dealings are reviewed/approved/noted by BORC and endorsed to Board for final approval per existing RPT policy guidelines.</p>

F. RISK MANAGEMENT SYSTEM

1) Disclose the following:

(a) Overall risk management philosophy of the Bank: (updated – October 2016)

The Board and its Risk Oversight Committee operate as the highest level of PNB's risk governance. Risk governance is undertaken by a structured hierarchy of committees (both at board level and at the executive / management level) each with specified accountabilities. The continuous flow of information between the board and board-level committees and the corresponding management committees; allow for consistent evaluation of the risks inherent in the business, raise the alarms, if any, and manage the business effectively with strong adherence to process management guidelines and controls.

Strong independent oversight has been established at all levels within the group. The Bank subscribes to the philosophy of integrity, accountability and transparency in its manner of doing business, dealing fairly with its clients, investors, stockholders, the communities affected by its activities and various public; professionalism among its Board of Directors, executives and employees in managing the Bank, its subsidiaries and affiliates; and respect for the laws and regulations of the countries affecting its businesses.

Members of the senior management team play a pivotal role in the day-to-day running of the bank. Executive officers are assigned to various management committees that provide the leadership and execution of the vision and policies approved by the bank's board of directors. The bank's business objectives are driven for most part by the day-to-day directions decided by these management committees with approvals and notation by the various board level committees as follows (see Figure 1):



Figure 1: Board & Management Committees

The risk management framework of the Bank is under the direct oversight of the Chief Risk Officer (CRO) who is directly reporting to the Risk Oversight Committee. The CRO is supported by Division Heads with specialized risk management functions to ensure that a robust organization is maintained. The Risk Management Group is independent from the business lines and organized into the following divisions: Credit Risk Division, BASEL and ICAAP Implementation Division, Market & ALM Division, Operational Risk Division, Information Security / Technology Risk Management, Trust and Fiduciary Risk Division and Business Intelligence & Warehouse Division.

- (b) A statement that the directors have reviewed the effectiveness of the risk management system and commenting on the adequacy thereof: (updated – October 2016)

The risk management system and the directors’ criteria for assessing its effectiveness are revisited on an annual basis and limit settings are discussed with the Business Units and presented to the Risk Oversight Committee for endorsement for final Board Approval.

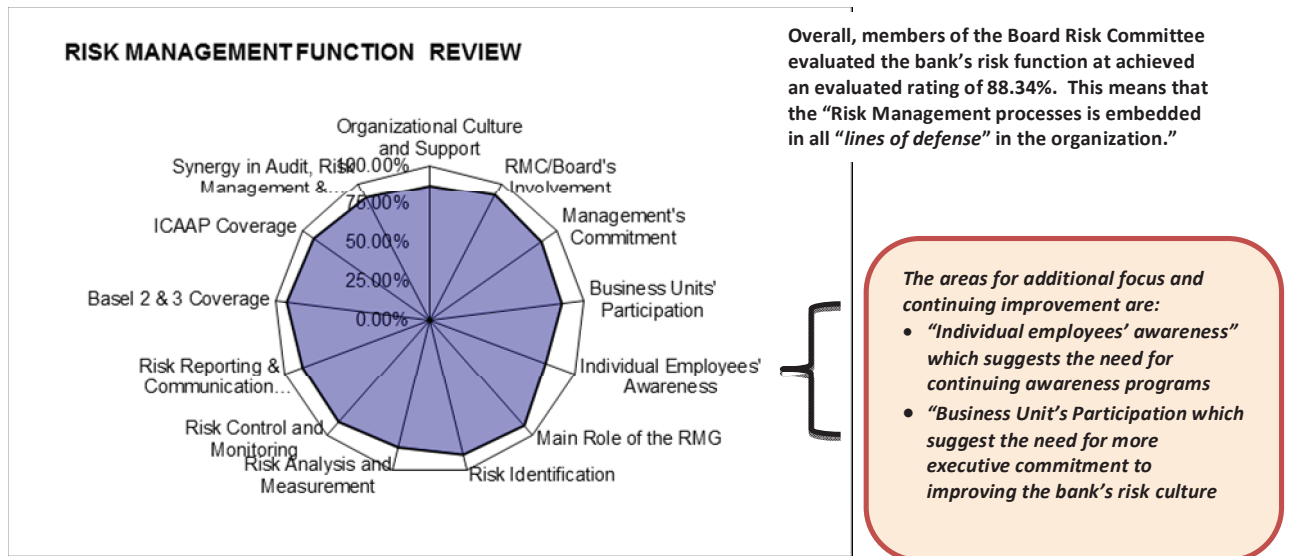


Figure 1: 2016 Overall Assessment of the Risk Management Function

Regular review and assessment of the Enterprise Risk Management Function is completed by both the senior management team (including 1-downs) and the Risk Oversight Committee members. The above evaluation refers to the review by the members of the Risk Oversight Committee.

