PILLAR 3
DISCLOSURES

31st DECEMBER 2024

Lidion Bank

RISK MANAGEMENT AND CONTROL

Overview of risk disclosures

These disclosures have been prepared in accordance with Article 6, paragraph 3 of the CRR No.575/2013 on a consolidated basis for the group of companies comprising Lidion Bank plc and its parent company Lidion Holdings plc (collectively, the Group). The Pillar 3 quantitative and qualitative disclosure requirements are governed by Banking Rule 07: Publication of Annual Report and Audited Financial Statements of Credit Institutions authorised under the Banking Act (Cap. 371) issued by the Malta Financial Services Authority. These disclosures will be published by the Group on an annual basis as a standalone document.

As per banking regulations, this report is not subject to an external audit, except to the extent that any disclosures are equivalent to those made in the financial statements which adhere to International Financial Reporting Standards (IFRS) as adopted by the EU. The Bank is satisfied that internal verification procedures ensure that these additional regulatory disclosures are presented fairly. These disclosures are also subject to a review by the Bank's external auditors.

Risk management and control principles

Managing and controlling risk is fundamental to the Bank's risk and control principles. During operations, the Bank's risk management and control approach is grounded in five key principles:

- Business management across the Bank holds accountability for all the risks assumed or incurred by their business operations and is responsible for actively managing risk exposures to ensure a balance between risk and return;
- An independent control process is an integral part of the Bank's structure. The aim is to provide an objective check on risk-taking activities and to support senior management in achieving appropriate alignment of the interests of all stakeholders including shareholders, clients and employees;
- Comprehensive, transparent and objective risk disclosure to senior management, committees of Bank, the Board of Directors (BoD), shareholders, regulators, and other stakeholders is an essential component of the risk control process;
- Earnings protection is based on limiting the scope for adverse variations in earnings and exposure to stress events. Controls are applied at the level of individual exposures and portfolios in each business and to risk in aggregate, across all businesses and major risk types, relative to the Bank's risk capacity. This capacity refers to the level of risk the Bank is capable of absorbing, based on its expected earnings power; and
- Protection of the Bank's reputation ultimately depends on the effective management and control of the risks incurred in the course of business.

The principles are the foundation upon which the more detailed risk management and control frameworks are built. These frameworks encompass qualitative elements, such as policies and authorities, as well as quantitative components including limits. They undergo continual adaptation and refinement to align with the evolving landscape of the Bank's business and the market environment.

Risk Statement

The Bank operates a diversified business model structured around three principal business lines: Lending, Factoring, and Corporate Banking. These services are designed to cater to the operational needs of various corporate clients, including those in growing sectors such as digital advertising. The Bank also offers a range of deposit and cash management solutions, further strengthening its position as a core banking partner for businesses.

In the short term, the Bank's strategic objective is to deepen its engagement with its existing customer base and leverage established relationships to grow its business. Over the medium to long term, the Bank intends to scale its operations across all three key business lines, with a focused effort on expanding its factoring portfolio, particularly within the digital advertising industry. This growth strategy is deliberately structured to align with the Bank's conservative risk culture and long-term sustainability.

The Bank maintains a comprehensive and prudently managed risk profile. The primary risks faced by the Bank include credit risk, concentration risk, operational risk, liquidity and funding risk, and solvency risk. The Bank also closely monitors other relevant risk categories, such as settlement risk, interest rate risk in the banking book, financial crime compliance risk, cyber risk, and business continuity risk. These risks are assessed through a comprehensive internal risk framework supported by detailed policies, regular reviews, and risk-specific controls.

The Bank's risk governance model reflects a strong risk culture embedded at all levels of the organization. Risk awareness is actively promoted through training, and personnel from the second line role are members of all key management committees or are actively requested to participate during the respective committee meetings. Staff across departments are encouraged to participate in risk identification and escalation processes, fostering shared accountability and responsiveness to emerging risks.

The Bank's Risk Appetite Framework and Risk Register which also includes tolerance levels, as approved by the Management Body, establishes a conservative stance across all material risk types. Investments in IT security, risk management systems, specialized personnel, and third-party expertise are prioritized to mitigate financial crime and cybersecurity risks. The Risk Appetite Framework supports strategic alignment by actively excluding business opportunities in sectors that fall outside acceptable risk parameters, including industries with high environmental impact or ethical concerns. Risk appetite is articulated through qualitative statements and quantitative metrics, including Key Risk Indicators (KRIs), which are monitored on an ongoing basis. These limits are reviewed periodically and adjusted as needed based on emerging risks or shifts in strategy. Escalation protocols are in place to address breaches or early warning signs.

The Bank's credit risk profile reflects its current business model and strategic focus. Lending activities span immovable property financing, working capital financing, renewable energy project financing, and asset financing. Credit exposures are managed within conservative internal thresholds, and subject to regulatory large exposure limits. While this may limit the Bank's ability to serve certain high-volume clients, it supports the Bank's commitment to financial soundness and risk discipline.

The Bank's risk governance and organisational arrangements are detailed in relevant sections of this report. These include the roles of the Board, management committees, and key officers responsible for risk oversight.

The Bank utilizes a formal risk management framework supported by dashboards and technology platforms. A structured risk identification and escalation process ensures timely and consistent treatment of risks across all areas of the business.

The Risk Management Function fosters a strong collaboration and a structured relationship with both Internal Audit and Legal and Compliance. The Internal Audit Function uses the Bank's risk register as a primary input for developing audit plans, ensuring a risk-based approach. Discussions between the Head of Risk and Internal Audit help align views on the risk landscape. Audit cycles are proposed and approved via the Audit Committee, with Internal Audit reporting back on findings and follow-up actions.

Legal and Compliance, Risk, and Financial Crime Compliance functions engage regularly, sharing responsibilities in areas such as regulatory impact assessments, ESG due diligence, and risk model development. This collaboration ensures that financial crime frameworks and ESG initiatives align with both compliance obligations and risk tolerance. Dual assessments by the Compliance and Risk Management Functions are applied to outsourcing, insurance, and customer onboarding procedures.

Risk reporting is conducted monthly to management and the Risk Committee, with key metrics also escalated to the Board. The Bank uses real-time systems such as SIEM and SOC for cyber and IT-related incidents. These tools feed into the Bank's incident management response framework.

Risk is systematically integrated into strategic decision-making. All new product proposals are reviewed by the Risk Management Function as part of the product approval process. Strategic and emerging risks are monitored and reported to the Risk Committee on an ongoing basis, ensuring alignment between long-term planning and the Bank's risk profile.

The adequacy of the Bank's risk management arrangements is supported by a comprehensive governance structure that includes oversight from the Board and various Board and Management Committees. These bodies ensure that risk management practices are consistent with the Bank's risk profile, business strategy, and regulatory obligations. The Bank employs an integrated approach to risk oversight, leveraging systems, personnel, and processes that ensure ongoing risk identification, assessment, and mitigation.

Key risk metrics, including capital adequacy ratios, liquidity coverage ratios, and other regulatory indicators, are disclosed in accompanying sections of this document. These figures provide transparency into the Bank's risk posture and affirm its adherence to prudential standards.

Risk management and control responsibilities

The Board of Directors has a strategic and supervisory function. It is responsible for the Bank's fundamental approach to risk, for approving the risk principles and for determining risk capacity and risk appetite. The Board recognizes that, for matters pertaining to the managing, monitoring and mitigating of risks, the Risk Committee is designated to undertake this responsibility. The Head of Risk is the executive responsible for risk framework and respective policies, including the Risk Governance and Management Framework and Risk Appetite Framework and their implementation and enforcement.

Board Committees

The Audit Committee oversees the quality and completeness of the Bank's financial reporting including accounting policies and financial statement disclosures, and oversees the internal audit function, ensuring that recommendations are actioned accordingly. It also oversees all related party balances and transactions.

The Risk Committee acts as the Risk Council of the BoD. In this capacity, it oversees the risk profile of the Bank on behalf of the BoD as well as the implementation of the risk management and control principles.

The Company Secretary acts as secretary to both Board committees.

Management Committees

The Credit Committee functions primarily as a deliberative and advisory body on matters concerning the management of the Bank's Credit management. The Credit Committee is responsible for assessing and managing credit risk, including evaluating borrower creditworthiness and potential default. It develops and oversees credit policies to ensure consistent and compliant lending practices. The Credit function is responsible for credit-policy and its implementation and enforcement.

The Financial Crime Compliance Committee has the overall responsibility for the onboarding of high-risk corporate accounts and the enforcement of the Bank's risk appetite with respect to corporate account opening.

Other Key roles

The Chief Financial Officer (CFO) is responsible for transparency in the financial performance of the Bank and its business groups, including high-quality and timely reporting and disclosure in line with regulatory requirements, corporate governance standards and global best practice.

The Head of Risk is responsible for implementing the risk principles in all areas of the Bank. Together with the Head of Risk, the Chief of Legal and Compliance is also responsible for the legal and compliance risk areas. The Head of Financial Crime/MLRO (FCC/MLRO), a separate individual within the Bank is responsible for preventing and detecting all financial crime risk originating from money laundering and terrorist financing. The FCC/MLRO is assisted by a deputy.

The Chief Technology Officer (CTO) of the Bank is responsible for overseeing the development and implementation of the Bank's information technology strategy to ensure alignment with its business goals, managing and optimizing the Bank's technology infrastructure, including networks, systems, and applications, to enhance operational efficiency and security. Additionally, the CTO collaborates closely with the risk management function to identify and mitigate ICT risks, ensuring compliance with regulatory requirements and safeguarding the Bank's sensitive data.

The Chief Legal and Compliance Officer (CLCO) of the Bank is tasked with overseeing legal and compliance functions to ensure adherence to laws and regulations governing banking operations. The CLCO provides guidance to senior management on legal matters and regulatory requirements, conducts risk assessments, and develops policies and procedures to mitigate legal and regulatory risks. Additionally, the CLCO collaborates with internal and external stakeholders to uphold the bank's reputation and integrity, while also integrating legal and compliance considerations into the overall risk management framework of the institution.

The risk control process

There are five key elements in the independent risk control process that have been implemented:

- Risk framework including governance, appetite and policies implementing the risk principles, reflecting the Bank's risk tolerance and risk appetite, which is consistent with the evolving business requirements and international best practice. The Bank's risk policies are principle-based, specifying minimum requirements, high-level controls and standards, and broad authorities and responsibilities. These complement the exercise of sound business judgment in determining actions and decisions.
- Risk identification through top-level governance, continuous monitoring of portfolios, assessment of risks in new businesses and complex or unusual transactions, and ongoing review of the risk profile in the light of market developments and external events;
- Risk measurement using methodologies and models which are independently verified and approved;
- Risk control by monitoring and enforcing compliance with risk principles, policies, and limits, and with regulatory requirements and by performing risk control self-assessments (RCSA) exercises; and
- Transparent risk reporting to stakeholders, and to management at all levels, on all relevant aspects of the approved risk control framework, including limits.

The Bank developed control processes around the establishment of new businesses, and the execution of complex or unusual transactions. These processes involve the business, and potentially all the control functions – risk control, legal, compliance, treasury, finance, tax, ICT and logistics, as necessary. The objective is to ensure that all critical elements are addressed across disciplines. A key consideration is whether such transactions can be effectively managed in relation to ongoing risk management, measurement, control, and reporting. The Bank also invests in I.T. solutions to improve its processes whilst managing, controlling and monitor risks.

Head of Risk is responsible to draft and maintain a dynamic Risk Register which defines, measures, and discloses for all types of risks of the Bank; the inherent risk, which includes likelihood and impact, the controls for each risk, which are individually rated and finally the residual risk. The result is compared with the risk tolerance of the Bank. Quantitative and qualitative elements are considered during the process.

Risk Management Framework

The Bank’s Risk Appetite Statement included in the Bank’s Risk Management Framework is presented to the Risk Committee and thereafter is reviewed and approved by the Board, outlining the most significant risks to which the Bank is exposed and providing guidance on acceptable risk types and maximum amounts. It is an integral component of the Bank’s overarching Risk Management Framework and aids in aligning strategy and business objectives with the Bank's mission, vision, and core values. This statement establishes the "tone at the top" and filters down to tactical and operational levels through risk policies, key risk indicators, limits, and established processes and controls. Supported by a Risk Appetite Dashboard, it delineates risk limits and triggers to benchmark the Bank's risk profile with its risk appetite (using a 'traffic lights approach').

Risk culture influences the decisions of management and employees during the Bank's day-to-day activities and impacts the risks assumed by the Bank. The Bank's management, including key function holders, contribute to internal communication of core values and expectations to employees. Employees are expected to be risk-aware and adhere to the Bank's policies, all applicable laws and regulations, and promptly escalating observed non-compliance.

The management body continually promotes, monitors, and assesses the Bank's risk culture, considering its impact on financial stability, risk profile, and robust governance, making necessary changes and aligning risk-taking behavior with the Bank's risk profile and long-term objectives.

The Bank's risk profile is managed within the risk appetite established by the Board, supported by a strong capital base and an adequate portfolio of highly liquid assets to meet financial obligations as they arise.

As at end of December 2024, the Board declares that the Bank's risk profile remained well within its risk appetite and tolerance levels as set by the Board. This is supported by adequate risk management arrangements in relation to the overall risk profile and business model.

Furthermore, the Bank is committed to ongoing review and enhancement of its risk management framework to adapt to evolving market conditions, regulatory changes, and emerging risks. The Bank's risk management systems are integral to the Bank's business operations and are continuously evaluated to ensure alignment with the risk appetite and strategic direction.

Disclosures to senior management and the Risk Committee are facilitated through the monitoring of Key Risk Indicators (KRIs), which serve as vital metrics for assessing the Bank's risk profile. These indicators are diligently monitored on a frequent basis to provide timely insights into emerging risks and trends. In the event of breaches or deviations from predetermined thresholds, reports are promptly escalated to the Risk Committee or the Board, in accordance with the Bank's Risk Appetite framework escalation procedure. This proactive approach ensures that senior management and governing bodies are promptly informed of any potential risk exposures, enabling informed decision-making and proactive risk management strategies.

The Bank upholds a steadfast commitment to maintaining robust risk management practices, characterized by systematic and regular reviews of its risk frameworks and policies. Annually, the Bank conducts assessments of its risk management strategies, whilst considering evolving banking regulations and industry standards. Additionally, the Bank employs diligent monitoring mechanisms to continuously assess the effectiveness of these frameworks in mitigating risks and promoting financial stability.

Risk categories

Business risks are the risks associated with a chosen business strategy – it is business management's responsibility to respond to fundamental changes in the economic environment and the competitive landscape. Business risks are not subject to independent risk control but will be factored into the Bank's planning and budgeting process and the assessment of the Bank's risk capacity and overall risk exposure. Business risks are also addressed in the Bank's Business Continuity and Recovery Planning (BCRP).

The primary and operational risks inherent in business activities are subject to independent risk control.

Primary risks are:

- Credit default risk – the risk of loss resulting from the failure of a client or counterparty to meet its contractual obligations. It arises on traditional banking products, such as loans and commitments, and on derivatives and similar transactions. A form of credit risk also arises on securities and other obligations in tradable form. Their fair values are affected by changing expectations about the probability of failure to meet obligations as well as actual failures. Where these instruments are held in connection with a trading activity, the Bank controls the risk as market risk;
- Concentration risk - refers to the potential adverse impact resulting from a significant exposure to specific counterparties, sectors, or geographic regions within a Bank's portfolio. It encompasses the risk of losses arising from dependencies on a limited number of counterparties or a high degree of correlation among exposures.
- Operational risk - the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external causes, whether deliberate, accidental or natural. Operational risks must be monitored, and are controlled and mitigated to the extent possible and desirable; and
- Liquidity and funding risk – the risk that the Bank might be unable to meet its payment obligations when due, or to borrow funds in the market on an unsecured or secured basis at an acceptable price to fund actual or proposed commitments.
- Solvency risk - refers to the potential threat that the Bank may not have sufficient capital to meet its long-term obligations or commitments. Solvency risk can lead to financial distress, default, or insolvency if not adequately managed.

Quantitative controls

In principle, for risks that are quantifiable the Bank will be measuring potential loss at two levels – expected loss and stress loss.