- (c) Period covered by the review;
One year.
- (d) How often the risk management system is reviewed and the directors’ criteria for assessing its effectiveness?
Annually.

Summary of RM Function Evaluation - 2015		
	Score	Assessment
Organizational Culture and Support	87.05%	Effective RM process in place
RMC/Board's Involvement	90.34%	Effective RM process in place
Management's Commitment	87.50%	Effective RM process in place
Business Units' Participation	85.80%	Effective RM process in place
Individual Employees' Awareness	79.83%	Effective RM process in place
Main Role of the RMG	91.89%	Very Effective RM process in place
Risk Identification	90.08%	Effective RM process in place
Risk Analysis and Measurement	85.32%	Effective RM process in place
Risk Control and Monitoring	88.89%	Effective RM process in place
Risk Reporting & Communication (internal&external)	87.86%	Effective RM process in place
Basel 2 & 3 Coverage	93.14%	Very Effective RM process in place
ICAAP Coverage	91.23%	Very Effective RM process in place
Synergy in Audit, Risk Management & Compliance	88.49%	Effective RM process in place
Average Rating	88.34%	Effective RM process in place

Figure 2: Summary of RM Function Evaluation

- (e) Where no review was conducted during the year, an explanation why not.
- (e)
- (e) Not Applicable.
- 2) (e) Risk Policy
- (e)
- (a) Company
- (e)
- (e) Give a general description of the company's risk management policy, setting out and assessing the risk/s covered by the system (ranked according to priority), along with the objective behind the policy for each kind of risk:
- (e)
- (e) The following are the basic principles that the Bank must adhere to in conducting its business, with the objective of minimizing risks and optimizing return on capital:
- (e)
- (e) • First, the Board of directors and its delegated committees have the responsibility of managing the Bank's overall strategies and objectives.
 - (e) • Second, the Bank works on the basis that risk taking decisions should always be made by a committee consisting of at least three persons, and not by one person alone regardless of position.
 - (e) • Third, the Bank has policies and procedures in place to guide line management in actually originating, approving and managing these risks.
 - (e) • Fourth, the Board Risk Oversight Committee is designated by the PNB Board of Directors to assist the Board to oversee the risk profile and the development/maintenance of the risk management framework of PNB and its related allied subsidiaries and affiliates. It is mandated to set risk appetite, approve frameworks, policies and processes for managing risk, and accept risks beyond the approval discretion provided to management.
 - (e) • Final Approval of the Bank's overall risk framework is accomplished by the Board of Directors en banc.
- (e)
- (a) Group
- (e)
- (e) Give a general description of the Group's risk management policy, setting out and assessing the risk/s covered by the system (ranked according to priority), along with the objective behind the policy for each kind of risk:
- (e)
- (e)
- (e)
- (e)
- (e)
- (e)