Expected loss is the loss that is expected to arise on average over time in connection with an activity. It is an inherent cost of such activity and must be factored into business plans. For lending instruments carried at amortised cost, expected loss is estimated using the Bank's expected credit loss model in accordance with IFRS9. Allowances for impairments specific for each lending contracts based on the expected credit loss model are accounted for.

Stress loss is the loss that could arise from extreme events, typically beyond the confidence level of the statistical loss estimate and is normally a scenario-based measure.

Concentration controls complement portfolio risk measures. Controls are generally applied where the Bank identifies those positions in different lending portfolios that are affected by changes in the same risk factor or group of correlated factors and there is the potential for significant loss in the event of extreme but plausible adverse developments. The Bank's concentration controls include credit limits for individual clients, counterparties, and counterparty groups.

Qualitative controls

While measuring risk is crucial, quantification alone may not capture the full scope of risks, as not all are easily quantifiable. Therefore, alongside rigorous measurement, due diligence, sound judgment, common sense, and an understanding of diverse potential outcomes, coupled with a readiness to question assumptions are essential components of fostering a robust risk culture for both risk management and control.

CREDIT RISK

Credit risk is the risk of financial loss resulting from failure by a client or counterparty to meet its contractual obligations. This can be caused by factors directly related to the counterparty, such as business or management problems, or from failures in the settlement process, for example on a lending transaction, where the Bank honours its obligation, but the counterparty fails to deliver the counter-value (settlement risk). Alternatively, it can be triggered by economic, pandemic, wars, or political difficulties in the country in which the counterparty is based or where it has substantial assets (country risk).

Sources of credit risk

Credit risk is inherent in lending products of the Bank namely asset financing, factored receivables and loans. The risk control processes applied to these products are fundamentally the same, and they are valued at amortised cost. Moreover, cash balances with other banks also carry a certain level of credit risk.

Credit risk control organisation and governance

Effective credit risk control is critical to the Bank's safety and soundness. The credit risk control framework is based on the risk management and control principles, supported by credit policies. It has both qualitative and quantitative elements. The Bank has established processes to ensure that risks are identified, assessed, pre-approved where necessary, and continuously monitored and reported. Measures and limits are applied to the credit risk of individual counterparties and counterparty groups, and the quality and diversification of portfolios and sub-portfolios are assessed, a key objective being to control risk concentrations.

The Credit Committee assesses the creditworthiness of individual counterparties and the adequacy and effectiveness of any security or credit hedges, and evaluates credit risk in portfolios, sub-portfolios and other aggregations, including country risk.

Subject to rigorous parameters, the Board of Directors has delegated authority to grant credit facilities and place them on the Bank’s balance sheet, in accordance with pre-established approval limits for senior management, the Credit Committee and for amounts higher than delegated authority limits, the Board of Directors. The Risk Management Function also participates in the Credit Committee meetings.

Credit risk control

Limits and controls

The Bank has established limits taking into consideration banking regulations including the large exposures limits, to constrain exposure to individual counterparties and counterparty groups and at portfolio and sub-portfolio levels, wherever risk concentrations are identified, including exposure to specific industries and countries, where appropriate.

At the level of the individual counterparty and counterparty group, the authorised officers will establish limits for all types of exposure. Credit engagements may not be entered into without the appropriate approvals and limits. When it comes to factoring, the Bank utilises a credit insurance with the aim to insure debtor limits when deemed necessary. The vast majority of the limits are insured.

Limits apply in a variety of forms to portfolios or sectors, where necessary, to restrict risk concentrations or areas of higher risk, or to control the rate of portfolio growth. The impact of variations in default rates and asset values is assessed using stress scenarios, considering risk concentrations. Stress loss limits will be applied to portfolios when considered necessary, including limits on exposures. For all exposures, the credit quality, and cash flow generation capacity of the counterparty over the full term of the obligation are considered when undertaking the credit assessment.

Risk mitigation

The Bank exerts risk mitigation techniques for its credit portfolios by way of collateral and loan to value ratios as well as insurance limits in the case of factoring receivables. In addition, the Bank has Key

Risk Indicators (KRIs) in place to monitor and manage credit risk on an ongoing basis, supporting early identification of potential deterioration in credit quality.

Reporting

An essential element of the credit risk control process is transparent and objective risk reporting. The Credit Function is responsible for risk reporting covering both exposure to individual counterparties from all products and activities, and portfolio risks. The Credit Function also supplies regular and ad hoc risk information to the Credit Committee, the Board of Directors and Regulators where applicable.

Credit risk measurement

Credit risk measurement is an essential component within the credit risk control framework. While measuring credit exposure from a loan which is fully drawn is straightforward, assessing portfolio involves estimating the likelihood of defaults, associated loss ratios and of default correlations between counterparties.

The Bank has developed tools to facilitate the quantification of credit risk of individual counterparties, employing the three generally accepted parameters: probability of default, loss given default and exposure at default.

Aligned with the Bank's internal governance standards and the regulatory capital framework requirements, the development and maintenance of models will adhere to global standards, and the models and their components will be subject to independent verification before implementation. Models must comply with established measurement standards to ensure consistency and enable meaningful aggregation of credit risk across all businesses. Furthermore, they are subject to ongoing review and updating.

Credit risk parameters

Three parameters are used to measure and control individual counterparty credit risk:

- the "probability of default", which is an estimate of the likelihood of the client or counterparty defaulting on its contractual obligations. This probability is assessed using rating tools tailored to the various categories of counterparties. Besides their use for credit risk measurement, ratings will be an important element in setting credit risk authorities;
- the likely recovery ratio on the defaulted claims, which is a function of the type of counterparty and any credit mitigation or support (such as security or guarantee), from which the "loss given default" is determined; and
- the current exposure to the counterparty and its possible future development, from which potential "exposure at default" is derived. In measuring individual counterparty exposure against credit limits, the Bank considers the "maximum likely exposure" measured to a high confidence level over the full life of all outstanding obligations, whereas in aggregating exposures to different counterparties for portfolio risk measurement, the expected exposure to each counterparty at a given time horizon (usually one year) generated by the same model is used.

These parameters are the basis for most internal measures of credit risk.

Expected loss

Credit losses must be expected as an inherent cost of doing business. But the occurrence of credit losses is erratic in both timing and amount, and those that arise usually relate to transactions entered in the previous accounting periods. In order to reflect the fact that future credit losses are implicit in today's portfolio, the Bank uses the concept of "expected loss".

Expected credit loss is a statistically based concept which is used to estimate the annual costs that are expected to arise, on average, from positions in the current portfolio that become impaired. The expected loss for a given credit facility is a function of the three components described above – probability of default, loss given default and exposure at default. The expected loss figures for individual counterparties are aggregated to derive the expected credit loss for the whole portfolio.

Expected loss is the foundation of credit risk quantification in all portfolios. It is an input to the valuation or pricing of some products, and the determinant of credit risk costs charged to the business in the management accounts, differs from the credit loss expense reported under International Financial Reporting Standards (IFRS). The Bank has a fully adopted the Expected Credit Loss Model for accounting in accordance with IFRS 9. Expected loss is also the starting point for the measurement of portfolio statistical loss and stress loss.

Composition of credit risk

The measures of credit risk differ, depending on the purpose for which exposures are aggregated – financial accounting under IFRS, the determination of regulatory capital, and the Bank's own internal management view, i.e. the way credit portfolio risk is managed.

Settlement risk

Settlement risk arises in transactions involving exchange of value when the Bank must honour its obligation to deliver without first being able to determine that the counter-value has been received.

Impairment and default – distressed claims

The Bank has classifications for distressed claims.

A loan carried at amortised cost is considered to be "past due" when a payment due has been missed. It is classified as "non-performing" when a loan is past due for more than 90 days and/or irrespective of the repayment not being overdue by 90 days, the Bank has reasons to doubt the eventual recovery of funds. When obligations have been restructured on concessionary terms, the loan is classified as "forborne".

Any claim, regardless of accounting treatment, is classified as "impaired" if the Bank considers it probable that it will suffer a loss on that claim as a result of the obligor's inability to meet its obligations according to the contractual terms, and after realization of any available collateral. "Obligations" in this context include interest payments, principal repayments, or other payments due.

Impairment under amortised cost valuation is recognised through the creation of an allowance or provision, which is charged to the statements of comprehensive income as credit loss expense. Portfolios of claims carried at amortised cost with similar credit risk characteristics are also assessed for collective impairment. A portfolio is considered impaired on a collective basis if there is objective evidence to suggest that it contains impaired obligations, but the individual impaired items cannot yet be identified.

The Bank reviews individual positions for impairment only after they have been in arrears for a certain time. Thus, to cover the time lag between the occurrence of an impairment event and its identification, collective loan loss allowances are established, based on the expected loss measured for the portfolio over the average period between trigger events and their identification for individual impairments.

Past due but not impaired loans

Past due but not impaired loans have suffered missed payments but are not considered impaired because the Bank expects ultimately to collect all amounts due under the contractual terms of the loans or with equivalent value.

Impaired loans, allowances, and provisions

There were impaired lending agreements and allowances specific for impairment on each lending contract based on the expected credit loss model as at 31 December 2024.

In general, the Bank's practice is to treat loans, factoring exposures and financial leases as non-performing exposures when upcoming cash flow problems of the clients are detected or if such exposures have exceeded the 90 days past due on their repayments.

The Bank will execute foreclosures by taking possession and disposing of the underlying assets to which it holds as security. Collateral is liquidated in the most expeditious manner and at prices considered fair. This may require that it purchases assets for its own account, where permitted by law, pending orderly liquidation.

Credit loss expense

The Bank's financial statements are prepared in accordance with IFRSs, under which, credit loss expense charged to the statements of comprehensive income in any period is the sum of net allowances based on the expected loss concept described under "Credit risk measurement "and direct write-offs minus recoveries arising in that period.

Rating system design and estimation of credit risk parameters

Probability of default

The Bank assesses the likelihood of default of individual counterparties using rating tools tailored to the various counterparty segments. The performance of rating tools, including their predictive power with regard to default events, is regularly validated and model parameters are adjusted as necessary.

Loss given default

Loss given default represents the Bank's expectation of a loss should default occur. It is expressed as percentage loss per unit of exposure and typically varies by type of counterparty, type and seniority of claim, and availability of collateral or other credit mitigation. Loss given default estimates the loss of principal, interest, and other amounts due (including work-out costs), and also takes into account the costs of carrying the impaired position during the work-out process.

Exposure at default

Exposure at default represents the amounts the Bank expects to be owed at the time of default. For outstanding loans, the exposure at default will be the drawn amount or face value. For loan commitments and for contingent liabilities, it includes any amount already drawn plus the further amount which is expected to be drawn at the time of default, should it occur. This calculation is based on a "credit conversion factor", a fixed percentage per product type derived from historical experience of drawings under commitments by counterparties within the year prior to their default.

CONCENTRATION RISK

A concentration of risk exists where positions in the lending financial instruments are affected by changes in the same risk factor or group of correlated factors, and the exposure could, in the event of extreme but plausible adverse developments, result in significant losses. The identification of risk concentrations necessarily entails judgment about potential future developments, which cannot be predicted with certainty. In determining whether a concentration of risk exists, risk controllers consider a number of elements, both individually and in combination including the risk reward profile of the positions. If a risk concentration is identified, it is assessed to determine whether it should be reduced or the risk should be mitigated, and the available means to do so. Identified concentrations are subject to increased monitoring and to Pillar II capital allocation.

OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, and systems, or from external causes, whether deliberate, accidental, or natural. It will be inherent in all the Bank's activities, not only in the business the Bank conducts but due to the fact it is a business – because the Bank is an employer, it may own and occupy property and hold assets, including information, belonging to both the Bank, as well as its clients. The approach to operational risk is not designed to eliminate risk per se but, rather, to contain it within acceptable levels, as determined by senior management, Risk Committee and Board of Directors and to ensure that the Bank have sufficient information to make informed decisions about additional controls, adjustments to controls, or other risk responses. The CEO, the CFO, Head of Risk, FCC / MLRO, Chief Legal and Compliance and Chief Technology Officer, share the responsibility for the independence, objectivity, and effectiveness of the operational risk framework.

Operational risk framework

Every function, whether a front-end business or a control or logistics unit, must manage the operational risks that arise from its own activities. Because these risks are pervasive, with a failure in one area potentially impacting many others, the Bank's framework will be based on mutual oversight across all functions. Each area of operations will therefore have established cross-functional cooperation with the Risk Management function as an integral part of its governance structure, to actively manage operational risk.

The foundation of the operational risk framework is the definition by all functions of their roles and responsibilities so that, collectively, they can ensure that there is adequate segregation of duties, complete coverage of risks and clear accountability. From this analysis, they will develop control objectives and standards to protect the Bank's tangible and intangible assets and interests, based on the types of operational risk events that might arise, ranging from daily reconciliation problems to potentially severe events such as fraud. The Bank recognizes that it cannot eliminate all risks, because errors and accidents will always happen, and that where possible, it is not always cost effective to do so. The Bank's internal control framework will differentiate potential events depending on their likely frequency and impact. Mitigation and prevention efforts focused on areas where the Bank is most exposed to severe events, including both those that are reasonably foreseeable and those that, while not predictable, are thought to be reasonably possible. For lower impact risks, the Bank will concentrate on management and monitoring.

The functions will monitor compliance with their controls and assess their operating effectiveness in several ways, including self-certification by staff, evaluation of responses by management, active involvement in updating of the Risk Register of the Bank and incident reporting. The implications of internal and external audit findings and other relevant sources of information will also be assessed. Furthermore, the Head of Risk conducts an RCSA exercise on the main processes of the Bank. During this exercise any gaps in the Bank's controls are identified and addressed and the Risk Register is updated accordingly.

As major operational risk events take place, the Bank will assess their causes and the implications for its control framework, whether or not they lead to direct financial loss. This will include events affecting third parties that are relevant to the Bank's business if sufficient information is made public. It is important to use all available information to test the control framework because, even if an internal event does not lead to a direct or indirect financial loss, it may indicate that the Bank's standards are not being complied with.

The totality of this information will be reviewed by functional managers to assess their operational risk exposure and the actions needed to address specific issues. These issues will be formally captured on the risk register, forming the basis of reporting to the Board of Directors.

Operational risk measurement

The Bank's policy sets forth a framework for the identification, management, monitoring and reporting on the Bank's exposure to this risk. When internal controls fail, operational risk can adversely affect the Bank's reputation, have legal or regulatory implications, and / or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through its control framework and by monitoring and responding to potential risks effectively. Controls include appropriate segregation of duties, ensuring that staff members have appropriate expertise and training and regular verification and reconciliation of transactions and accounts.

The Bank maintains a regularly updated business continuity and disaster recovery plan. This plan outlines standard procedures to be followed in the event of operational disruptions, ensuring the efficient and prioritized resumption of core services and critical functions. Additionally, the Bank mitigates the likelihood and/or impact of specific events through its comprehensive insurance coverage, which undergoes annual monitoring and renewal.

The Bank continues to invest in IT within its activities and strengthen its online presence, while cognisant of the evolving cyber threats landscape. The Bank maintains zero tolerance to events that could compromise the confidentiality and integrity of data as well as the availability of its IT systems.

The Bank does not set limits on operational risk but will report the measured risk through the standard reporting processes. It allocates capital for operational risk in line with the basic indicator approach as regulated in the Capital Requirement Regulation.

LIQUIDITY AND FUNDING RISK MANAGEMENT

Liquidity risk is the risk of being unable to raise funds to meet payment obligations when they fall due. Funding risk is the risk of being unable, on an ongoing basis, to borrow funds in the market at an acceptable price to fund actual or proposed commitments and thereby support the Bank's current business and desired strategy. Liquidity and funding are not the same, but they are closely related, and both are critical to a credit institution.

Liquidity must be continuously managed to ensure that the Bank can survive a crisis, whether it is a general market event, a localised difficulty affecting a smaller number of institutions, or a problem unique to an individual firm. An institution that is unable to meet its liabilities when they fall due may collapse, even though it is not insolvent, because it is unable to borrow on an unsecured basis or does not have sufficient good quality assets to borrow against or liquid assets to sell to raise immediate cash.

Liquidity approach

The Bank's approach to liquidity management is to ensure that it will always have sufficient liquidity to meet liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking sustained damage to its business.

Central to the integrated framework is an assessment of all material, known and expected cash flows and the level of high-grade collateral that could be used to raise additional funding. It entails both careful monitoring and control of the daily liquidity position, and regular liquidity stress testing.

The liquidity position will be assessed and managed under a variety of potential scenarios encompassing both normal and stressed market conditions. The Bank will consider the possibility that its access to markets could be impacted by a stress event affecting some part of its business or, in the extreme case, if it was to suffer a period of general market uncertainty.

Liquidity management

The Bank will manage its liquidity position in order to be able to ride out a crisis without damaging the ongoing viability of its business. This is complemented by the Bank's funding risk management which aims to achieve the optimal liability structure to finance its businesses cost-efficiently and reliably. The long-term stability and security of the Bank's funding in turn will help protect its liquidity position in the event of an the Bank-specific crisis.

Liquidity modelling and contingency planning

The liquidity position is managed and monitored on an ongoing basis by the Treasury Function and liquidity risk is monitored continuously by the Risk Management Function.

Liquidity is also assessed within the Internal Liquidity adequacy assessment process (ILAAP). Anticipating significant loan drawdowns, whilst efficiently monitoring and anticipating customer accounts including fixed term deposits withdrawals, is essential to avoid situations of liquidity shortages including the possibility that deposits are not renewed or else or replaced by new customer deposits. Liquidity crisis scenario analysis will support the liquidity management process so that immediate corrective measures, such as the build-up of a liquidity buffer to absorb potential sudden liquidity gaps, can be put in place.

The Bank regularly evaluates the impact of a liquidity crisis scenario, combining a firm-specific crisis with market disruption, across various time horizons. This includes envisioning large drawdowns on otherwise stable client deposits, challenges in renewing or replacing maturing unsecured funding, and limited capacity to generate liquidity from trading assets. Liquidity crisis scenario analysis supports the liquidity management process by enabling the implementation of immediate corrective measures, such as establishing a liquidity buffer to absorb potential sudden liquidity gaps

The starting point for stress testing analyses will be a breakdown of the contractual maturity of the Bank's assets and liabilities. Since a liquidity crisis could have a myriad of causes, the Bank focuses on a scenario that encompasses all potential stress effects across all markets, currencies, and products.

Liquidity needs may result from commitments and contingencies, including credit lines extended to secure the liquidity needs of clients. The Bank regularly monitors undrawn committed credit facilities and other latent liquidity risks.

Liquidity limits and controls

While its estimated capacity to generate liquidity when required will naturally vary, the Bank generally applies a constant limit structure, which imposes a ceiling on the projected net funding requirement along the cash ladder. Limits are based on the amount of cash the Bank believes it could raise in a firm-specific crisis.

As part of the ILAAP process and Recovery Planning, the Bank sets fallback plans for liquidity crisis management, the cornerstone of which is the Bank’s access to secured funding either from the market mainly through deposits or through interbank lending or through central bank collateralised lending, coupled with the ability to turn sufficient liquid assets into cash within a short time frame. Other strategies include the reduction of factoring business.

Liquidity ratios

In addition to the limits and controls described above, the Bank also measures Liquidity Coverage Ratio. This considers the Bank’s level of high-quality liquid assets against expected net cash outflows over a 30-day period. The Bank needs to have sufficient liquidity to cover all projected outflows.

The Net Stable Funding Ratio which aims at ensuring a sound funding structure over one year in an extended stress scenario. NSFR requires the Bank to maintain sufficient stable funding relative to required stable funding, to reflect the Bank’s long-term funding profile. Assets have to be matched, to a predetermined extent depending on their liquidity profile at a one-year horizon, with sources of funding that can be considered stable over the same one-year horizon.

Key metrics:

		Lidion Group consolidated	Lidion Bank standalone	
		31/12/2024	31/12/2024	31/12/2023
	Available own funds (amounts)			
1	Common Equity Tier 1 (CET1) capital (€ million)	21.00	21.83	12.85
2	Tier 1 capital (€ million)	21.00	21.83	12.85
3	Total capital (€ million)	21.00	21.83	13.19
	Risk-weighted exposure amounts			
4	Total risk exposure amount (€ million)	96.71	96.95	70.37
	Capital ratios (as a percentage of risk-weighted exposure amount)			
5	Common Equity Tier 1 ratio (%)	21.71%	22.52%	18.27%
6	Tier 1 ratio (%)	21.71%	22.52%	18.27%
7	Total capital ratio (%)	21.71%	22.52%	18.75%
	Additional own funds requirements to address risks other than the risk of excessive leverage (as a percentage of risk-weighted exposure amount)			
EU 7a	Additional own funds requirements to address risks other than the risk of excessive leverage (%)	4.50%	4.50%	5.50%
EU 7b	of which: to be made up of CET1 capital (percentage points)	2.53%	2.53%	3.09%
EU 7c	of which: to be made up of Tier 1 capital (percentage points)	3.38%	3.38%	4.13%
EU 7d	Total SREP own funds requirements (%)	12.50%	12.50%	13.50%
	Combined buffer and overall capital requirement (as a percentage of risk-weighted exposure amount)			
8	Capital conservation buffer (%)	2.50%	2.50%	2.50%
EU 8a	Conservation buffer due to macro-prudential or systemic risk identified at the level of a Member State (%)	0.00%	0.00%	0.00%
9	Institution specific countercyclical capital buffer (%)	0.91%	0.91%	0.84%
EU 9a	Systemic risk buffer (%)	0.00%	0.00%	0.00%
10	Global Systemically Important Institution buffer (%)	N/A	N/A	N/A
EU 10a	Other Systemically Important Institution buffer (%)	N/A	N/A	N/A
11	Combined buffer requirement (%)	3.41%	3.41%	3.34%
EU 11a	Overall capital requirements (%)	15.91%	15.91%	16.84%
12	CET1 available after meeting the total SREP own funds requirements (%)	9.21%	10.02%	5.25%
	Leverage ratio			
13	Total exposure measure (€ million)	284.08	284.96	154.55
14	Leverage ratio (%)	7.39%	7.66%	8.32%
	Additional own funds requirements to address the risk of excessive leverage (as a percentage of total exposure measure)			
EU 14a	Additional own funds requirements to address the risk of excessive leverage (%)	0.00%	0.00%	0.00%
EU 14b	of which: to be made up of CET1 capital (percentage points)	0.00%	0.00%	0.00%
EU 14c	Total SREP leverage ratio requirements (%)	3.00%	3.00%	3.00%
	Leverage ratio buffer and overall leverage ratio requirement (as a percentage of total exposure measure)			
EU 14d	Leverage ratio buffer requirement (%)	0.00%	0.00%	0.00%
EU 14e	Overall leverage ratio requirement (%)	3.00%	3.00%	3.00%
	Liquidity Coverage Ratio			
15	Total high-quality liquid assets (HQLA) (Weighted value -average) (€ million)	163.56	163.56	56.83
EU 16a	Cash outflows - Total weighted value (€ million)	76.34	76.34	23.45
EU 16b	Cash inflows - Total weighted value (€ million)	28.23	28.23	16.46
16	Total net cash outflows (adjusted value) (€ million)	48.11	48.11	6.99
17	Liquidity coverage ratio (%)	340.06%	340.06%	844.79%
	Net Stable Funding Ratio			
18	Total available stable funding (€ million)	242.13	242.71	105.53
19	Total required stable funding (€ million)	68.89	69.02	49.18
20	NSFR ratio (%)	351.49%	351.65%	214.58%

Overview of total risk exposure amounts:

		Lidion Group consolidated		Lidion Bank standalone		
		Total risk exposure amounts (TREA)	Total own funds requirements	Total risk exposure amounts (TREA)		Total own funds requirements
		31/12/2024	31/12/2024	31/12/2024	31/12/2023	31/12/2024
		€ million	€ million	€ million	€ million	€ million
1	Credit risk (excluding CCR)	82.96	6.64	83.61	62.97	6.69
2	Of which the standardised approach	82.96	6.64	83.61	62.97	6.69
EU 4a	Of which equities under the simple riskweighted approach	0	0	0	0	0
5	Of which the Advanced IRB (A-IRB) approach	0	0	0	0	0
6	Counterparty credit risk – CCR	0	0	0	0	0
7	Of which the standardised approach	0	0	0	0	0
9	Of which other CCR	0	0	0	0	0
15	Settlement risk	0	0	0	0	0
16	Securitisation exposures in the non-trading book (after the cap)	0	0	0	0	0
17	Of which SEC-IRBA approach	0	0	0	0	0
18	Of which SEC-ERBA (including IAA)	0	0	0	0	0
19	Of which SEC-SA approach	0	0	0	0	0
EU 19a	Of which 1 250 % / deduction	0	0	0	0	0
20	Position, foreign exchange and commodities risks (Market risk)	0	0	0	0	0
21	Of which the standardised approach	0	0	0	0	0
EU 22a	Large exposures	0	0	0	0	0
23	Operational risk	13.75	1.10	13.34	7.40	1.02
EU 23a	Of which basic indicator approach	13.75	1.10	13.34	7.40	1.02
24	Amounts below the thresholds for deduction (subject to 250 % risk weight)	0	0	0	0	0
29	Total	96.71	7.74	96.95	70.37	7.71

Rows 3, 4, 8, EU8a, EU8b, 10, 11, 12, 13, 14, 22, EU23b, EU23c, 25, 26, 27 and 28 from table Overview of Total Risk Exposures Amount have been removed as these are Not Applicable to the Bank.

The Bank's Return on Assets calculated as the net profit divided by the balance sheet total was 1.0% in 2024.

The calculation of "CET 1 available after meeting the total SREP own funds requirement (%)" has been updated in 2024 to follow regulatory interpretation of the calculation of this metric and as a result the 2023 comparative has been updated.

Funding

Through broad diversification of its funding sources (by market, product, and currency), the Bank maintains a well-balanced portfolio of liabilities, which will generate a stable flow of financing and provide protection in the event of market disruptions. This, together with its centralised funding management, will enable the Bank to pursue a strategy of efficient funding of business activities.

Funding approach

Short to medium- and long-term funding activities will be planned by assessing the overall funding profile of the balance sheet, taking due account of the effective maturity of the asset base and the amount of maturing funding that will have to be replaced. The ability to continue to fund ongoing business activities through periods of difficult market conditions is also factored in.

To ensure that a well-balanced and diversified liability structure is preserved, the Bank's finance and treasury functions will routinely monitor the Bank's funding status and report its findings on a regular basis to the senior management, Head of Risk and also share this information during the Asset and Liability Committee meetings.

SOLVENCY RISK

Solvency risk refers to the potential threat that the Bank may not have sufficient capital to meet its long-term obligations or commitments. This can lead to financial distress, default, or insolvency if not adequately managed. The Bank effectively manages solvency risk by maintaining adequate capital reserves, undertake prudent financial management practices, and ongoing monitoring of financial health and performance metrics. Capital management is reported and discussed at the Asset and Liability Committee (ALCO), Risk Committee and also Board.

The annual ICAAP exercise includes an assessment of both Pillar I and Pillar II risks, including credit default, Concentration risk, operational risk, IRRBB risk and other key risks. The Bank's stress testing framework forms an integral part of the ICAAP.

Several severe but plausible scenarios are developed that test the resilience of the Bank's business model and risk profile.

OTHER RELEVANT RISKS

IRRBB

Interest rate risk in the banking book refers to the potential adverse impact on the Bank's earnings and capital resulting from fluctuations in interest rates. This risk arises from the maturity mismatch between a Bank's assets and liabilities, as changes in interest rates can affect the value of these financial instruments differently. The Bank considers impacts on the Net Interest Income (NII) and Economic Value of Equity (EVE). The Bank has met the IRRBB outlier test requirements as defined under the Delegated Regulation (EU) 2024/857 and is not classified as an outlier institution.

The Bank addresses Interest Rate Risk as part of its Internal Capital Adequacy Assessment Process (ICAAP) and stress testing. Interest rates are a focal point of discussion during meetings of the ALCO.

Financial Crime Compliance Risk

This risk entails potential losses resulting from the Bank's exposure to financial crime. The Bank is dedicated to combating financial crime, adhering to relevant laws and regulations, and safeguarding itself, its customers, and its employees. It has established a Financial Crime Compliance function and committee to address these concerns and promotes a zero-tolerance approach towards financial crime.

Cyber Risk

Cyber risk encompasses threats to an organization's operations, assets, or data from cyber-attacks, security breaches, or technological vulnerabilities such as malware and phishing scams. Managing this risk involves robust cybersecurity measures, employee training, and incident response plans. The Bank addresses cyber risk within its risk management framework and discusses it in detail at the Risk Committee.

Business Continuity Risk

This risk involves the susceptibility of the Bank's critical operations, processes, or services to disruption due to unforeseen events like natural disasters or pandemics. Effective management requires robust business continuity plans, disaster recovery strategies, and resilience measures, including identifying critical dependencies and conducting regular testing and exercises.

Environmental, Social and Governance Risk

The Bank is committed to play a positive role in relation to Environmental Social and Governance ("ESG") risks and Factors. As a licenced credit institution, the Bank understands its responsibility towards the abovementioned factors, comprehending compliance with legal and regulatory mandates as well as further good practices and initiatives. The Bank also understands its critical role of engaging as much as possible with internal and external stakeholders to provide sound responses to these complex matters. Therefore, the Bank is dedicated and committed to address these factors comprehensively whilst enhancing its performance in these areas, as an integral component of its entire business strategy, incorporating ESG considerations throughout its operations and balances and controls throughout its functioning. The Bank remains cognizant of its exposure to ESG risks in the short, medium and also long term, diligently tracking regulatory guidelines, developments, and supervisory expectations. Consequently, measures aimed at mitigating such risks are integrated into the Bank's risk management framework. The Bank performed a materiality assessment in terms of ESG factors and has set internal governance arrangements to address these matters in a soundly and holistic manner. The Bank's internal governance mechanisms ensure active participation from the Board and senior management in fostering a risk-aware culture, defining risk appetite, and managing ESG risks. This is facilitated by clearly delineated responsibilities and reporting lines, ensuring the integration of ESG risks into the Bank's business strategy, processes, and risk management practices.

STRESS TESTING

The Bank's stress testing framework forms an integral part of the ICAAP and ILAAP suite of documents. A number of severe but plausible scenarios, are developed to test the resilience of the Bank's business model and risk profile. The Stress testing encompasses all material risks faced by the Bank. The ICAAP and ILAAP, which ensures that the Bank is adequately capitalised, is reviewed in detail by senior management, Risk Committee, and ultimately approved by the Board of Directors.

When assessing the Bank's capital and liquidity adequacy, the Bank considers the impact of economic cycles and other external/internal risks and factors. In this regard, the use of stress testing complements the risk assessment performed within the ICAAP and ILAAP documents.

Through stress-testing scenarios, the Bank estimates the impact on its capital and liquidity under both market-wide conditions, which refers to an event that negatively affects the financial system or the real economy, and idiosyncratic, which relates to an event that negatively affects the Bank. The Bank aligns with the EBA's methodology used for its 2023 EU-wide stress test which requires banks to apply the adverse macro-financial scenario developed by the European Systemic Risk Board (ESRB).

When conducting stress testing, the Bank considers all its business lines. The outcomes of these stress tests assist the Bank's risk management function in updating its regulatory-related Key Risk Indicators.

CAPITAL MANAGEMENT

Table EU OVC - ICAAP information

Row number	Explanation
(a)	**Capital Management** In managing its capital, the Bank considers a variety of requirements and expectations. Sufficient capital must be in place to support current and projected business activities, according to both the Bank's own internal assessment and the requirements of its regulators, in particular its regulator, the Malta Financial Services Authority (MFSA). Capital is also managed in order to achieve sound capital ratios that ensure that the Bank remains well-capitalised. This will be crucial in retaining clients' confidence in the Bank's financial strength and also in supporting the Bank's funding position and favourable borrowing costs in the international financial markets. The Bank aims to maintain sound capital ratios at all times, and it therefore considers not only the current situation but also projected developments in both its capital base and capital requirements. The main tools by which the Bank manages the supply side of its capital ratios are active management of capital instruments and dividend payments. **Capital adequacy management** Ensuring compliance with minimum regulatory capital requirements and targeted capital ratios is central to capital adequacy management. In this ongoing process, the Bank manages towards Tier 1 and Total capital target ratios. In setting key risk indicators, the Bank takes into account the regulatory minimum capital requirements and regulator's expectations that the Bank holds adequate capital. The Bank's capital management approach ensures a sufficient level of capitalisation, to meet both short- and long-term capital obligations, to manage the risk exposures at hand while enabling business growth and providing adequate returns to the shareholders. Risk capital management does not in any way substitute risk mitigation measures. It is vital that the structure of limits and thresholds should be able to prevent concentrations of risk from building up in such a way as to compromise a significant portion of the Bank's capital resources. **Use of Stress Testing Results** The Bank conducts stress testing to assess the resilience of its capital and liquidity positions under adverse scenarios. The results of these stress tests are crucial in calibrating the Bank's regulatory Key Risk Indicators (KRIs) related to capital and liquidity. These KRIs are closely monitored by the Risk Management Function, calculated on a weekly basis, and formally reported on a monthly basis to the Risk Committee and the Board of Directors. This process ensures that early warning signals are promptly identified, and appropriate mitigating actions can be taken in a timely manner.

Row number	Explanation
	Adoption of a Forward-Looking Approach The Bank adopts a forward-looking approach to risk and capital management, incorporating comprehensive financial projections over a three-year horizon. These projections include detailed forecasting of capital adequacy, liquidity coverage, leverage, and other key regulatory ratios. This forward-looking view enables the Bank to anticipate potential capital and liquidity needs, assess the impact of strategic initiatives, and support sustainable business growth while maintaining compliance with regulatory requirements. **Alignment of Capital Adequacy Assessment with the Risk Appetite Framework** The Bank's capital adequacy assessment is fully aligned with its Risk Appetite Statement, ensuring coherence between strategic objectives and risk-bearing capacity. The capital and liquidity KRIs, which reflect the Bank's tolerance for risk, are embedded within the Risk Appetite Framework. This alignment reinforces the Bank's commitment to maintaining a sound risk profile and supports informed decision-making at all levels. **Consideration of CRR III and EBA Guidelines** The Bank continuously monitors and incorporates developments in the regulatory landscape, including the Capital Requirements Regulation III (CRR III) and relevant guidelines issued by the European Banking Authority (EBA). These regulatory frameworks are considered in the Bank's risk and capital planning processes to ensure preparedness for future regulatory requirements and to maintain alignment with best practices in risk governance and transparency. **Incorporation of ICAAP within the Overall Risk Management Process** The Internal Capital Adequacy Assessment Process (ICAAP) is integrated into the Bank's risk identification, measurement, monitoring, and reporting processes, ensuring that internal capital levels remain commensurate with the Bank's risk profile and strategic plans. The ICAAP supports a proactive approach to capital planning, mainly since it contributes to the updating of internal key risk indicators and in facilitating internal dialogue across functions and fostering a culture of prudent risk-taking. **Governance Processes Involved** The governance framework supporting the process used to assess and identify the adequacy of internal capital this assessment is structured across several levels. The Risk Committee oversees the Bank's risk profile, including the monitoring and reporting of regulatory capital and liquidity ratios, ensuring they remain within the Board-approved risk appetite. The Board of Directors retains strategic and supervisory responsibilities, including the approval of projections and the Risk Appetite Framework. Capital management is under the direct control of the Board of Directors. At the management level, the Credit Committee monitors credit risk including capital implications on the lending business, while the Asset and Liability Committee (ALCO) manages liquidity, funding, and interest rate risk in the banking book, assessing their effects on capital should adjustments in the asset liabilities take place. These committees are supported by the Risk Management, Finance, Treasury, and Legal and Compliance functions, which provide the necessary analysis, reporting, and assurance to inform decisions. This integrated process ensures that capital adequacy assessments reflect a holistic view of the Bank's risk exposures, business strategy, and regulatory expectations, beyond the formal ICAAP framework.

Row number	Explanation
	ICAAP and ILAAP The Bank's ICAAP 2024 submission includes a suite of documents which consists of the core information items as requested in the EBA's Guidelines. The Bank prepared five documents, being: • The Business model, strategy, and corporate governance document; • The Stress testing document; • The ICAAP document; • The ILAAP document; and • The Capital and Liquidity Adequacy Statement. ***ICAAP*** The document follows the principles outlined in Article 73 of Directive 2013/36/EU ("CRD IV") to have in place sound, effective and comprehensive strategies, and processes to assess and maintain on an ongoing basis the amounts, types and distribution of internal capital that are commensurate to the nature and level of the risks to which the Bank is or might be exposed. Through the ICAAP report, the Bank identifies the most material risks to capital emanating from its business model and describes the manner in which these risks are effectively controlled. In view of this, the Bank has a detailed description of its forward-looking capital plan and whether sufficient capital is in place to satisfy the respective capital requirements. The report looks into the economic perspective of capital, where it comprises internal ratios calculated by the Bank on current financial results. The Bank's material risks with potential to cause material economic losses and deplete internal capital are accounted for. For the ICAAP document under the Economic Perspective, CRR 3 figures were taken into account as the starting point comparative against the internal model estimations. Despite that CRR III has been implemented on 1 January 2025, thereby being after the reference date for this document, it was noted that using the CRR 3 regulatory components would deem more beneficial as it provides a true and fair view of the outcomes, especially due to the forward-looking nature of the ICAAP report. To this extent, the Bank presented CRR2, CRR 3 and internal calculations and compared the latter two in order to arrive to the economic capital. The economic capital is the result of the maximum between the CRR 3 capital requirements under the economic perspective and the capital requirements based on the Bank's internal estimates prepared as part of this ICAAP. This result is compared with the Bank 's TSCR to seek the following: Whether sufficient capital to satisfy the capital requirements under the economic perspective is in place, and if additional capital requirements over and above the P2R are deemed necessary.

Row number	Explanation
	ILAAP The objective of the ILAAP is to ensure the survival of the Bank by ensuring the maintenance of sufficient counterbalancing capacity and stable funding to bear material liquidity and funding risks and cover net liquidity outflows under an adverse and extreme scenario. In line with the ECB Guide to the ILAAP, the Bank implements an economic perspective by assessing whether it has enough liquidity to cover all its material liquidity risks. The Bank simulates a survival period assessment by utilising the methodology prescribed under the ECB's 'Sensitivity analysis of Liquidity Risk – Stress Test' of February 2019 ("ECB Sensitivity Analysis"). This methodology requires the utilisation of static reference data, by contractual maturity, as at the applicable reference data, and thus, no forecasts arising from the generation of new business, such as the issuance of new loans or the generation of new customers deposit funding, can be simulated as part of the exercise. The Bank's survival period is determined based on the first maturity bucket in which its net liquidity position turns negative, being the point at which the Bank would have depleted all of its available liquidity. The Bank also compares the derived results with the median survival period of EU Banks. ***Stress Testing*** The Bank's stress scenarios are designed to be severe, but plausible, and relevant to the vulnerabilities of the Bank's business model, also in accordance with the EBA 2025 supervisory stress testing methodology. In this respect, the Bank considers the following adverse scenarios as most relevant at the time of preparation of this document: ***Aggravation of geopolitical tensions in Eastern Europe and the Middle East ('the market-wide scenario')*** As a base case scenario, the Bank assumes a static balance sheet approach. In line with the EBA 2025 supervisory stress testing methodology, the Bank's RWAs for the starting point (December 2024) are calculated under CRR 3. The elements stressed reduction in Net Interest Margin (NIM), increase in Credit Losses, decline in market value of investments, operational losses and higher administrative expenses ***A cyber-attack on the Bank ('the idiosyncratic scenario')*** The scenario assumes a cyber attack on the Bank's IT systems through spear phishing leading. The impact of this attack including potential lossess are simulated accordingly ***Climate risk disorderly transition*** This scenario assumes the aggravation of the economic situation being due climate polices across economic sectors being delayed or divergent, transitioning away from fossil fuels and carbon-intensive production and consumption requires significant shift towards emissions-neutral alternatives in all sectors, policy-makers increasing the implicit cost of emissions and higher costs. The scenario also assume that the Paris targets are met by the end of the century, although at higher economic costs. As a result of all the above, climate-related variables are shocked in 2024 due to a sudden, disorderly change in policy stance in the context of the NGFS disorderly change in policy stance. Frontloading approach was adopted, whereby the longer-term effects transition risk is assumed to take place in the first year of stress.

Row number	Explanation
	Reverse stress testing In accordance with the EBA Guidelines, the Bank conducted reverse stress testing (RST). The primary objective of reverse stress testing is to evaluate the viability and sustainability of the Bank's business model and strategy, as well as to identify scenarios in which the institution may face failure or become likely to fail. In this regard, the Bank creates scenarios that could breach its regulatory ratios. This contrasts with traditional stress testing, which primarily assesses whether the Bank maintains sufficient capital and liquidity buffers. The Bank performed a liquidity and a capital reverse stress testing. The Bank sets the time horizon used for the liquidity reverse stress testing between one to three months for all scenarios which is based on the BIS document published on "Supervisory and bank stress testing: range of practices". Key considerations for the capital scenario include, the dependency on a specifc customer, 0% interest rate environment, and Economic downturn in Euro Area.

Row number	Explanation
(b)	The following section provides a summary of the results included in the Bank's ICAAP and ILAAP suite of documents. **ICAAP** The Bank has sufficient capital to satisfy the capital requirements arising from its economic risks. The internal analysis shows that the Bank has sufficient capital to satisfy the capital requirements under the economic perspective, no capital add-on to the P2R is deemed necessary. **ILAAP** The Bank does not only have sufficient liquidity to cover its liquidity risks but also fares better than the median survival period of EU Banks under all stress scenarios (adverse and extreme). Therefore, the Bank does not require any additional liquidity buffer under the economic perspective. **Stress testing - the Market-wide scenario** Under stress, the Bank's total capital ratio decreases, but not enough to breach the Total SREP Capital Requirement (TSCR). The same applies for the Leverage Ratio, as well as the Liquidity Coverage Ratio (LCR), and Net Stable Funding Ratio (NSFR), all of which were not breached under periods of aggravation of geopolitical tensions. **Stress testing - the Idiosyncratic scenario** All the key regulatory metrics, namely the Capital Adequacy Ratio, Leverage ratio, Liquidity Coverage Ratio, and Net Stable Funding Ratio, were not breached following the presented Idiosyncratic Scenario stresses. **Stress testing - the climate risk scenario** No material impact was noted from this stress scenario, implying that the Bank can absorb any stress outlined from the climate risks mentioned above without breaching any Capital or Liquidity regulatory thresholds. **Reverse stress testing** From a Capital point of view, the potential loss of business from a product line of the Bank does not alone pose an immediate risk to the Bank's regulatory capital ratios over the next three years. The Bank has enough capital buffer to withstand such an event. Hower when including a zero rate enviroment, or a market wide shock or all scenarios together, this results into a breach in the TSCR in the second and third year of the projected period. Overall, the Bank believes its internal controls including capital monitoring, revenue diversification, and stress testing measures are sufficient to manage these risks.

REMUNERATION POLICY

The BoD approves and oversees remuneration, including responsibility for identifying and approving staff whose professional activities have or may have a material impact on the Bank's Risk profile (the Identified Staff). Further to this, the BoD reviews and approves the Remuneration Policy of the Bank. Therefore, their mandate comprises the selection of such Identified Staff as well as the actual remuneration policy that will be applied to such staff.

The Remuneration policy to be changed to Policy throughout this paragraph for Identified Staff is designed to ensure that the Bank's remuneration structure is consistent with and promotes sound and effective risk management, discourages the targeting of short-term gains at the expense of long-term goals, and prevents the fostering of a culture where excessive risk taking is practiced.

The Policy includes provisions in terms of fixed and variable remuneration and the Board oversees such process. In case of incentives, those are always subject to the staff's performance within their function and also the Bank's performance. The BoD is committed to review the Remuneration Policy on a yearly basis.

Regarding risk-control functions, such functions are assessed on their success in developing appropriate policies, effective risk management controls and procedures, amongst other factors.

Recommendations regarding fixed and variable remuneration of identified staff are always presented to the Bank's Risk Committee to examine whether any incentives consider risk, capital, liquidity and likelihood and timing of earnings.

1 . Variable remuneration, in the form of performance-based bonuses, is awarded in the year following the performance period only after the financial statements have been audited. While no formal multi-year deferral policy or vesting schedule is in place, this delay introduces a limited deferral element. Bonuses are paid in full once awarded and are not subject to claw back or performance-based vesting beyond initial approval.
2 . The Bank does not operate a formalised individual ratio between fixed and variable remuneration, as variable remuneration is awarded on a discretionary basis and remains low relative to fixed pay. This limits the total variable remuneration awarded across the Bank, ensuring that such remuneration remains proportionate and does not incentivise undue risk-taking. In all cases, variable remuneration remains a small portion of total staff remuneration and does not exceed 100% of fixed remuneration for any staff member.
3. Bonuses are awarded based on the performance of the Bank during the previous financial year. Criteria include profitability, achievement of strategic objectives, and compliance with regulatory obligations. No remuneration is awarded solely on short-term financial gains, and overall/individual qualitative factors are also considered.
4. The Bank operates as a single establishment and does not have distinct profit centres that are separately reportable. Accordingly, remuneration is disclosed in aggregate form and is not broken down by business area, as such segmentation would not be meaningful or reflective of the Bank's operational structure.
5. During the period 2024, variable remuneration was awarded in the form of performance bonuses, totalling EUR 155,000. No severance payments were made during the reporting period. No deferred remuneration applies beyond the timing of bonus award being after approval of the financial statements.

The remuneration paid during the current period to the executive directors, whose actions have a material impact on the risk profile of the Bank was EUR 212,539 (2023: EUR 196,919). Directors' fees paid to non-executive directors during the period for the Bank were EUR 593,160 (2023: EUR 392,735).

INTERNAL AUDIT

During the financial year ended on 31 December 2024, the Bank continued its internal audit program which is outsourced to an independent professional services firm. The internal audit supports and reports to the Bank's Audit Committee by independently assessing the effectiveness of the Bank's system of internal controls and ensuring compliance with statutory, legal and regulatory requirements. The Audit Committee approves the internal auditors' audit programs, analyses and reviews the audit findings and follows up on the implementation of changes and improvements in controls and procedures resulting from the internal auditors' findings. Accordingly, all key issues raised by the internal audit are communicated through the Audit Committee to the management responsible from the risk and control areas.

Internal audit has unrestricted access to all accounts, books and records and is provided with all information and data needed to fulfil its duties. Coordination and close cooperation with the external auditors are important to enhance the efficiency of the internal auditor's work.

SHARES AND CAPITAL INSTRUMENTS

Shares

The majority of Tier 1 capital comprises ordinary share capital attributed to Lidion Holdings plc, a Maltese public limited liability company bearing company registration number C-57008. As at 31 December 2024, total equity as reported in the financial statements of the Bank amounted to 23,072,943 (2023: EUR 13,717,876). This serves as the basis for determining the regulatory eligible Tier 1 capital adjusted for regulatory deductions, and was represented by a total of EUR 8,616,433 (2023: EUR 8,616,433) ordinary issued share capital, shareholders' advances of EUR 13,118,088 (2023: EUR 6,458,036) and retained earnings of EUR 1,771,770 (2023 loss: EUR 923,245) and non-distributable reserves of EUR 433,348 (2023: EUR 433,348).

Capital Instruments

Additional Tier 1 capital

Additional Tier 1 instruments are perpetual instruments which can only be redeemed if they are called by the issuer. If such a call is not exercised at the respective call date, the terms might include a change from fixed to floating coupon payments and, in the case of innovative instruments only, a limited step-up of the interest rate. Non-innovative instruments do not have a step-up of the interest rate and are therefore viewed as having a higher equity characteristic for regulatory capital purposes.

As at 31 December 2024, the Bank had not issued any hybrid instruments.

Tier 2 capital

During the year ended 31 December 2024, the Bank had paid back the subordinated debt which was present in 2023 of EUR 1,684,000 which instrument qualified as a Tier 2. The amount of subordinated debt which qualifies as Tier 2 is equivalent to EUR nil (2023: EUR 336,800).

Distributions to shareholders

From its inception, Lidion Bank never paid any dividend to shareholders registered as of the date of the AGM (the record date).

Any payment of dividend would be dependent on the Bank's targeted capital ratios and cash flow generation.

The Board of Directors provides its recommendation on whether a dividend payment to the shareholders is to be made. However, it is the shareholders at the Annual General Meeting who finally decide on the payment of a dividend or otherwise.

For the period ended 31 December 2024, no dividend was paid to Lidion Holdings plc.

Lidion Bank

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