Risk Exposure	Risk Management Policy	Objective
Enterprise Risk Management (ERM) Framework	ERM Policy Document	To formalize the Bank's ERM Framework and to articulate the roles and responsibilities of the Board of Directors, management and employees, and relevant committees accordingly. It is intended that this framework will provide the overall guidance in the Risk Management functions of <u>identification, measurement, analysis, monitoring and control of risks</u> .
Market Risk	Market Risk Management Manual	The Market Risk Manual covers subsidiaries and affiliate with market risk exposure. This include Value At Risk (VaR) Monitoring and setting of VaR Limits.
Liquidity Risk	Liquidity Risk Management Manual	The Liquidity Risk Management Manual covers subsidiaries and affiliate with funding liquidity risk exposure. This would include monitoring of liquidity gaps and the setting of cumulative liquidity gap limit up to one year.
Interest Rate Risk	Interest Rate Risk in the Banking Book	The Interest Rate Risk Management Manual covers subsidiaries and affiliate with exposure in net interest income arising from mismatch of repriceable assets and repriceable liabilities. This would include the monitoring of repricing gap and the setting of the Earnings at Risk Limit for the repricing gap per tenor bucket.
Market Risk Price Risk in the Trading Portfolio	<p>The Bank's trading positions are sensitive to changes in the market prices and rates. PNB is subject to trading market risk in its position taking activities for the fixed income, foreign exchange and equities markets.</p> <p>The Bank also employs the stop loss monitoring tool to monitor the exposure in the price risks. Stop loss limits are set up to prevent actual losses resulting from mark to market. To complement the VAR measure, the Bank performs stress testing and scenario analysis wherein the trading portfolios are valued under several market scenarios.</p>	<p>To calculate the risks in the trading portfolio, the Bank employs the Value at Risk (VAR) methodology with 99% confidence level and one holding period (equities and FX VAR) to ten day holding period for fixed income VAR.</p> <p>VAR limits have been established annually and exposures against the VAR limits are monitored on a daily basis. The VAR figures are back tested against actual (interest rates) and hypothetical profit and loss (FX and Equities) to validate the robustness of the VAR mode.</p>
Structural Market Risk	Structural interest rate risk arises from mismatches in the interest profile of the Bank's assets and liabilities. Limits have been set on the tolerable level of earnings at risk. Compliance to the limit is monitored regularly.	To monitor the structural interest rate risk, the Bank uses a re-pricing gap report wherein the repricing characteristics of its balance sheet positions are analyzed to come up with a repricing gap per tenor bucket. The total repricing gap covering the one-year period is multiplied by assumed change in interest rates based on observed volatility at 99% confidence level to obtain an approximation of the change in net interest earnings.
Liquidity and Funding Risk	The Bank seeks to manage its liquidity through active management of liabilities, regular analysis of the availability of liquid asset portfolio as well as regular testing of availability of money market lines and repurchase facilities aimed to address any unexpected liquidity situations.	The tools used for monitoring liquidity include gap analysis of maturities of relevant assets and liabilities reflected in the maximum cumulative outflow (MCO) report, as well as an analysis of sufficiency of liquid assets over deposit liabilities and regular monitoring of concentration risks in deposits by tracking accounts with large balances. The MCO focuses on a 12-month period wherein the 12-month cumulative outflow is compared to the acceptable MCO limit set by the Bank.
Credit Risk	All credit risk policies issued by the regulatory bodies (BSP, SEC, PDIC, BIR, etc.) automatically form part of the Bank's board-approved risk policies. These risk policies	The Bank's credit risk weighted assets are continuously monitored to ensure that the exposures are kept within limits (both internal and external).

	<p>reflect the Bank's lending profile and focus on:</p> <ul style="list-style-type: none"> a) the risk tolerance and/or risk appetite; b) the required return on asset that the Bank expects to achieve; c) the adequacy of capital for credit risk. 	<p>Adherence to regulatory policies and requirements are also prioritized with a view to protecting Bank assets as well as servicing client's requirements</p>
Operational Risk		
<p>People Risk</p>	<p>HR Policies are defined to encompass all related personnel factors such as: hiring, training, compensation and benefits, performance management – to ensure the readiness of all bank personnel to perform the functions as designated.</p>	<ul style="list-style-type: none"> a) Hiring: Continuous partnership between the HR Group and the lines of business and support units exist to ensure that the final accountability for hiring of personnel lies in the unit where each candidate is to be assigned. A thorough background check on each candidate is also accomplished to ensure this conforms with the bank's level of standards b) Training: each personnel is required to attend a specified number of hours on training (both internal and external. Training Workshops may also be conducted within the specific lines of business as the executive in charge sees fit. Specialized training is also given due focus where needed. c) Compensation & Benefits (C&B): A regular review of the Bank's overall C&B policies is accomplished with the assistance of 3rd party subject matter experts to ensure that the Bank's benefits program is in line with the Board approved policies. d) Performance Management: A uniform standard of performance appraisal is applied to all personnel of the Bank based on an annual review of each employee's objectives. These objectives are reviewed by the seniors in charge to ensure that these are in line with the Bank's overall strategic and revenue and expense objectives. <p>Annual evaluation and the implementation of balanced scorecards are used to ensure that ill-fitted personnel are either re-trained, re-tooled and re-skilled to equip them better.</p>
<p>Process Risk</p>	<p>Operational Policies and Procedures follow a formal process of approval via the Operations Committee. The OPCOM is a management level committee to ensure that most processes are designed with audited fail-safes and checking procedures.</p>	<p>The overall foundation of the formalized operational policies and procedures stems from a strict separation of functions by the revenue generating side and the implementation and systems side of the Bank.</p> <p>The Internal Audit Group, as well as the various officers tasked with the review function, regularly monitors the implementation of these documented policies and procedures.</p>
<p>Business Strategy Risk</p>	<p>Annual Strategic Planning Exercise is accomplished to document the bank's objectives for a minimum of 3 years. A quarterly review of the bank's profitability is accomplished accordingly</p>	<p>Strategic Risk can arise when the direction/strategy of the bank can lead to non-achievement of business targets. This results in a new focus of a business sector without consolidating this with the bank's overall business plan and strategy.</p> <p>At PNB, strategic risk is managed through each business sector performing "actuals vs targets" sessions with and report to the Board of Directors through regular Management Profitability Reporting Sessions. In addition, the coordination between business sectors are done through regular meetings by the Senior Management Team to ensure that overall business targets are continually revisited.</p>
<p>Business Environment Risk</p>	<p>Product Management Framework New Product Roll outs go through a rigorous process where elements such as:</p>	<p>Product Management Business Framework where old and new products alike are monitored by assigned product managers who are fully involved and</p>

	competition, regulations, legal, client acceptability, profitability – are taken into account.	engaged in coordinating with the various business sector heads in achieving the bank's business plan. Further, a Product Committee composed of senior managers has been convened and meets regularly to ensure that business environment is closely monitored as to competition; delivery channels and over all service levels are kept at acceptable levels.
Information Technology Risk	Information Technology Strategic Plan is formulated in line with the overall bank's business plan. This is formalized via the approval channel – Board IT Governance Committee and Board of Directors. Enterprise Project Management (EPMF) Framework for technology driven Projects where both the business, technology and support groups are involved	The Bank has institutionalized and implemented the board-level IT Governance Committee which is composed of members of the senior management team, who discuss the monthly ITG. Further, the Bank has formalized the Project Implementation Process (through the EPMF for defined systems implementation to include among others the creation of a PROJECT STEERING COMMITTEE to oversee the project's progress and to ensure that the project's objectives are achieved.
Information Security Risk	Enterprise Information Security Policies, the cornerstone of the Bank's information security management system, is a component of an effective Corporate Governance. This communicates Management's directives and support for PNB's information security programs and strategies. The high level security policies stated herein are based on International Organization for Standardization (ISO) 27000 series of internationally-accepted information security and risk management standards, related laws and regulations.	Adoption of globally accepted ISMS (Information Security Management System – in compliance with BSP Circulars and ISO mandated functions) – is continuously reviewed and revised as necessary to ensure that the bank's information assets are duly protected and that the risk of theft, leakage and fraud are minimized, and/or eliminated.
Business Continuity Risk	Business Continuity Program – administered throughout the organization where each business unit formulates individual BCP.	a) Call Tree Program (a component of the BCP) is administered throughout organization to ensure that each personnel stays connected when an emergency situation arises from natural and man-made disasters b) Business Impact Analysis – is accomplished on a regular basis to provide a central forum of prioritizing services whenever an emergency situation arises c) BCP Technical Tests are done on an annual basis to determine readiness of the bank's applications and system for continued delivery of prioritized services

Note: The Bank applies the same risk management policy for both the Bank and its subsidiaries and affiliates as a Group.

(c) Minority Shareholders

Indicate the principal risk of the exercise of controlling shareholders' voting power.

Risk to Minority Shareholders
Stockholders holding or representing at least two thirds (2/3) of the outstanding capital stock of the corporation may control the vote for matters such as the amendment of articles of incorporation, removal of directors, shorten or extend corporate term, increase or decrease capital, sale or other disposition of assets, invest corporate funds in another corporation or business or for any other purpose, declaration of dividends, merger or consolidation, voluntary dissolution, etc.

3) Control System Set Up

(a) Company

Briefly describe the control systems set up to assess, manage and control the main issue/s faced by the company: