

Keeping the

Spirit

CARD SME Bank, Inc.
Annual Report 2013





Our Vision

CARD SME Bank, Inc. envisions building a sustainable financial and capacity building institution owned and led by socially-and-economically challenged families by providing integrated Microfinance, Small and Medium Enterprise (MSME) and social development (credit with education, leadership with a heart, innovative community programs) services to an expanding membership base by organizing and empowering women and their families; and continue upholding the highest standards of stewardship of financial, human and institutional resources.

Our Objectives

As a member of CARD MRI, CARD SME Bank, Inc.'s objectives are likewise aligned with the group which is to provide a holistic approach to poverty eradication by:

- Continuously assisting the matured clients of CARD micro-entrepreneurs whose financial needs are beyond microfinance product lines through provision of bigger capital with longer and flexible repayment terms, savings as well as other products and services that will help sustain and expand on-going businesses;
- Identifying, recruiting and supporting new-to-CARD SMEs that are not currently being adequately served by other financial institutions; and
- Assisting microentrepreneurs who show potential to fast track their growth through the provision of higher level of microfinance funding.

About the Cover

The strongest and most united groups rise to the highest levels of performance. This is what we aim for our institution. CARD SME Bank's team spirit brings energy and passion as we create our distinct mark and pursue our vision and mission. The cover photo represents our nurturing culture and supportive team. Our encouraging stance allows us to stay focused on the big picture despite the challenges ahead.



The President's Report

CARD SME Bank, Inc. has been steadily growing for the last few years. Our team is working hard to ensure that we will be the bank of choice for small and medium enterprises. We can do this if we make our institution more accessible and familiar to our target clients.

This year, we faced the challenge of competing with bigger banks in the SME lending business but we managed to grow the number of our clients served by 51 percent. We served a total of 177,078 clients in 2013 from 116,629 clients in 2012, coupled with an increase in loan disbursed to PhP 2,636,481,474 in 2013 from PhP 1,670,394,000 in 2012. We also re-structured our organization in order for us to strengthen our focus and our capability to compete in the market.

We are glad to present to you what we have achieved in 2013:

Performance Indicators as of December 2013	
Number of total clients served	177,078
Number of clients including savers	170,560
Number of active clients with loans	99,553
Amount of loans disbursed	PhP 2,636,481,474
Amount of loans outstanding	PhP 908,414,813
Amount of savings	PhP 828,455,067
Repayment rate	98.84%
PAR 1 rate	2.26%

Moving on to 2014 and the years ahead, challenges are tougher as all other banks are gearing up for the 2015 ASEAN Integration and I believe that we are ready to face these challenges. Our team's capacity to deliver our commitment will be a force to reckon with.



Mary Jane A. Perreras
President and CEO

Making a mark

Right from the beginning, our institution aspires to make a distinct mark in the banking industry. In 2013, we embarked on several initiatives reinforcing our core competence as a full-service thrift bank providing our customers deposit products: savings, checking and time deposit accounts, as well as business and consumer loans. Apart from these products, we still continue to do our part, being one of the institutions under CARD MRI, in nation building by delivering microfinance loans to less fortunate members who want to gain financial freedom.

One of the initiatives in 2013 was the introduction of two loan products to fill the void in the housing and agricultural financing requirements in the CALABARZON region and other nearby cities and municipalities. First, The Bahay Katuparan Loan was launched during the same year. A loan program designed, with our customers in mind, providing an affordable and hassle-free application housing loan facility. To support this program and establish a one-stop shop for our customers, we have formed an alliance with Bella Vita Land Corporation, an Ayala-owned real estate developer that develops and constructs socialized and economic housing projects, to give our customers access to low-cost, quality and beautifully designed houses.



Second, in cooperation with International Finance Corporation or IFC, the Agri-finance loan facility was launched later in the year in response to the increasing need for funding assistance of farmers in the Agri-Agra sector, which is neglected by bigger banks and other lending institutions. Our Agri-finance loan aims to support farmers to maintain and ultimately increase their crop production every year.

In support of our existing and newly developed products, another initiative taken was the reorganization among the ranks as well as in the middle management level. This aims to streamline processes, without compromising accuracy and expediency, and deliver timely and relevant services to our customers.

Although a lot has been done in 2013 to strengthen and improve our position, we will not stop there. We will remain focused and strive to make our mark in the banking industry. We will continue to be relentless in 2014 and the years to come as we face the ever-evolving challenges ahead.

Pursuing excellence

As we value education and competence among our personnel, we are pleased to report six of our staff who recently gained their Master's Degree. Jeffrey Rondina graduated from the Asian Institute of Management (AIM), while Allan D. Dimaano, Maritess Angara, Rosella Sansano, Eva Mandalihan and Catalino del Mundo graduated from the Development Academy of the Philippines (DAP).





Organizations We Work With

PARTNERSHIP/COLLABORATION

Agricultural Guarantee Fund Pool
 ANR Cooperative
 Banco de Oro
 Bank of the Philippine Islands (BPI)
 Bank of the Philippine Islands and Mitsui Sumitomo Insurance (BPI/MS)
 BPI Globe Banko
 ChinaBank Savings
 Development Bank of the Philippines (DBP)
 German Savings Bank Foundation, Germany
 Landbank of the Philippines
 Maybank
 Metro Commercial & Industrial Services Corporation
 Metropolitan Bank & Trust Corporation (MBTC)
 Planters Development Bank
 PS Bank
 Rizal Commercial Banking Corporation
 Rocking Moon Foundation
 Rural Bank of Lobo, Inc.
 Rural Bank of Talisay, Inc.
 Savings Bank Foundation for International Cooperation (SBFIC), Germany
 Security Bank

SGV & Co.
 Small Business Corporation
 Sparkasse Essen, Germany
 Triple A Security Agency Incorporation
 Union Bank of the Philippines
 United Coconut Planters Bank
 Bellavita Land Corporation
 International Finance Corporation
 Social Security System
 Sparkassen International Development Trust (SIDT)
 Sparkasse Rothenburg

REGULATORY BODIES

Bangko Sentral ng Pilipinas (BSP)
 Philippine Deposit Insurance Corporation (PDIC)

AFFILIATIONS

Bankers Institute of the Philippines, Inc. (BAIPHIL)
 BAP Credit Bureau
 Chambers of Commerce, San Pablo Chapter
 Chamber of Thrift Banks
 Micro Finance Data Sharing (MIDAS)
 San Pablo Bankers' Association



Our Areas of Coverage

Head Office: San Pablo City, Laguna

Sto. Tomas Branch: Sto. Tomas, Batangas | Tanauan City | Malvar | Laurel | Talisay

Lipa Branch: Lipa City | Mataas na Kahoy | Balete | Ibaan | Padre Garcia | Rosario | Cuenca | San Jose

Tagaytay Branch: Tagaytay City, Cavite | Silang | GMA | Mendez | Naic | Indang | Alfonso | Tanza | Maragondon

Batangas Branch: Batangas City | Lobo | Bauan | San Pascual | Lemery | Taal | Sta. Teresita

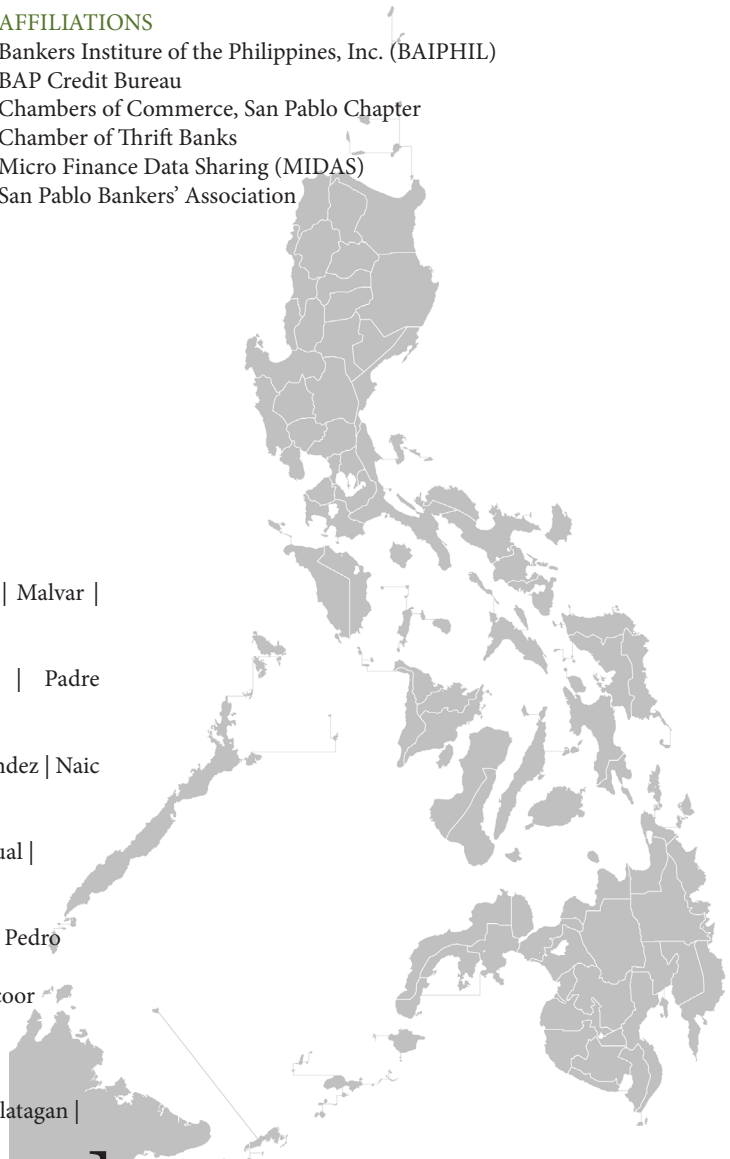
Sta. Rosa Branch: Sta. Rosa, Laguna | Cabuyao | Biñan | San Pedro

Cavite Branch: Cavite City | Noveleta | Kawit | Rosario | Bacoor

Calamba Branch: Calamba City

Balayan Branch: Balayan, Batangas | Agoncillo | Calaca | Calatagan | San Luis | Lian | Nasugbu | Tuy

Dasmariñas Branch: Dasmariñas, Cavite | Imus | Trese Martires | General Trias





Our Team



The Management Committee

Mary Jane A. Perreras
President and CEO

Cynthia B. Baldeo
Executive Vice President and COO

Cherry A. Boncajes
Assistant Vice President - Operations

Anna Lorraine J. Maur
Assistant Vice President - Finance

Ronald A. Inciong
Assistant Vice President - Credit Risk

Dennis O. Dimaculangan
Assistant Vice President -
Account Management Group

Manolo M. Martinez
Assistant Vice President -
Marketing and Product Development

Allan D. Dimaano
Senior Program Manager

Angela A. Poonin
Senior Personnel Manager

Mary Ann C. Resplandor
Assistant General Accounting Manager

Anna Therese A. de Leon
Internal Audit Manager

Jeffrey M. Rondina
Chief Compliance Officer

Peter C. Pasia
Legal Officer

Jerry V. Montejo
Regional Director

Noralyn D. Silvestre
Regional Director

Joy G. Palomique
Regional Director

Anita F. Rapera
Regional Director

Ross Meinard C. Ramos
IT Head

Eduardo L. Dimaano, Jr.
Information Security Officer



Board of Directors

Jaime Aristotle B. Alip, Ph.D.
Chairman

Flordeliza L. Sarmiento
Vice Chairperson

Milagros C. Rojas
Treasurer

Mary Jane A. Perreras
Member

Elma B. Valenzuela
Member

Ma. Elena M. Ruiz
Member

Gloria R. Estrellado
Independent Member

Dr. Gilbert M. Llanto
Independent Member

Atty. Wilfredo B. Domo-ong
Independent Member



Branch Opening

To make our products and services accessible to our clients, we added three more branches in Calamba, Laguna, Balayan, Batangas, and Dasmariñas, Cavite.





Feeding Program

To promote the importance of good nutrition, we organized feeding programs for our members' children.





 **Partnership with other organizations**

To further improve our products and services to respond to the different needs of our clients, we partnered with International Finance Corporation (IFC), Social Security System (SSS), BellaVita Land Corporation and Sparkassen International Development Trust (SIDT) this year.



Sportsfest

To promote camaraderie and the importance of an active lifestyle, a sportsfest was held for CARD SME Bank, Inc. staff.





Capacity Building and Exposure Trip

To enhance and strengthen the capabilities of our staff, we support their aspirations in acquiring a post-graduate degree. Some of our staff were also sent to exposure trips abroad to learn more about the different practices that can be adopted by our bank.





Financial Statements

CARD SME BANK, INC., A THRIFT BANK
STATEMENTS OF FINANCIAL POSITION

	December 31, 2013	December 31, 2012 (As restated - Notes 2 and 25)	January 1, 2012 (As restated - Notes 2 and 25)
ASSETS			
Cash and Other Cash Items (Note 6)	₱4,610,455	₱2,903,536	₱16,409,109
Due from Bangko Sentral ng Pilipinas (Notes 6 and 14)	50,603,710	31,379,001	14,646,774
Due from Other Banks (Note 6)	83,462,403	74,480,762	80,910,070
Available-for-Sale Investments (Note 7)	–	8,000,000	9,435,558
Held-to-Maturity Investments (Note 8)	26,078,103	26,236,233	26,279,591
Loans and Receivables (Note 9)	910,974,414	556,271,170	365,754,041
Property and Equipment (Note 10)	37,667,311	31,705,794	8,136,577
Investment Properties (Note 11)	10,205,436	16,188,218	21,671,491
Assets Held by Special Purpose Vehicle (Note 12)	4,371,336	5,882,554	5,882,554
Deferred Tax Assets - net (Note 20)	25,418,282	24,410,765	8,853,469
Other Assets (Note 13)	10,581,226	7,009,734	4,018,813
TOTAL ASSETS	₱1,163,972,676	₱784,467,767	₱561,998,047
LIABILITIES AND EQUITY			
Liabilities			
Deposit Liabilities (Notes 14 and 21)			
Demand	₱441,307	₱730,357	₱733,577
Savings	828,013,759	501,698,935	321,157,151
	828,455,066	502,429,292	321,890,728
Bills Payable (Note 15)	–	26,476,877	65,389,307
Income Tax Payable (Note 20)	10,305,392	4,577,903	4,844,812
Retirement Liability (Note 19)	29,089,823	45,991,003	26,361,595
Other Liabilities (Note 16)	28,389,523	16,930,853	16,753,933
	896,239,804	596,405,928	435,240,375
Equity			
Common Stock (Note 18)	251,019,938	215,513,825	161,008,400
Surplus (Deficit)	41,823,625	6,811,910	(20,115,552)
Net Unrealized Gain on Available-for-Sale Investments (Note 7)	–	–	890,650
Remeasurement Loss on Retirement Plan (Note 19)	(25,110,691)	(34,263,896)	(15,025,826)
	267,732,872	188,061,839	126,757,672
TOTAL LIABILITIES AND EQUITY	₱1,163,972,676	₱784,467,767	₱561,998,047

See accompanying Notes to Financial Statements.

CARD SME BANK, INC., A THRIFT BANK
STATEMENTS OF INCOME

	Years Ended December 31	
		2012
		(As restated -
	2013	Notes 2 and 25)
INTEREST INCOME ON		
Loans and receivables (Note 9)	₱346,292,876	₱220,242,016
Due from BSP and other banks (Note 6)	2,411,461	5,965,055
Investments securities (Note 8)	1,688,598	1,504,322
	350,392,935	227,711,393
INTEREST EXPENSE ON		
Deposit liabilities (Notes 14 and 21)	18,694,433	16,907,099
Bills payable (Note 15)	39,755	2,745,787
Others	58,880	—
	18,793,068	19,652,886
NET INTEREST INCOME	331,599,867	208,058,507
OTHER INCOME		
Gain on initial recognition of investment properties (Note 11)	1,142,321	1,700,035
Gain (loss) on sale of assets - net (Notes 10, 11 and 12)	(1,901,246)	121,489
Dividend income	200,000	200,000
Loan fees, service fees and penalties	16,040	41,435
Miscellaneous	1,872,854	1,854,319
TOTAL OPERATING INCOME	332,929,836	211,975,785
OPERATING EXPENSES		
Compensation and fringe benefits (Notes 19 and 21)	126,380,839	77,714,446
Transportation and travel (Note 21)	20,865,086	13,664,104
Taxes and licenses (Note 27)	20,100,917	13,236,031
Stationery and office supplies	13,051,048	8,720,514
Occupancy (Notes 21 and 22)	12,843,986	7,638,548
Provision for credit and impairment losses (Notes 9, 11 and 12)	11,882,068	8,380,619
Meetings and seminars (Note 21)	11,408,788	9,739,107
Employee trainings (Note 21)	10,589,404	8,985,844
Depreciation and amortization (Notes 10 and 11)	8,438,281	5,642,611
Information technology (Note 21)	5,901,205	6,571,913
Security, messengerial and janitorial	5,432,429	3,963,614
Insurance	4,475,760	3,917,331
Repairs and maintenance	3,671,091	2,282,807
Power, light and water	3,051,621	2,035,325
Representation and entertainment	2,940,466	2,181,218
Postage, telephone and cable	2,040,029	1,530,385
Professional fees	1,673,142	968,740
Fines, penalties & other charges	1,502,438	—
Program monitoring	1,288,229	646,308
Miscellaneous (Note 11)	5,682,512	2,971,278
TOTAL OPERATING EXPENSES	273,219,339	180,790,743
INCOME BEFORE INCOME TAX	59,710,497	31,185,042
PROVISION FOR INCOME TAX (Note 20)	18,643,593	4,257,580
NET INCOME	₱41,066,904	₱26,927,462

See accompanying Notes to Financial Statements.

CARD SME BANK, INC., A THRIFT BANK
STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31	
		2012
	2013	(As restated - Notes 2 and 25)
NET INCOME	₱41,066,904	₱26,927,462
OTHER COMPREHENSIVE INCOME (LOSS)		
Other comprehensive loss to be reclassified to profit or loss in subsequent periods:		
Changes in unrealized loss on available-for-sale investments (Note 7)	—	(890,650)
Other comprehensive gain (loss) not to be classified to profit or loss in subsequent periods:		
Gain (loss) on remeasurement of retirement plan (Note 19)	13,076,008	(27,482,957)
	13,076,008	(28,373,607)
Income tax relating to the components of other comprehensive income	(3,922,803)	8,244,887
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX	9,153,205	(20,128,720)
TOTAL COMPREHENSIVE INCOME	₱50,220,109	₱6,798,742

See accompanying Notes to Financial Statements.

CARD SME BANK, INC., A THRIFT BANK

STATEMENTS OF CHANGES IN EQUITY

	Common Stock (Note 18)	Surplus/ Deficit	Unrealized Gain (Loss) on Available-for- Sale Investments (Note 7)	Remeasurement Gain (Loss) on Retirement (Note 19)	Total
Balance at January 1, 2013, as previously reported	₱215,513,825	₱5,757,125	₱–	₱–	₱221,270,950
Effect of retrospective application of PAS 19 (Revised) - Notes 2 and 25	–	1,054,785	–	(34,263,896)	(33,209,111)
Balance at January 1, 2013, as Restated	215,513,825	6,811,910	–	(34,263,896)	188,061,839
Collection of subscriptions Receivable	35,506,113	–	–	–	35,506,113
Total comprehensive income for the year	–	41,066,904	–	9,153,205	50,220,109
Cash dividends declared and paid	–	(6,055,189)	–	–	(6,055,189)
Balance at December 31, 2013	₱251,019,938	₱41,823,625	₱–	(25,110,691)	₱267,732,872
Balance at January 1, 2012, as previously reported	₱161,008,400	(₱19,522,372)	₱890,650	₱–	₱142,376,678
Effect of retrospective application of PAS 19 (Revised) - Notes 2 and 25	–	(593,180)	–	(15,025,826)	(15,619,006)
Balance at January 1, 2012, as Restated	161,008,400	(20,115,552)	890,650	(15,025,826)	126,757,672
Collection of subscriptions Receivable	54,505,425	–	–	–	54,505,425
Total comprehensive income for the year	–	26,927,462	(890,650)	(19,238,070)	6,798,742
Balance at December 31, 2012	₱215,513,825	₱6,811,910	₱–	(₱34,263,896)	₱188,061,839

See accompanying Notes to Financial Statements.

CARD SME BANK, INC., A THRIFT BANK
STATEMENTS OF CASH FLOWS

	Years Ended December 31	
		2012
		(As restated -
	2013	Notes 2 and 25)
CASH FLOWS FROM OPERATING ACTIVITIES		
Income before income tax	₱59,710,497	₱31,185,042
Adjustments for:		
Retirement expense (Note 19)	17,867,608	8,451,893
Provision for credit and impairment losses (Notes 9, 11 and 12)	11,882,068	8,380,619
Depreciation and amortization (Notes 10 and 11)	8,438,281	5,642,611
Loss (gain) on sale of assets	3,092,194	(121,489)
Amortization of premium of held-to-maturity (HTM) investments	158,130	43,358
Fair value gain on initial recognition of investment properties (Note 11)	(1,142,321)	(1,700,035)
Gain on sale of asset held by special purpose vehicle	(1,190,948)	—
Changes in operating assets and liabilities:		
Increase in the amounts of:		
Loans and receivables	(344,132,661)	(198,937,840)
Deposit liabilities	326,025,774	180,538,564
Other assets	(3,571,492)	(2,990,921)
Other liabilities	11,454,605	176,920
Net cash generated from operations	88,591,735	30,668,722
Income taxes paid	(17,846,424)	(11,836,898)
Contributions to the retirement fund (Note 19)	(21,692,780)	(16,305,442)
Net cash provided by operating activities	49,052,531	2,526,382
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisitions of:		
Property and equipment (Note 10)	(14,315,760)	(25,360,233)
Unquoted debt securities (Note 9)	(20,000,000)	—
Proceeds from sale or maturities of:		
Investment properties (Note 11)	2,664,951	4,038,202
Assets held by special purpose vehicle	1,537,500	—
AFS investments	8,000,000	—
Net cash used in investing activities	(22,113,309)	(21,322,031)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash dividends paid	(6,055,189)	—
Availments of bills payable	—	65,000,000
Settlement of bills payable	(26,476,877)	(103,912,430)
Collections of subscriptions receivable (Note 18)	35,506,113	54,505,425
Net cash provided by financing activities	2,974,047	15,592,995

	Years Ended December 31	
		2012
		(As restated -
	2013	Notes 2 and 25)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	₱29,913,269	(₱3,202,654)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		
Cash and other cash items	2,903,536	16,409,109
Due from Bangko Sentral ng Pilipinas	31,379,001	14,646,774
Due from other banks	74,480,762	80,910,070
	108,763,299	111,965,953
CASH AND CASH EQUIVALENTS AT END OF YEAR		
Cash and other cash items	4,610,455	2,903,536
Due from Bangko Sentral ng Pilipinas	50,603,710	31,379,001
Due from other banks	83,462,403	74,480,762
	₱138,676,568	₱108,763,299
OPERATIONAL CASH FLOWS FROM INTEREST		
Interest received	₱347,558,820	₱228,313,179
Interest paid	18,898,519	18,788,456

See accompanying Notes to Financial Statements.

CARD SME BANK, INC., A THRIFT BANK

NOTES TO FINANCIAL STATEMENTS

1. Corporate Information

CARD SME Bank Inc., A Thrift Bank, [Formerly: Rural Bank of Sto. Tomas (Batangas), Inc.] (the Bank) was incorporated in the Philippines on October 4, 1961. The Bank was granted the authority to operate by the Bangko Sentral ng Pilipinas (BSP) on May 10, 1962. Its principal place of business is at #61 Insular Building, Rizal Avenue, San Pablo City, Laguna. The Bank offers a wide range of products and services such as deposit and loan products mainly to the consumer market.

In 2007, the Bank (with existing branches in Sto. Tomas, Batangas; Lipa City, Batangas; and Tagaytay City, Cavite) became a member of Center for Agriculture and Rural Development (CARD) – Mutually Reinforcing Institutions (MRI) when CARD, Inc. and CARD Employees' Multipurpose Cooperative, Inc. acquired the majority of its voting stock. The rehabilitation court and the BSP approved the sale and transfer of shares of stock on September 5, 2007 and February 7, 2008, respectively.

The Monetary Board, in its Resolution No. 1757 dated December 9, 2010, has approved the Bank's application for conversion into a regular thrift bank.

The BSP and Philippine Securities and Exchange Commission (SEC) approved on April 8, 2011 and May 11, 2011, respectively, the Bank's amended Articles of Incorporation (AOI) and new by-laws. The approved amendments to the Bank's AOI follow:

- a. Change of the corporate name from 'Rural Bank of Sto. Tomas (Batangas), Inc.' to 'CARD SME Bank, Inc., A Thrift Bank';
- b. Change of the primary and secondary purposes from that of rural banking to thrift banking;
- c. Change of the principal office address from 'General Malvar Avenue, Sto. Tomas, Batangas' to 'San Pablo City, Laguna'; and
- d. Extension of the Bank's corporate life for another fifty (50) years from the date of expiration on February 6, 2012.

The Bank was granted by the BSP the authority to operate as a thrift bank on June 15, 2011. On July 25, 2011, the Bank has formally started its operations as a thrift bank.

As a thrift bank, the Bank can now (1) provide short term working capital, medium and long-term financing, to business engaged in agricultural services, industry and housing; (2) provide diversified financial and allied services for its chosen market and constituents especially for small and medium enterprises, microfinance and individuals; and (3) carry on activities specified under Section 10 of Republic Act (RA) 7906, otherwise known as '*Thrift Banks Act of 1995*'.

In 2011, the BSP approved the conversion of its thirteen (13) existing Other Banking Offices (OBOs) into Micro-Banking Offices (MBOs) including the establishment of sixteen (16) additional MBOs. Likewise, three (3) branches (Batangas City, Sta. Rosa City and Cavite City) and four (4) MBOs were opened in 2012. Further, additional three (3) branches (Calamba City, Balayan and Dasmariñas) and forty-three (43) MBOs were opened in 2013.

2. Significant Accounting Policies

Basis of Preparation

The accompanying financial statements have been prepared on a historical cost basis, except for available-for-sale (AFS) investments which have been measured at fair value. The financial statements are presented in Philippine peso, the Bank's functional currency. All values are rounded to the nearest peso unless otherwise indicated.

The financial statements provide comparative information in respect of the previous period. In addition, the Bank presents an additional statement of financial position at the beginning of the earliest comparative period presented when there is a retrospective application of an accounting policy, a retrospective restatement, or a reclassification of items in the financial statements. An additional statement of financial position as at January 1, 2012 is presented in these financial statements due to retrospective application of certain accounting policies (Note 25).

Statement of Compliance

The financial statements of the Bank have been prepared in accordance with Philippine Financial Reporting Standards (PFRS).

Presentation of Financial Statements

The Bank presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery (asset) or settlement (liability) within 12 months after the reporting date (current) and more than 12 months after the reporting date (noncurrent) is presented in Note 17.

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position only when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or to realize the assets and settle the liability simultaneously. Income and expenses are not offset in the statement of income unless required or permitted by any accounting standard or interpretation and as specifically disclosed in the accounting policies of the Bank.

In prior years, the Bank presented a single statement of comprehensive income. Starting 2013, the Bank decided to separate the single statement into statement of income and statement of comprehensive income to give a clear and more relevant information to the users of the financial statements for the difference of profit or loss and other comprehensive income. The change in presentation has no impact to the financial position or performance of the Bank.

Changes in Accounting Policies and Disclosures

The Bank applied, for the first time, certain standards and amendments that require restatement of previous financial statements. Unless otherwise indicated, these new and revised accounting standards have no impact to the Bank. Except for these standards and amended PFRS which were adopted as at January 1, 2013, the accounting policies adopted are consistent with those of the previous financial year.

PFRS 7, Financial Instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities (Amendments)

These amendments require an entity to disclose information about rights of set-off and related arrangements (such as collateral agreements). The new disclosures are required for all recognized financial instruments that are set off in accordance with Philippine Accounting Standards (PAS) 32, *Financial Instruments: Presentation*. These disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or 'similar

agreement', irrespective of whether they are set-off in accordance with PAS 32. The amendments require entities to disclose, in a tabular format, unless another format is more appropriate, the following minimum quantitative information. This is presented separately for financial assets and financial liabilities recognized at the end of the reporting period:

- a) The gross amounts of those recognized financial assets and recognized financial liabilities;
- b) The amounts that are set off in accordance with the criteria in PAS 32 when determining the net amounts presented in the statement of financial position;
- c) The net amounts presented in the statement of financial position;
- d) The amounts subject to an enforceable master netting arrangement or similar agreement that are not otherwise included in (b) above, including:
 - i. Amounts related to recognized financial instruments that do not meet some or all of the offsetting criteria in PAS 32; and
 - ii. Amounts related to financial collateral (including cash collateral); and
- e) The net amount after deducting the amounts in (d) from the amounts in (c) above.

The amendments have no impact on the Bank's financial position or performance.

PFRS 13, Fair Value Measurement

PFRS 13 establishes a single source of guidance under PFRSs for all fair value measurements. PFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under PFRS. PFRS 13 defines fair value as an exit price. PFRS 13 also requires additional disclosures.

As a result of the guidance in PFRS 13, the Bank re-assessed its policies for measuring fair values, in particular, its valuation inputs such as non-performance risk for fair value measurement of liabilities. The Bank has assessed that the application of PFRS 13 has not materially impacted its fair value measurements. Additional disclosures, where required, are provided in the individual notes relating to the assets and liabilities whose fair values were determined. Fair value hierarchy is provided in Note 4.

PAS 1, Presentation of Financial Statements - Presentation of Items of Other Comprehensive Income or OCI (Amendments)

The amendments to PAS 1 introduced a grouping of items presented in OCI. Items that will be reclassified (or "recycled") to statements of income at a future point in time (for example, upon derecognition or settlement) will be presented separately from items that will never be recycled.

The amendments affect presentation only and have no impact on the Bank's financial position or performance.

PAS 19, Employee Benefits

On January 1, 2013, the Bank adopted the revised PAS 19.

For defined benefit plans, the revised PAS 19 requires all actuarial gains and losses to be recognized in other comprehensive income and unvested past service costs previously recognized over the average vesting period to be recognized immediately in profit or loss when incurred.

Prior to adoption of the revised PAS 19, the Bank recognized actuarial gains and losses as income or expense when the net cumulative unrecognized gains and losses for each individual plan at the end of the previous period exceeded 10.0% of the higher of the defined benefit obligation and the fair value of the plan assets and recognized unvested past service costs as an expense on a straight-

line basis over the average vesting period until the benefits become vested. Upon adoption of the revised PAS 19, the Bank changed its accounting policy to recognize all actuarial gains and losses in other comprehensive income and all past service costs in profit or loss in the period they occur.

The revised PAS 19 replaced the interest cost and expected return on plan assets with the concept of net interest on defined benefit liability or asset which is calculated by multiplying the net balance sheet defined benefit liability or asset by the discount rate used to measure the employee benefit obligation, each as at the beginning of the annual period.

The revised PAS 19 also amended the definition of short-term employee benefits and requires employee benefits to be classified as short-term based on expected timing of settlement rather than the employee's entitlement to the benefits. In addition, the revised PAS 19 modifies the timing of recognition for termination benefits. The modification requires the termination benefits to be recognized at the earlier of when the offer cannot be withdrawn or when the related restructuring costs are recognized.

Changes to definition of short-term employee benefits and timing of recognition for termination benefits do not have any impact to the Bank's financial position and financial performance.

The changes in accounting policies have been applied retrospectively. The effects of adoption on the financial statements are as follows:

	December 31, 2012	January 1, 2012
Increase (decrease) in:		
<u>Statements of financial position</u>		
Retirement asset	(₱1,450,585)	₱—
Retirement liability	45,991,003	22,312,866
Deferred tax asset	14,232,477	6,693,860
Remeasurement gain (loss) on retirement plan	(34,263,896)	(15,025,826)
Surplus	11,285,061	(593,180)
		<u>2012</u>
<u>Statements of income</u>		
Compensation and fringe benefits		(₱2,354,235)
Provision for income tax		<u>(706,271)</u>
Net income		(₱1,647,964)
<u>Statements of comprehensive income</u>		
Net income		(₱1,647,964)
Other comprehensive income:		
Remeasurement loss of defined benefit Obligation		<u>(19,238,070)</u>
Total comprehensive income for the year		<u><u>(₱20,886,034)</u></u>

The Bank obtained the services of an external actuary to compute the impact to the financial statements upon adoption of the standard. The Bank chose to close to 'Surplus' the net effect of all transition adjustments as at January 1, 2012 (the transition date) upon retrospective application of PAS 19 (Revised).

The adoption did not have an impact on the statement of cash flows.

The revised PAS 19 also requires more extensive disclosures. The required disclosures are presented in Note 19.

Annual Improvements to PFRS (2009-2011 cycle)

The *Annual Improvements to PFRS (2009-2011 cycle)* contain non-urgent but necessary amendments to PFRS. The Bank adopted these amendments for the current year.

PAS 1, Presentation of Financial Statements - Clarification of the requirements for comparative information

The amendments clarify the requirements for comparative information that are disclosed voluntarily and those that are mandatory due to retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the financial statements. An entity must include comparative information in the related notes to the financial statements when it voluntarily provides comparative information beyond the minimum required comparative period. The additional comparative period does not need to contain a complete set of financial statements. On the other hand, supporting notes for the third balance sheet (mandatory when there is a retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the financial statements) are not required. During the period, the Bank restated its 2012 and 2011 financial statements to effect the retrospective application of revised PAS 19 (Note 25). As a result, the Bank has not included comparative information in the notes to the financial statements in respect of the opening statement of financial position as at January 1, 2012.

PAS 16, Property, Plant and Equipment - Classification of servicing equipment

The amendment clarifies that spare parts, stand-by equipment and servicing equipment should be recognized as property, plant and equipment when they meet the definition of property, plant and equipment and should be recognized as inventory if otherwise. The amendment does not have any significant impact on the Bank's financial position or performance.

PAS 32, Financial Instruments: Presentation - Tax effect of distribution to holders of equity instruments

The amendment clarifies that income taxes relating to distributions to equity holders and to transaction costs of an equity transaction are accounted for in accordance with PAS 12, *Income Taxes*. The amendment does not have any significant impact on the Bank's financial position or performance.

Summary of Significant Accounting Policies

Foreign Currency Transactions

For financial reporting purposes, foreign currency-denominated monetary assets and liabilities are translated to Philippine peso based on the Philippine Dealing and Exchange Corporation (PDEx) closing rate prevailing at end of year, and foreign currency-denominated income and expenses at the rate at transaction date. Foreign exchange differences arising from restatements of foreign currency-denominated monetary assets and liabilities are credited to or charged against operations.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the initial transaction date. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.



Fair Value Measurement

The Bank measures financial instruments, such as derivatives, at fair value at each reporting date. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 4.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- in the principal market for the asset or liability, or
- in the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to by the Bank.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities in the absence of a principal market, in the most advantageous market for the asset or liability
- Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognized in the financial statements on a recurring basis, the Bank determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at every reporting date.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash and other cash items, amounts due from BSP and other banks that are convertible to known amounts of cash with original maturities of three months or less from dates of placements and that are subject to insignificant risk of changes in value.

Financial Instruments - Initial Recognition and Subsequent Measurement

Date of recognition

Purchases or sales of financial assets that require delivery of the assets within the time frame established by regulation or convention in the marketplace are recognized on the settlement date. Generally, settlement date is the date on which the transaction is settled by delivery of the assets that are subject of the agreement. Settlement date accounting refers to (a) the recognition of an asset on the day it is received by the Bank, and (b) the derecognition of an asset and recognition of any gain or loss on disposal on the day that such asset is delivered by the Bank. Deposits, amounts due from other banks and loans receivables are recognized when cash is received by the Bank or advanced to the borrowers.

Initial recognition of financial instruments

All financial instruments are initially measured at fair value. Except for financial assets and financial liabilities at fair value through profit or loss (FVPL), the initial measurement of financial assets and liabilities includes transaction costs. The Bank classifies its financial assets in the following categories: financial assets at FVPL, held-to-maturity (HTM) investments, AFS investments, and loans and receivables. The classification depends on the purpose for which the investments were acquired and whether they are quoted in an active market, and for HTM investments, the ability and intention to hold the investment until maturity. Management determines the classification of its investments at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date. Financial liabilities are classified into financial liabilities at FVPL and other financial liabilities at amortized cost.

As at December 31, 2013 and 2012, the Bank has no financial assets and financial liabilities at FVPL.

Determination of fair value

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Bank determines the policies and procedures for non-recurring measurement, such as investment properties. External valuers are involved for valuation of significant assets, such as investment properties. Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

'Day 1' difference

Where the transaction price in a non-active market is different from the fair value or from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the Bank recognizes the difference between the transaction price and fair value (a 'Day 1' difference) in the statement of income unless it qualifies for recognition as some other type of asset. In cases where data are not observable, the difference between the transaction price and model value is only recognized in the statement of income when the inputs become observable or when the instrument is derecognized. For each transaction, the Bank determines the appropriate method of recognizing the 'Day 1' difference amount.

HTM investments

HTM investments are quoted nonderivative financial assets with fixed or determinable payments and fixed maturities for which the Bank's management has the positive intention and ability to hold to maturity. After initial measurement, these investments are subsequently measured at amortized cost using the EIR method, less any impairment in value. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR. The amortization is included in 'Interest income' in the statement of income. The losses arising from impairment of such investments are recognized in the statement of income under 'Provision for credit and impairment losses'.

If the Bank sells more than an insignificant amount of HTM investments prior to maturity (other than in specific circumstances), the entire category would be tainted and reclassified as AFS investments. Furthermore, the Bank would be precluded from using the HTM investment category for the following two years.

Loans and receivables

This accounting policy relates to the statement of financial position captions 'Due from BSP', 'Due from other banks', and 'Loans and receivables'. These are nonderivative financial assets with fixed or determinable payments and fixed maturities that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as financial assets at FVPL or designated as AFS investments.

After initial measurement, loans and receivables are subsequently measured at amortized cost using the EIR method, less allowance for credit losses and unearned interest income. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortization is included in the 'Interest income' in the statement of income. The losses arising from impairment are recognized in 'Provision for credit and impairment losses' in the statement of income.

Other financial liabilities at amortized cost

This category represents issued financial instruments or their components, which are not designated at FVPL where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares. The components of issued financial instruments that contain both liability and equity elements are accounted for separately, with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component on the date of issue. The liabilities are classified under 'Deposit liabilities', 'Bills payable', or other appropriate financial liability accounts in the statement of financial position.

After initial measurement, financial liabilities not qualified as and not designated as FVPL, are subsequently measured at amortized cost using the EIR method. Amortized cost is calculated by taking into account any discount or premium on the issue and fees that are an integral part of the EIR.

Classification of Financial Instruments between Debt and Equity

A financial instrument is classified as debt if it provides for a contractual obligation to:

- deliver cash or another financial asset to another entity;
- exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Bank; or
- satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

If the Bank does not have an unconditional right to avoid delivering cash or another financial asset to settle its contractual obligation, the obligation meets the definition of a financial liability.

Derecognition of Financial Assets and Liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of financial assets) is derecognized when:

- the rights to receive cash flows from the asset have expired;
- the Bank retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a “pass-through” arrangement; or
- the Bank has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained the risk and rewards of the asset but has transferred the control over the asset.

Where the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control over the asset, the asset is recognized to the extent of the Bank’s continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Financial liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or has expired. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the statement of income.

Offsetting Financial Instruments

Financial assets and financial liabilities are only offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognized amounts and the Bank intends to either settle on a net basis, or to realize the asset and the liability simultaneously. This is not generally the case with master-netting agreements, and the related assets and liabilities are presented gross in the statement of financial position.

Impairment of Financial Assets

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets at amortized cost

For loans and receivables, due from BSP and other banks, and HTM investments which are carried at amortized cost, the Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses for impairment. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the counterparties' ability to pay all amounts due according to the contractual terms of the assets being evaluated. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment for impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of loss is charged to the statement of income. Financial assets at amortized cost, together with the associated allowance accounts, are written off when there is no realistic prospect of future recovery and all collateral has been realized. If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is reduced by adjusting the allowance account. If a future write-off is later recovered, any amounts formerly charged are credited to the 'Provision for credit and impairment losses' in the statement of income.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of such credit risk characteristics as industry, collateral type, past-due status and term. Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with changes in related observable data from period to period (such as changes in unemployment rates, property prices, payment status, or other factors that are indicative of incurred losses of the Bank and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

Restructured loans

Where possible, the Bank seeks to restructure loans, which may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews restructured loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original EIR. The difference between the recorded value of the original loan and the present value of the restructured cash flows, discounted at the original EIR, is recognized in 'Provision for credit and impairment losses' in the statement of income.

AFS investments

For AFS investments, the Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired.

In case of unquoted equity investments classified as 'AFS investments', the amount of the impairment is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses shall not be reversed.

In the case of debt instruments classified as AFS investments, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Future interest income is based on the reduced carrying amount and is accrued based on the rate of interest used to discount future cash flows for the purpose of measuring impairment loss. Such accrual is recorded as part of 'Interest income' in the statement of income. If subsequently, the fair value of a debt instrument increased and the increase can be objectively related to an event occurring after the impairment loss was recognized in the statement of income, the impairment loss is reversed through the statement of income.

In the case of equity investments classified as AFS investments, this would include a significant or prolonged decline in the fair value of the investments below its cost. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in the statement of income is removed from equity and recognized in the statement of income. Impairment losses on AFS investments are not reversed through the statement of income. Increases in fair value after impairment are recognized directly in other comprehensive income.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization and accumulated impairment losses, if any.

The initial cost of property and equipment consists of its purchase price, including taxes and any directly attributable costs to bring the asset to its working condition and location for its intended use. Expenditures incurred after items of property and equipment have been put into operation, such as repairs and maintenance are normally charged against operations in the period in which the costs are incurred. In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in the future economic benefits expected to be obtained from the use of an item property and equipment beyond its originally assessed standard of performance, the expenditures are capitalized as an additional cost of property and equipment.

Depreciation is computed using the straight-line method over the estimated useful lives of the respective assets. Leasehold improvements are amortized over the shorter of the estimated useful life of 5 years or the period of the lease agreement.



The estimated useful lives of the depreciable assets are as follows:

Furniture, fixtures and equipment	3 years
Leasehold improvements	3-5 years or the terms of the related leases, whichever is shorter
Transportation equipment	3-5 years
Building	5-15 years

The useful life and the depreciation and amortization method are reviewed periodically to ensure that the period and the method of depreciation and amortization are consistent with the expected pattern of economic benefits from items of property and equipment.

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of income in the year the asset is derecognized.

The carrying values of the property and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, an impairment loss is recognized under 'Provision for credit and impairment losses' in the statement of income.

Investment Properties

Investment properties are measured initially at cost, including transaction costs. An investment property acquired through an exchange transaction is measured at fair value of the asset acquired unless the fair value of such an asset cannot be measured in which case the investment property acquired is measured at the carrying amount of asset given up. Foreclosed properties are classified under 'Investment properties' upon either:

- entry of judgment in case of judicial foreclosure;
- execution of sheriff's certificate of sale in case of extra-judicial foreclosure; or
- notarization of the deed of dacion en payment in kind (dacion en pago).

The difference between the fair value of the asset acquired and the carrying amount of the asset given up is recognized under 'Gain on initial recognition of investment properties' in the statement of income.

Subsequent to initial recognition, investment properties are stated at cost less accumulated depreciation and accumulated impairment losses, if any.

Depreciation on buildings and improvements is calculated on a straight-line basis over the estimated useful life of ten years from the time of acquisition of the investment properties.

Investment properties are derecognized when they have either been disposed of or when the investment property is permanently withdrawn from use and no future benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognized in the statement of income in the period of retirement or disposal. Expenditures incurred after the investment properties have been put into operations, such as repairs and maintenance costs, are charged against income in the year in which the costs are incurred.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by cessation of owner-occupation or of construction or development, or commencement of an operating lease to another party. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale.

For transfers from investment property to owner-occupied property, the deemed cost of property for subsequent accounting is its depreciated cost at the date of change in use. If the property occupied by the Bank as an owner-occupied property becomes an investment property, the Bank accounts for such property in accordance with the policy stated under 'Property and equipment' up to the date of change in use.

Assets Held by Special Purpose Vehicle (SPV)

Assets held by SPV are recognized if the sale of the asset is highly probable, evidenced by the management's commitment to sell the asset. Assets held by SPV are carried at lower of cost less any impairment in value and net realizable value.

If an asset ceased to be classified as assets held by SPV, it shall be measured at the lower of its carrying amount before the asset was classified as such, adjusted for any depreciation, amortization or revaluations that would have been recognized had it not been classified as such, and its recoverable amount at the date of the subsequent decision not to sell. The Bank shall include any required adjustment to the carrying amount of an asset that ceases to be classified as asset held by SPV in the statement of income.

Impairment of Property and Equipment, Investment Properties and Assets Held by SPV

At each reporting date, the Bank assesses whether there is any indication that its property and equipment, investment properties, and assets held by SPV are impaired. When an indicator of impairment exists or when an annual impairment testing for an asset is required, the Bank makes a formal estimate of recoverable amount. Recoverable amount is the higher of an asset's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is assessed as part of the cash generating unit to which it belongs. Where the carrying amount of an asset exceeds its recoverable amount, the asset (or cash generating unit) is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is charged against operations in the year in which it arises.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation and amortization, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the statement of income. After such a reversal, the depreciation and amortization expense is adjusted in future years to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining life.

Equity

Common stock represents the aggregate amount of fully paid capital stock which is determined using the nominal or par value of shares that have been issued. When the shares are sold at a premium, the difference between the proceeds and par value is credited to 'Capital paid in excess of par value', net of direct costs incurred related to the equity issuance. If 'Capital paid in excess of par value' is not sufficient, the excess is charged against surplus.

Subscriptions receivable pertains to uncollected portion of subscribed stocks.

Surplus (deficit) represents the accumulative balance of periodic net income or loss, dividend contributions, prior period adjustments, effect of changes in accounting policy and other capital adjustments.

Own equity instruments which are reacquired (treasury stocks) are recognized at cost and deducted from equity. No gain or loss is recognized in the statement of income on the purchase, sale, issue or cancellation of the Bank's own equity instruments. Any difference between the carrying amount and the consideration, if reissued, is recognized in 'Capital paid in excess of par value'. Voting rights related to treasury stocks are nullified for the Bank and no dividends are allocated to them. When the stocks are retired, the 'Common stock' account is reduced by its par value and the excess of cost over par value upon retirement is debited to 'Capital paid in excess of par value' at the time the stocks were issued and to surplus for the remaining balance.

Revenue Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The Bank has assessed that it is acting as a principal (as opposed to as an agent) in all revenue arrangements. The following specific recognition criteria must also be met before the revenue is recognized:

Interest income

For all financial assets measured at amortized cost and interest-bearing instruments, interest income is recorded at the EIR, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options), includes any fees (such as service fees) or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses. The adjusted carrying amount is calculated based on the original EIR. The change in carrying amount is recorded as 'Interest income' in the statement of income.

Once the recorded value of a financial asset or group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the original EIR used to discount future cash flows.

'Unearned interest income' is recognized as income over the terms of the receivables using the EIR method and shown as deduction from loans.

Loan fees, service fees and penalties

Loan fees are recognized over the term of the credit lines granted to each borrower. Service fees are accrued when earned. Penalties are recognized only upon collection or where there is a reasonable degree of certainty as to their collectability.

Costs and Expenses

Costs and expenses encompass losses as well as those expenses that arise in the course of the ordinary activities of the Bank. Costs and expenses are recognized when incurred.

Retirement Benefits

The Bank operates a defined benefit retirement plan which requires contributions to be made to a separately administered fund.

The net defined benefit liability or asset is the aggregate of the present value of the defined benefit obligation at the end of the reporting period reduced by the fair value of plan assets (if any), adjusted for any effect of limiting a net defined benefit asset to the asset ceiling. The asset ceiling is the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

The cost of providing benefits under the defined benefit retirement plan is determined using the projected unit credit method.

Retirement costs comprise the following:

- Service cost
- Net interest on the net defined benefit liability or asset
- Remeasurements of net defined benefit liability or asset

Service costs which include current service costs, past service costs and gains or losses on non-routine settlements are recognized as expense in the statement of income. Past service costs are recognized when the plan amendment or curtailment occurs. These amounts are calculated periodically by independent qualified actuaries.

Net interest on the net defined benefit liability or asset is the change during the period in the net defined benefit liability or asset that arises from the passage of time which is determined by applying the discount rate based on government bonds to the net defined benefit liability or asset. Net interest on the net defined benefit liability or asset is recognized as expense or income in the statement of income.

Remeasurements, comprising of actuarial gains and losses, the effect of the asset ceiling, excluding net interest and the return on plan assets (excluding net interest), are recognized immediately in the statement of financial position with a corresponding debit or credit to 'Gain (loss) on remeasurement of retirement liability' under other comprehensive income in the period in which they occur. Remeasurements are not reclassified to the statement of income in subsequent periods.

Plan assets are assets that are held by a long-term employee benefit fund or qualifying insurance policies. Plan assets are not available to the creditors of the Bank, nor can they be paid directly to the Bank. Fair value of plan assets is based on market price information. When no market price is available, the fair value of plan assets is estimated by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets (or, if they have no maturity, the expected period until the settlement of the related obligations). If the fair value of the plan assets is higher than the present value of the defined benefit obligation, the measurement of the resulting defined benefit asset is limited to the present value of economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

The Bank's right to be reimbursed of some or all of the expenditure required to settle a defined benefit obligation is recognized as a separate asset at fair value when and only when reimbursement is virtually certain.

Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset. A reassessment is made after inception of the lease only if one of the following applies:

- a. There is a change in contractual terms, other than renewal or extension of the arrangement;
- b. A renewal option is exercised or extension granted, unless the term of the renewal or extension was initially included in the lease term;
- c. There is a change in the determination of whether fulfillment is dependent on a specified asset;
or
- d. There is a substantial change to the asset.

Where reassessment is made, lease accounting shall commence or cease from the date when the change in circumstances gave rise to the reassessment of the scenarios (a), (c) or (d) above, and at the date of renewal or extension period for scenario (b).

Bank as lessee

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as an expense under 'Occupancy' account in the statement of income on a straight-line basis over the lease term.

Income Taxes

Current tax

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted as at the reporting date.

Deferred tax

Deferred tax is provided, using the balance sheet liability method, on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognized for all taxable temporary differences with certain exceptions. Deferred tax assets are recognized for all deductible temporary differences, carryforward of unused tax credits from excess minimum corporate income tax (MCIT) over regular corporate income tax (RCIT), if any, and unused net operating loss carryover (NOLCO), if any, to the extent that it is probable that taxable income will be available against which the deductible temporary differences and carryforward of unused excess MCIT over RCIT and unused NOLCO can be utilized except:

- a. Where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

- b. In respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed as at reporting date and recognized to the extent that it has become probable that future taxable income will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are applicable to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Current tax and deferred tax relating to items recognized directly in equity is also recognized in equity and not in the statement of income.

Deferred tax assets and liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and deferred taxes related to the same taxable entity and the same taxation authority.

Provisions

Provisions are recognized when the Bank has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Bank expects some or all of a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the statement of income, net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an 'Interest expense' in the statement of income.

Related Party Relationships and Transactions

Related party relationship exists when one party has the ability to control, directly, or indirectly through one or more intermediaries, the other party or exercises significant influence over the other party in making financial and operating decisions. Such relationship also exists between and/or among entities which are under common control with the reporting enterprise, or between and/or among the enterprise and its key management personnel, directors, or its shareholders. In considering each possible related party relationship, attention is directed to the substance or the relationship, and not merely the legal form.

Contingent Liabilities and Contingent Assets

Contingent liabilities are not recognized in the financial statements but are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized but are disclosed in the financial statements when an inflow of economic benefits is probable.

Events After the Reporting Date

Post-year-end events that provide additional information about the Bank's position at the reporting date (adjusting events), are reflected in the financial statements. Post-year-end events that are not adjusting events, if any, are disclosed when material in the notes to the financial statements.

Future Changes in Accounting Policies

Standards issued but not yet effective up to date of issuance of the Bank's financial statements are listed below. The listing consists of standards and interpretations issued, which the Bank reasonably expects to be applicable at a future date. The Bank intends to adopt these standards when they become effective. Except as otherwise indicated, the Bank does not expect the adoption of these new and amended PFRS, PAS and Philippine Interpretations to have significant impact on its financial statements.

PAS 36, Impairment of Assets - Recoverable Amount Disclosures for Non-Financial Assets (Amendments)

These amendments remove the unintended consequences of PFRS 13 on the disclosures required under PAS 36. In addition, these amendments require disclosure of the recoverable amounts for the assets or cash-generating units (CGUs) for which impairment loss has been recognized or reversed during the period. These amendments are effective retrospectively for annual periods beginning on or after January 1, 2014 with earlier application permitted, provided PFRS 13 is also applied. The amendments affect disclosures only and have no impact on the Bank's financial position or performance.

Investment Entities (Amendments to PFRS 10, PFRS 12 and PAS 27)

These amendments are effective for annual periods beginning on or after January 1, 2014. They provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under PFRS 10. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss. It is not expected that this amendment would be relevant to the Bank.

Philippine Interpretation IFRIC 21, Levies (IFRIC 21)

IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated before the specified minimum threshold is reached. IFRIC 21 is effective for annual periods beginning on or after January 1, 2014. The Bank does not expect that IFRIC 21 will have material financial impact in future financial statements.

PAS 39, Financial Instruments: Recognition and Measurement - Novation of Derivatives and Continuation of Hedge Accounting (Amendments)

These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. These amendments are effective for annual periods beginning on or after January 1, 2014. The amendments have no impact on the Bank.

PAS 32, Financial Instruments: Presentation - Offsetting Financial Assets and Financial Liabilities (Amendments)

The amendments clarify the meaning of "currently has a legally enforceable right to set-off" and also clarify the application of the PAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. The amendments affect presentation only and have no impact on the Bank's financial performance. The amendments to PAS 32 are to be retrospectively applied for annual periods beginning on or after January 1, 2014.

PAS 19, *Employee Benefits - Defined Benefit Plans: Employee Contributions* (Amendments)
The amendments apply to contributions from employees or third parties to defined benefit plans. Contributions that are set out in the formal terms of the plan shall be accounted for as reductions to current service costs if they are linked to service or as part of the remeasurements of the net defined benefit asset or liability if they are not linked to service. Contributions that are discretionary shall be accounted for as reductions of current service cost upon payment of these contributions to the plans. The amendments to PAS 19 are to be retrospectively applied for annual periods beginning on or after July 1, 2014. The amendments have no impact on the Bank's financial position or performance.

Annual Improvements to PFRS (2010-2012 cycle)

The Annual Improvements to PFRS (2010-2012 cycle) contain non-urgent but necessary amendments to the following standards:

PFRS 2, Share-based Payment - Definition of Vesting Condition

The amendment revised the definitions of vesting condition and market condition and added the definitions of performance condition and service condition to clarify various issues. This amendment shall be prospectively applied to share-based payment transactions for which the grant date is on or after July 1, 2014. This amendment does not apply to the Bank as it has no share-based payments.

PFRS 3, Business Combinations - Accounting for Contingent Consideration in a Business Combination

The amendment clarifies that a contingent consideration that meets the definition of a financial instrument should be classified as a financial liability or as equity in accordance with PAS 32. Contingent consideration that is not classified as equity is subsequently measured at fair value through profit or loss whether or not it falls within the scope of PFRS 9 (or PAS 39, if PFRS 9 is not yet adopted). The amendment shall be prospectively applied to business combinations for which the acquisition date is on or after July 1, 2014. The Bank shall consider this amendment for future business combinations.

PFRS 8, Operating Segments - Aggregation of Operating Segments and Reconciliation of the Total of the Reportable Segments' Assets to the Entity's Assets

The amendments require entities to disclose the judgment made by management in aggregating two or more operating segments. This disclosure should include a brief description of the operating segments that have been aggregated in this way and the economic indicators that have been assessed in determining that the aggregated operating segments share similar economic characteristics. The amendments also clarify that an entity shall provide reconciliations of the total of the reportable segments' assets to the entity's assets if such amounts are regularly provided to the chief operating decision maker. These amendments are effective for annual periods beginning on or after July 1, 2014 and are applied retrospectively. The amendments have no impact on the Bank's financial position or performance.

PFRS 13, Fair Value Measurement - Short-term Receivables and Payables

The amendment clarifies that short-term receivables and payables with no stated interest rates can be held at invoice amounts when the effect of discounting is immaterial.

PAS 16, Property, Plant and Equipment - Revaluation Method - Proportionate Restatement of Accumulated Depreciation

The amendment clarifies that, upon revaluation of an item of property, plant and equipment, the carrying amount of the asset shall be adjusted to the revalued amount, and the asset shall be treated in one of the following ways:

- a. The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated depreciation at the date of revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account any accumulated impairment losses.
- b. The accumulated depreciation is eliminated against the gross carrying amount of the asset.

The amendment is effective for annual periods beginning on or after July 1, 2014. The amendment shall apply to all revaluations recognized in annual periods beginning on or after the date of initial application of this amendment and in the immediately preceding annual period. The amendment has no impact on the Bank's financial position or performance.

PAS 24, Related Party Disclosures - Key Management Personnel

The amendments clarify that an entity is a related party of the reporting entity if the said entity, or any member of a group for which it is a part of, provides key management personnel services to the reporting entity or to the parent company of the reporting entity. The amendments also clarify that a reporting entity that obtains management personnel services from another entity (also referred to as management entity) is not required to disclose the compensation paid or payable by the management entity to its employees or directors. The reporting entity is required to disclose the amounts incurred for the key management personnel services provided by a separate management entity. The amendments are effective for annual periods beginning on or after July 1, 2014 and are applied retrospectively. The amendments affect disclosures only and have no impact on the Bank's financial position or performance.

PAS 38, Intangible Assets - Revaluation Method - Proportionate Restatement of Accumulated Amortization

The amendments clarify that, upon revaluation of an intangible asset, the carrying amount of the asset shall be adjusted to the revalued amount, and the asset shall be treated in one of the following ways:

- a. The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated amortization at the date of revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account any accumulated impairment losses.
- b. The accumulated amortization is eliminated against the gross carrying amount of the asset.

The amendments also clarify that the amount of the adjustment of the accumulated amortization should form part of the increase or decrease in the carrying amount accounted for in accordance with the standard.

The amendments are effective for annual periods beginning on or after July 1, 2014. The amendments shall apply to all revaluations recognized in annual periods beginning on or after the date of initial application of this amendment and in the immediately preceding annual period. The amendments have no impact on the Bank's financial position or performance.

Annual Improvements to PFRS (2011-2013 cycle)

The Annual Improvements to PFRS (2011-2013 cycle) contain non-urgent but necessary amendments to the following standards:

PFRS 1, First-time Adoption of Philippine Financial Reporting Standards - Meaning of 'Effective PFRSs'

The amendment clarifies that an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but that permits early application, provided either standard is applied consistently throughout the periods presented in the entity's first PFRS financial statements. This amendment is not applicable to the Bank as it is not a first-time adopter of PFRS.

PFRS 3, Business Combinations - Scope Exceptions for Joint Arrangements

The amendment clarifies that PFRS 3 does not apply to the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself. The amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no impact on Bank.

PFRS 13, Fair Value Measurement - Portfolio Exception

The amendment clarifies that the portfolio exception in PFRS 13 can be applied to financial assets, financial liabilities and other contracts. The amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no significant impact on the Bank's financial position or performance.

PAS 40, Investment Property

The amendment clarifies the interrelationship between PFRS 3 and PAS 40 when classifying property as investment property or owner-occupied property. The amendment stated that judgment is needed when determining whether the acquisition of investment property is the acquisition of an asset or a group of assets or a business combination within the scope of PFRS 3. This judgment is based on the guidance of PFRS 3. This amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no significant impact on the Bank's financial position or performance.

PFRS 9, Financial Instruments

PFRS 9, as issued, reflects the first and third phases of the project to replace PAS 39 and applies to the classification and measurement of financial assets and liabilities and hedge accounting, respectively. Work on the second phase, which relate to impairment of financial instruments, and the limited amendments to the classification and measurement model is still ongoing, with a view to replace PAS 39 in its entirety. PFRS 9 requires all financial assets to be measured at fair value at initial recognition. A debt financial asset may, if the fair value option (FVO) is not invoked, be subsequently measured at amortized cost if it is held within a business model that has the objective to hold the assets to collect the contractual cash flows and its contractual terms give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal outstanding. All other debt instruments are subsequently measured at fair value through profit or loss. All equity financial assets are measured at fair value either through other comprehensive income (OCI) or profit or loss. Equity financial assets held for trading must be measured at fair value through profit or loss. For liabilities designated as at FVPL using the fair value option, the amount of change in the fair value of a liability that is attributable to changes in credit risk must be presented in OCI. The remainder of the change in fair value is presented in the statement of income, unless presentation of the fair value change relating to the entity's own credit risk in OCI

would create or enlarge an accounting mismatch in the statement of income. All other PAS 39 classification and measurement requirements for financial liabilities have been carried forward to PFRS 9, including the embedded derivative bifurcation rules and the criteria for using the FVO. The adoption of the first phase of PFRS 9 will have an effect on the classification and measurement of the Bank's financial assets, but will potentially have no impact on the classification and measurement of financial liabilities.

On hedge accounting, PFRS 9 replaces the rules-based hedge accounting model of PAS 39 with a more principles-based approach. Changes include replacing the rules-based hedge effectiveness test with an objectives-based test that focuses on the economic relationship between the hedged item and the hedging instrument, and the effect of credit risk on that economic relationship; allowing risk components to be designated as the hedged item, not only for financial items, but also for non-financial items, provided that the risk component is separately identifiable and reliably measurable; and allowing the time value of an option, the forward element of a forward contract and any foreign currency basis spread to be excluded from the designation of a financial instrument as the hedging instrument and accounted for as costs of hedging. PFRS 9 also requires more extensive disclosures for hedge accounting.

PFRS 9 currently has no mandatory effective date. PFRS 9 may be applied before the completion of the limited amendments to the classification and measurement model and impairment methodology. The Bank will not adopt the standard before the completion of the limited amendments and the second phase of the project.

Philippine Interpretation IFRIC 15, Agreements for the Construction of Real Estate

This interpretation covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. The SEC and the Financial Reporting Standards Council (FRSC) have deferred the effectivity of this interpretation until the final Revenue standard is issued by the International Accounting Standards Board (IASB) and an evaluation of the requirements of the final Revenue standard against the practices of the Philippine real estate industry is completed. Adoption of the interpretation when it becomes effective will not have any impact on the financial statements of the Bank.

3. Significant Accounting Judgments and Estimates

The preparation of the financial statements in compliance with PFRS requires the Bank to make judgments and estimates that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingent assets and contingent liabilities. Future events may occur which will cause the assumptions used in arriving at the estimates to change. The effects of any change in estimates are reflected in the financial statements as they become reasonably determinable.

Judgments and estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Judgments

(a) Operating leases - Bank as lessee

The Bank has entered into commercial property leases with various entities wherein the latter retain all the significant risks and rewards of ownership of those properties leased out under operating leases.

(b) Classification of HTM investment

The classification requires significant judgment. In making this judgment, the Bank evaluates its intention and ability to hold such investments to maturity. If the Bank fails to keep these investments to maturity other than in certain specific circumstances - for example, selling an insignificant amount close to maturity - it will be required to reclassify the entire portfolio as AFS investments. The investments would therefore be measured at fair value and not at amortized cost. The Bank has assessed that it has the intention and ability to hold these investments until maturity. As at December 31, 2013 and 2012, the carrying value of HTM investments amounted to ₱26.1 million and ₱26.2 million, respectively.

(c) Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Refer to Note 4 for the fair value measurement of financial assets and liabilities.

(d) Financial assets not quoted in an active market

The Bank classifies financial assets by evaluating, among others, whether the asset is quoted or not in an active market. Included in the evaluation on whether the asset is quoted in an active market is the determination on whether the quoted prices are readily and regularly available, and whether those prices represent actual and regularly occurring market transactions on an arm's-length basis.

(e) Determination of functional currency

PAS 21, *The Effects of Changes in Foreign Exchange Rates*, requires the Bank to use its judgment to determine its functional currency such that it most faithfully represents the economic effects of the underlying transactions, events and conditions that are relevant to the Bank. In making this judgment, the Bank considers the following:

- the currency that mainly influences sales prices for financial instruments and services (this will often be the currency in which sales prices for its financial instruments and services are denominated and settled);
- the currency in which funds from financing activities are generated; and
- the currency in which receipts from operating activities are usually retained.

The Bank has determined that its functional currency is Philippine peso.

(f) Contingencies

The amount of probable costs for the resolution of any possible claims against the Bank is to be determined in consultation with outside legal counsel which will handle the Bank's defense in any legal contingencies and will be based upon the analysis of potential results.

(g) Going concern

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

Estimates

(a) Credit losses on loans and receivables

The Bank reviews its loans and receivables at each reporting date to assess whether an allowance for credit losses should be set up. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of allowance required. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

The Bank also makes a collective impairment allowance against exposures which, although not specifically identified as requiring a specific allowance, have a greater risk of default than when originally granted. This collective allowance is based on any deterioration in the internal rating of the loan or investment since it was granted or acquired. This collective allowance is based on changes in factors that are indicative of incurred losses, such as deterioration in payment status and underlying property prices, among others.

As at December 31, 2013 and 2012, the carrying values of loans and receivables and related allowance for credit losses are disclosed in Note 9.

(b) Impairment of AFS investments

The Bank determines that AFS investments are impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment. In making this judgment, the Bank treats 'significant' generally as a decline in fair value of 20.00% or more below the investment's original cost and 'prolonged' when a decline lasted for more than twelve months.

In addition, the Bank evaluates when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows. Management believes there is no objective evidence of impairment on these investments.

The carrying value of AFS investments is disclosed in Note 7 and there was no evidence of impairment for these investments.

(c) Estimated useful lives of property and equipment and investment properties

The Bank estimates the useful lives of its property and equipment and investment properties based on the period over which the assets are expected to be available for use. The Bank reviews annually the estimated useful lives based on factors that include asset utilization, internal technical evaluation, technological changes, environmental and anticipated use of the assets. A reduction in the estimated useful lives of property and equipment and investment properties would increase the recorded depreciation and amortization and decrease the assets. The estimated lives of property and equipment and investment properties are disclosed in Note 2.

(d) Impairment of property and equipment, investment properties and assets held by SPV

The Bank assesses impairment on property and equipment, investment properties and assets held by SPV, whenever events or changes in circumstances indicate that the carrying amount of property and equipment, investment properties and assets held by SPV may not be recoverable. The factors that the Bank considers important which could trigger an impairment review include the following:

- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the manner of use of the acquired assets or the strategy for overall business; and
- significant negative industry or economic trends.

The Bank recognizes an impairment loss whenever the carrying amount of its property and equipment, investment properties and assets held by SPV exceeds their recoverable amount.

As at December 31, 2013 and 2012, the carrying values of property and equipment, investment properties and assets held by SPV and their related allowance for impairment losses are disclosed in Notes 10, 11 and 12, respectively.

(e) Present value of pension benefits

The cost of defined benefit pension plan and other post employment benefits is determined using actuarial valuations. The actuarial valuation involves making assumptions about discount rates, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and long term nature of these plans, such estimates are subject to significant uncertainty. All assumptions are reviewed at each reporting date.

In determining the appropriate discount rate, management considers the market yields on Philippine government bonds with terms consistent with the expected employee benefit payout as at reporting date, with extrapolated maturities corresponding to the expected duration of the defined benefit obligation.

The present value of the retirement liability and fair value of plan assets are disclosed in Note 19.

(f) Recognition of deferred tax assets

The amount of deferred tax asset recognized by the Bank is based on the estimate of future taxable income. Significant management judgment is required to determine the amount of deferred tax asset that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning.

The Bank reviews the carrying amount of deferred tax asset at each reporting date and reduces this to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the deferred tax asset to be utilized.

As at December 31, 2013 and 2012, the carrying values of deferred tax assets are disclosed in Note 20.

4. Fair Value Measurement

The Bank uses a hierarchy for determining and disclosing the fair value of its assets and liabilities (see accounting policy on Fair Value Measurement).

As at December 31, 2013 and 2012, the Bank has no financial instruments carried at fair value. The Bank's unquoted AFS investments are carried at cost less any impairment because the fair value could not be reliably determined.

The following table summarizes the carrying amounts and the fair values by level of the fair value hierarchy of the Bank's financial assets and liabilities as at December 31, 2013:

	Carrying Value	Fair value measurement using		
		Quoted prices in active markets (Level 1)	Significant unobservable inputs (Level 3)	Total Fair Value
Assets for which fair values are disclosed:				
Held-to-Maturity investments	₱26,078,103	₱27,499,089	₱—	₱27,499,089
Loans and receivables				
SME loans	97,994,442	—	110,157,371	110,157,371
Investment properties	10,205,436	—	34,909,820	34,909,820
Assets held by Special Purpose Vehicle	4,371,336	—	15,567,350	15,567,350

As at December 31, 2012, the fair value of the financial assets and liabilities of the Bank approximate their carrying values except for the following:

	Carrying Value	Fair Value
SME loans	₱133,498,797	₱137,397,084
Held-to-Maturity investments	26,236,233	27,875,883

The fair values of cash and other cash items, due from BSP, due from other banks, microfinance loans and receivables, deposit liabilities, bills payable, accounts payable and accrued interest payable approximate their carrying values in view of the relatively short-term maturities of these instruments.

Fair values of noncurrent portion of receivables and held-to-maturity investments are estimated using the discounted cash flow methodology, based on prevailing market rates for similar financial assets, taking into account the remaining maturities and applicable spreads of the counterparties.

Instruments in Level 3 include those for which there is currently no active market.

There were no transfers between fair value categories for assets and liabilities measured at fair value in 2013 and 2012.

5. Financial Risk Management Objectives and Policies

In the course of the business cycle, the Bank has exposure to the following risks from its use of financial instruments: (a) credit risk; (b) market risk; and (c) liquidity risk.

The Bank adheres to the proactive and prudent approach of managing the business that recognizes and manages risks to continuously provide quality financial services to clients and to protect shareholders' value. Risk management process involves setting of revenue goals, definition of risk philosophy and creating risk culture, determining opportunities that would create risk in the future, identifying and assessing the risk, evaluating and defining risk tolerance, taking actions to mitigate and control the risks through defined roles and responsibilities, close monitoring of the scenarios, reporting of risk taking performance, revalidation of risk methodologies and adjustment of the systems and policies necessary to effectively minimize risk level.

The BOD through its Risk Management Committee (RMC) is responsible for the development and oversight of the Bank's risk management program, identification and evaluation of risk exposures, monitoring the Bank's implementation of risk management policies and procedures, and for reviewing and evaluating the adequacy of risk management framework in relation to the risks faced by the Bank. The RMC regularly reports to the BOD the results of reviews of actual implementation of risk management policies. Risk management of the Bank is strengthened with conjunction of Audit Committee (AC) and Internal Audit (IA) functions. IA undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the AC.

a. Credit risk

Credit risk is the risk of financial loss to the Bank if the counterparty to a financial instrument fails to meet its contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

Management of credit risk

Credit risk is being managed by instilling credit discipline both among the staff and the borrowers. The Bank's staff performs in-depth credit evaluation and close monitoring of account throughout the borrowing period, hence, on-time service delivery motivates the borrowers to fulfill their financial obligation to the highest standards. Borrowers are well-oriented and deeply committed on the credit repayment design they undertake.

For microfinance loans, loan portfolio was diversified in different economic activities or projects. There is geographical diversification to spread the risk brought about by natural calamities. Proper target market selection, rigorous character and background investigation, members' or borrowers' education or training on credit discipline in microfinance and validation of utilization of loan proceeds are applied. Intensive monitoring of all branches is conducted by the Area Manager, Regional Director and Executive Vice President. Staff skills and competencies are regularly updated. Strategies are identified to manage competitors. Development of new client or market-oriented loan or deposit products and enhancement of product design systems and procedures, monitoring of members without loans and motivating qualified members to borrow are regularly done. Cost-cutting measures were planted to achieve improved profitability. Financial ratios and evaluation of compliance with BSP standards are regularly monitored.

Furthermore, the Bank has a preventive delinquency management approach through proper and strict credit delivery deliver, monitoring and collection. Close monitoring through conduct of weekly center meetings is being implemented allowing the early determination of early warning signals on each borrower-member. A daily monitoring on the number of defaulted members and intensive follow-up areas strictly being implemented. Various remedial measures are likewise being implemented to allow rehabilitation of defaulted borrowers. Defaulted borrowers which failed to cooperate despite remedial efforts done are referred to the bank's legal counsel for collection or filing of appropriate legal action.

In general, borrowers are also perpetual savers. Consequently, their savings balances are pledged and serve as guarantee to their loans, which increase their borrowing capacity. Each business unit has a Unit Manager who reports on all credit-related matters to the local management consisting of the Area Manager, Regional Director and Executive Vice President.

Each business unit is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolio. Regular audits of business units and credit processes are undertaken by IA.

All past due or impaired accounts are reported on a daily, weekly and monthly bases. Consistent monitoring for this group of accounts is established by competent and diligent staff to maximize recovery. Incentives have been established and subjected to review and assessment periodically. These are given to staff to recover from the accounts and to fully instill credit discipline to clients. Restructuring of loan payments are done after full compliance of approved policies and procedures. Writing off bad accounts is approved by the BOD and reported to the BSP in compliance with the Manual of Regulations for Banks.

Maximum exposure to credit risk

Table below provides the analysis of the maximum exposure to credit risk of the Bank's financial instruments, excluding those where the carrying values as reflected in the statement of financial position and related notes already represent the financial instrument's maximum exposure to credit risk, before and after taking into account collateral held or other credit enhancements.

2013				
	Maximum Exposure to Credit risk	Fair value of Collateral and Credit Enhancements	Financial effect of Collateral or Credit Enhancement	Net Exposure to Credit risk
Loans and discounts:				
Microfinance loans	₱790,990,996	₱121,454,937	₱121,454,937	₱669,536,059
SME loans	86,791,575	36,636,715	21,261,194	65,530,381
REM loans	101,785	331,872	101,785	–
2012				
	Maximum Exposure to Credit risk	Fair value of Collateral and Credit Enhancements	Financial effect of Collateral or Credit Enhancement	Net Exposure to Credit risk
Loans and discounts:				
Microfinance loans	₱427,168,351	₱65,629,417	₱65,629,417	₱361,538,934
SME loans	122,673,483	19,636,700	10,741,094	111,932,389
REM loans	243,540	906,251	243,540	–

Credit enhancement for microfinance loans pertains to deposit hold-out from center fund savings equivalent to 15.0% of the outstanding loan to the member as at December 31, 2013 and 2012. Credit enhancement for REM and SME loans consists of chattel and real estate mortgages.

The Bank has no financial instruments with rights of set-off in accordance to PAS 32 as at December 31, 2013 and 2012. There are also no financial instruments that are subject to an enforceable master netting arrangements or similar agreements which require disclosure in the financial statements in accordance with amendments on PFRS 7.

The Bank assessed that it has no credit risk exposures relating to off-balance sheet items.

Additionally, the table below shows the distribution of maximum credit exposure by industry sector of the Bank as at December 31, 2013 and 2012:

	2013				
	Loans and Receivables	Due from BSP and Other Banks	Investment Securities*	Other Assets**	Total
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods	₱343,247,369	₱—	₱—	₱—	₱343,247,369
Manufacturing	137,445,837	—	—	—	137,445,837
Financial intermediaries	1,020,098	83,462,403	26,078,103	—	110,560,604
Government	20,092,290	50,603,710	—	—	70,696,000
Other community, social and personal service activities	98,423,965	—	—	—	98,423,965
Agriculture, hunting and forestry	157,476,129	—	—	—	157,476,129
Others	184,289,636	—	—	312,000	184,601,636
	941,995,324	134,066,113	26,078,103	312,000	1,102,451,540
Allowance for credit losses	(31,019,735)	—	—	—	(31,019,735)
Unearned interest and discount	(1,175)	—	—	—	(1,175)
Total	₱910,974,414	₱134,066,113	₱26,078,103	₱312,000	₱1,071,430,630

	2012				
	Loans and Receivables	Due from BSP and Other Banks	Investment Securities*	Other Assets**	Total
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods	₱311,645,077	₱—	₱—	₱—	₱311,645,077
Manufacturing	87,580,961	—	—	—	87,580,961
Financial intermediaries	1,502,017	74,480,762	—	—	75,982,779
Government	—	31,379,001	34,236,233	—	65,615,234
Other community, social and personal service activities	54,210,658	—	—	—	54,210,658
Agriculture, hunting and forestry	45,240,831	—	—	—	45,240,831
Others	79,363,990	—	—	256,668	79,620,658
	579,543,534	105,859,763	34,236,233	256,668	719,896,198
Allowance for credit losses	(22,443,370)	—	—	—	(22,443,370)
Unearned interest and discount	(828,994)	—	—	—	(828,994)
Total	₱556,271,170	₱105,859,763	₱34,236,233	₱256,668	₱696,623,834

* Investment securities consist of AFS investments and HTM securities

** Other assets include refundable deposits

Credit quality

Loans and receivables and AFS investments rated as high and standard grades refer to those accounts that do not have greater than normal risk or have potential weaknesses only.

High grade represents those accounts granted to borrowers which are availed loans intended for microeconomic activities that are current or investments in government securities or debt securities issued by reputable institutions.

Standard grade represents those accounts granted to borrowers which have availed loans intended for financing business capital emergency needs, multi-purpose requirements and housing improvements.

The table below shows the credit quality per class of financial assets as at December 31, 2013 and 2012:

	2013				
	Neither Past Due Nor Impaired		Past Due but not Impaired	Individually Impaired	Total
	High Grade	Standard Grade			
AFS investments	P=	P=	P=	P=	P=
HTM investments	26,078,103	—	—	—	26,078,103
Loans and receivables:	—	—	—	—	—
Due from BSP	50,603,710	—	—	—	50,603,710
Due from other banks	83,462,403	—	—	—	83,462,403
Loans and discounts:	—	—	—	—	—
Microfinance	—	800,832,491	1,815,200	7,051,890	809,699,581
SME	28,565,296	57,747,751	1,554,403	10,126,992	97,994,442
REM	—	—	—	721,965	721,965
Unquoted debt securities	21,112,388	—	—	—	21,112,388
Other receivables:	—	—	—	—	—
Accrued interest receivable	7,717,894	—	—	—	7,717,894
Accounts receivable	—	—	—	4,010,365	4,010,365
Sales contract receivable	—	738,689	—	—	738,689
Other assets - refundable deposits	—	312,000	—	—	312,000
	P217,539,794	P859,630,931	P3,369,603	P21,911,212	P1,102,451,540

	2012				
	Neither Past Due Nor Impaired		Past Due but not Impaired	Individually Impaired	Total
	High Grade	Standard Grade			
AFS investments	P8,000,000	P=	P=	P=	P8,000,000
HTM investments	26,236,233	—	—	—	26,236,233
Loans and receivables:	—	—	—	—	—
Due from BSP	31,379,001	—	—	—	31,379,001
Due from other banks	74,480,762	—	—	—	74,480,762
Loans and discounts:	—	—	—	—	—
Microfinance	—	433,549,818	650,880	3,331,750	437,532,448
SME	74,494,926	48,066,728	4,421,802	5,686,347	132,669,803
REM	—	—	246,000	1,170,345	1,416,345
Unquoted debt securities	1,502,017	—	—	—	1,502,017
Other receivables:	—	—	—	—	—
Accrued interest receivable	4,683,779	—	—	—	4,683,779
Accounts receivable	—	—	—	910,148	910,148
Other assets - refundable deposits	—	256,668	—	—	256,668
	P220,776,718	P481,873,214	P5,318,682	P11,098,590	P719,067,204

Aging analysis of past due but not impaired loans and receivables

The following table shows the total aggregate amount of loans and discounts that are contractually past due but not considered as impaired per delinquency bucket as at December 31, 2013 and 2012.

2013				
	Less than 30 Days	31 to 60 Days	61 to 90 Days	Total
Microfinance	₱453,849	₱726,690	₱634,661	₱1,815,200
SME	956,139	362,479	235,785	₱1,554,403
	₱1,409,988	₱1,089,169	₱870,446	₱3,369,603

2012				
	Less than 30 Days	31 to 60 Days	61 to 90 Days	Total
Microfinance	₱92,837	₱286,942	₱271,101	₱650,880
SME	2,944,024	738,009	739,769	4,421,802
REM	—	—	246,000	246,000
	₱3,036,861	₱1,024,951	₱1,256,870	₱5,318,682

b. Market Risk

Market risk is the risk of loss to future earnings, fair values or future cash flows that may result from changes in the price of a financial instrument. The value of a financial instrument may change as a result of changes in interest rates. The Bank is exposed to market risk, although minimal, due to its placement to government debt securities, under 'Unquoted debt securities classified as loans.

Interest rate risk

The Bank's nominal interest rate for REM loans and microfinance loans are set at fixed rate of 21.0% and 28.0% per annum, respectively. For SME loans, interest rate charged to a borrower shall depend on the credit risk rating classification, the deposit level of the client as a percentage of the loan, and the internal basic interest rate.

The effect of interest repricing on loans is immaterial to the Bank therefore sensitivity analysis is no longer presented.

The Bank's savings deposit liabilities include compulsory and voluntary savings that earns 1.5% to 2.0% per annum. The bulk of Tiwala savings accounts are concentrated on 30 days to one year maturity with interest rate of less than 2.5%.

In order to manage its interest rate risk, the Bank places its excess funds in high yield investments and other short-term time deposits and treasury notes. It also matches its interest rate and maturity to avoid negative gaps between the sources and applications.

Foreign currency risk

The Bank has no foreign currency denominated transactions, thus, it has no exposure to changes in foreign exchange rates.

c. Liquidity Risk

Liquidity risk is generally defined as the current and prospective risk to earnings or capital arising from the Bank's inability to meet its obligations when they come due without incurring unacceptable losses or costs.



The Asset Liability Management Committee is responsible for formulating the Bank's liquidity risk management policies. Liquidity management is among the most important activities conducted within the Bank. The Bank manages its liquidity risk through analyzing net funding requirements under alternative scenarios, diversification of funding sources and contingency planning. The Bank utilizes a diverse range of sources of funds, although short-term deposits made with the Bank's network of domestic branches comprise the majority of such funding.

Liquidity risk is managed by the Bank through holding sufficient liquid assets and appropriate assessment to ensure short-term funding requirements are met and by ensuring the high collection performance at all times. Deposits with banks are made on a short-term basis with almost all being available on demand or within one month.

The Treasury Group uses liquidity forecast models that estimate the Bank's cash flow needs based on the Bank's actual contractual obligations and under normal circumstances and extraordinary circumstances.

Analysis of financial assets and financial liabilities by remaining maturities

The table below shows the maturity profile of the Bank's financial assets and financial liabilities based on contractual undiscounted cash flows as at December 31, 2013 and 2012:

	2013				
	On demand	1 to 6 months	6 to 12 months	Beyond 1 year	Total
Financial Assets					
HTM investment*	₱—	₱15,602,051	₱527,359	₱11,816,294	₱27,945,704
Loans and receivables:	—	—	—	—	—
Due from BSP	50,603,710	—	—	—	50,603,710
Due from other banks	49,064,893	34,397,510	—	—	83,462,403
Loans and discounts*	16,637,261	756,123,777	104,730,666	43,076,611	920,568,315
Unquoted debt securities*	—	14,042,420	3,024,745	17,977,064	35,044,229
Other receivables:	—	—	—	—	—
Accrued interest receivable	7,365,641	352,253	—	—	7,717,894
Accounts receivable	4,010,365	—	—	—	4,010,365
Sales contract receivable	25,282	510,776	87,565	115,066	738,689
Other assets - refundable deposits	—	—	—	312,000	312,000
	127,707,152	821,028,787	108,370,335	73,297,035	1,130,403,309
Financial Liabilities					
Deposit liabilities:					
Demand	441,307	—	—	—	441,307
Savings	50,631,505	518,970,212	258,412,042	—	828,013,759
Other liabilities	22,277,022	—	—	—	22,277,022
	73,349,834	518,970,212	258,412,042	—	850,732,088
Net undiscounted financial assets (liabilities)	₱54,357,318	₱302,058,575	(₱150,041,707)	₱73,297,035	₱279,671,221

*Includes future interest

	2012				
	On demand	1 to 6 months	6 to 12 months	Beyond 1 year	Total
Financial Assets					
AFS investments*	₱—	₱—	₱3,518,392	₱5,345,594	₱8,863,986
HTM investment*	—	445,119	679,105	26,751,659	27,875,883
Loans and receivables:					
Due from BSP	31,379,001	—	—	—	31,379,001
Due from other banks	24,804,464	51,782,761	—	—	76,587,225
Loans and discounts*	43,978,553	225,651,402	322,420,727	29,631,730	621,682,412
Unquoted debt securities	—	1,525,824	—	—	1,525,824

(Forward)

	2012				
	On demand	1 to 6 months	6 to 12 months	Beyond 1 year	Total
Other receivables:					
Accrued interest receivable	₱4,332,618	₱351,161	₱—	₱—	₱4,683,779
Accounts receivable	910,148	—	—	—	910,148
Other assets - refundable deposits	—	—	—	256,668	256,668
	105,404,784	279,756,267	326,618,224	61,985,651	773,764,926
Financial Liabilities					
Deposit liabilities:					
Demand	730,357	—	—	—	730,357
Savings	61,266,718	278,773,062	65,841,927	98,632,794	504,514,501
Bills payable*	—	8,982,579	19,043,921	—	28,026,500
Other liabilities	14,258,327	—	—	—	14,258,327
	76,255,402	287,755,641	84,885,848	98,632,794	547,529,685
Net undiscounted financial assets (liabilities)	₱29,149,381	(₱7,999,374)	₱241,732,376	(₱36,647,143)	₱226,235,241

*Includes future interest

6. Cash and Cash Equivalents

The composition of this account follows:

	2013	2012
Cash and other cash items	₱4,610,455	₱2,903,536
Due from BSP	50,603,710	31,379,001
Due from other banks	83,462,403	74,480,762
	₱138,676,568	₱108,763,299

The account with BSP is maintained in compliance with the BSP requirements to maintain regular and liquidity reserves on deposits.

Due from other banks consists of:

	2013	2012
Demand deposit	₱42,106,728	₱18,677,929
Savings deposit	6,958,165	5,440,189
Time certificate of deposit	34,397,510	50,362,644
	₱83,462,403	₱74,480,762

Due from other banks bears annual interest rates ranging from 0.8% to 1.75%. In 2013 and 2012, interest income on due from other banks amounted to ₱2.4 million and ₱6.0 million, respectively.

7. Available-for-Sale Investments

In 2012, AFS investments consist of the Bank's investment in 50,000 redeemable preferred shares of Small Business Corporation (SBC) with an annual dividend rate of 4.0% and a minimum holding period of three years starting December 9, 2010, and Micro, Small and Medium Enterprises (MSME) notes with an annual interest rate of 1.1% and maturity of one year. The two investments matured in 2013.

Unrealized gain on AFS investments amounted to nil as at December 31, 2013 and 2012.

8. Held-to-Maturity Investments

This account represents investment in government securities bearing annual interest rate of 6.3% to 7.0% in 2013 and 2012, respectively.

Interest income earned for HTM investments amounted to ₱1.7 million and ₱1.5 million in 2013 and 2012, respectively.

9. Loans and Receivables

This account consists of:

	2013	2012
Loans and discounts:		
Microfinance (Note 15)	₱809,699,581	₱437,532,448
Small and medium enterprises	97,994,442	133,498,797
Real estate mortgage	721,965	1,416,345
	908,415,988	572,447,590
Unearned interest income	(1,175)	(828,994)
	908,414,813	571,618,596
Unquoted debt securities	21,112,388	1,502,017
Other receivables:		
Accrued interest receivable (Note 21)	7,717,894	4,683,779
Accounts receivable	4,010,365	910,148
Sales contracts receivable	738,689	—
	941,994,149	578,714,540
Less allowance for credit losses	(31,019,735)	(22,443,370)
	₱910,974,414	₱556,271,170

In 2013, the Bank purchased three (3) MSME notes accounted for as unquoted debt securities amounting to ₱20.0 million. Interest rates range from 0.9% to 1.3% with maturity ranging from 360 to 1,094 days.

Loans and discounts earn interest ranging from 32.8% to 58.8% in 2013 and 2012, respectively.

The following table shows the interest income per class of loans and receivables:

	2013	2012
Loans and discounts:		
Microfinance	₱324,319,196	₱185,921,049
SME	21,759,817	33,654,567
REM	175,638	642,885
Unquoted debt securities	38,225	23,515
	₱346,292,876	₱220,242,016

Interest income on past due loans and receivables amounted to ₱2.83 million and ₱1.02 million in 2013 and 2012, respectively.

As at December 31, 2013 and 2012, microfinance loans amounting to nil and ₱39.5 million are held as collateral to the Bank's borrowings (Note 15).

BSP Reporting

In accordance with BSP regulations, the Bank considers as part of portfolio-at-risk (PAR) an installment payment that is past due for a day only. As at December 31, 2013 and 2012, the Bank's PAR amounted to ₱21.3 million and ₱15.5 million, respectively. The allowance for credit losses recognized for past due loans amounted to ₱18.3 million and ₱90.0 million as at December 31, 2013 and 2012, respectively.

Current banking regulations allow banks with no unbooked valuation reserves and capital adjustments to exclude from nonperforming classification those receivables classified as Loss in the latest examination of the BSP which are fully covered by allowance for credit losses, provided that interest on said receivables shall not be accrued.

As at December 31, 2013 and 2012, nonperforming loans (NPLs) not fully covered by the allowance for credit losses follow:

	2013	2012
Total NPLs	₱19,774,421	₱12,232,105
NPLs fully covered by allowance for credit losses	(18,453,495)	(10,902,789)
Balance at end of year	₱1,320,926	₱1,329,316

Generally, NPLs refer to loans whose principal and/or interest is unpaid for thirty days or more after due date or after they have become past due in accordance with existing BSP rules and regulations. This shall apply to loans payable in lump sum and loans payable in quarterly, semi-annual, or annual installments, in which case, the total outstanding balance thereof shall be considered nonperforming.

In the case of loans that are payable in monthly installments, the total outstanding balance thereof shall be considered nonperforming when three or more installments are in arrears.

In the case of loans that are payable in daily, weekly, or semi-monthly installments, the total outstanding balance thereof shall be considered nonperforming at the same time that they become past due in accordance with existing BSP regulations, i.e., the entire outstanding balance of the receivable shall be considered as past due when the total amount of arrearages reaches ten percent (10.0%) of the total receivable balance.

Loans are classified as nonperforming in accordance with BSP regulations, or when, in the opinion of management, collection of interest is doubtful. Loans are not reclassified as performing until interest and principal payments are brought current or the loans are restructured in accordance with existing BSP regulations, and future payments appear assured.

The following table shows the secured and unsecured portions of loans and discounts as at December 31, 2013 and 2012:

	2013	2012
Secured portion		
Deposit hold-out	₱121,454,937	₱65,629,417
REM	14,793,372	7,372,509
Chattel mortgage	14,162,016	4,274,836
	150,410,325	77,276,762
Unsecured portion	758,005,663	495,170,828
	₱908,415,988	₱572,447,590

The Bank also obtains additional security in the form of members' joint guarantees (under memorandum of agreements signed among various member groups) and post-dated checks of members.

The movements in allowance for credit losses follow:

	2013			2012		
	Loans and discounts	Accounts receivable	Total	Loans and discounts	Accounts receivable	Total
Balance at beginning of year	₱21,533,222	₱910,148	₱22,443,370	₱16,025,711	₱387,104	₱16,412,815
Provisions	10,010,896	7,210	10,018,106	7,788,681	591,938	8,380,619
Write-offs	(1,013,661)	(428,080)	(1,441,741)	(2,281,170)	(68,894)	(2,350,064)
Balance at end of year	₱30,530,457	₱489,278	₱31,019,735	₱21,533,222	₱910,148	₱22,443,370
Individually impaired	₱12,049,124	₱489,278	₱12,538,402	₱5,731,765	₱910,148	₱6,641,913
Collectively impaired	18,481,333	–	18,481,333	15,801,457	–	15,801,457
	₱30,530,457	₱489,278	₱31,019,735	₱21,533,222	₱910,148	₱22,443,370
Gross amounts of loans individually determined to be impaired, before deducting any individually assessed impairment losses	₱17,900,847	₱4,010,365	₱21,911,212	₱10,188,442	₱910,148	₱11,098,590

As at December 31, 2013 and 2012, allowance provided by the Bank for past due accounts amounted to ₱18.3 million and ₱11.9 million, respectively.

Information on the concentration of credit as to industry of loans and receivables (gross of unearned discounts and allowance for impairment and credit losses) follows:

	2013		2012	
	Amount	%	Amount	%
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods	₱343,247,369	35.94	₱311,645,077	53.77
Agriculture, hunting and forestry	157,476,129	16.49	46,069,825	7.96
Manufacturing	137,445,837	14.39	87,580,961	15.11
Other community, social and personal service activities	131,514,343	13.77	54,210,658	9.35
Financial intermediaries	1,020,098	0.11	1,502,017	0.26
Others	184,289,636	19.30	78,534,996	13.55
	₱954,993,412	100%	₱579,543,534	100%

The BSP considers that loan concentration exists when total loan exposure to a particular industry or economic sector exceeds 30.0% of total loan portfolio. Identified concentrations of credit risks are controlled and managed accordingly. Thrift banks are not covered by the loan concentration limit of 30.0% prescribed by the BSP.

10. Property and Equipment

The composition of and movements in this account follow:

2013							
	Furniture, Fixtures and Equipment	Leasehold Improvements	Transportation Equipment	Building	Construction in Progress	Land	Total
Cost							
Balance at beginning of year	₱14,783,912	₱7,405,455	₱6,986,929	₱7,057,552	₱—	₱10,651,530	₱46,885,378
Acquisition	6,036,766	4,512,002	53,570	1,301,503	1,520,000	891,919	14,315,760
Disposals/Reversal	(1,070,188)	—	(56,900)	(86,477)	—	—	(1,213,565)
Balance at end of year	19,750,490	11,917,457	6,983,599	8,272,578	1,520,000	11,543,449	59,987,573
Accumulated Depreciation and Amortization							
Balance at beginning of year	8,137,226	2,846,934	2,548,015	1,647,409	—	—	15,179,584
Depreciation and amortization	4,008,739	1,993,838	1,490,850	781,549	—	—	8,274,976
Disposals	(1,056,886)	—	(56,899)	(20,513)	—	—	(1,134,298)
Balance at end of year	11,089,079	4,840,772	3,981,966	2,408,445	—	—	22,320,262
Net Book Value	₱8,661,411	₱7,076,685	₱3,001,633	₱5,864,133	₱1,520,000	₱11,543,449	₱37,667,311

2012							
	Furniture, Fixtures and Equipment	Leasehold Improvements	Transportation Equipment	Building	Construction in Progress	Land	Total
Cost							
Balance at beginning of year	₱9,247,074	₱3,182,138	₱2,250,738	₱3,289,871	₱484,500	₱—	₱18,454,321
Acquisition	6,101,889	3,738,817	4,848,846	3,767,681	—	6,903,000	25,360,233
Disposals	(565,051)	—	(112,655)	—	—	—	(677,706)
Transfers (Note 11)	—	484,500	—	—	(484,500)	3,748,530	3,748,530
Balance at end of year	14,783,912	7,405,455	6,986,929	7,057,552	—	10,651,530	46,885,378
Accumulated Depreciation and Amortization							
Balance at beginning of year	5,863,598	1,539,962	1,618,081	1,296,103	—	—	10,317,744
Depreciation and amortization	2,838,679	1,306,972	1,042,589	351,306	—	—	5,539,546
Disposals	(565,051)	—	(112,655)	—	—	—	(677,706)
Balance at end of year	8,137,226	2,846,934	2,548,015	1,647,409	—	—	15,179,584
Net Book Value	₱6,646,686	₱4,558,521	₱4,438,914	₱5,410,143	₱—	₱10,651,530	₱31,705,794

Loss on disposal of property and equipment amounted to ₱0.08 million and nil in 2013 and 2012, respectively.

The total cost of fully depreciated assets still in use is ₱9.0 million and ₱5.5 million in 2013 and 2012, respectively.

11. Investment Properties

The composition of and movements in this account follow:

2013			
	Land	Building	Total
Cost			
Balance at beginning of year	₱22,650,822	₱1,530,500	₱24,181,322
Foreclosures	1,292,321	—	1,292,321
Disposals	(5,949,987)	(670,418)	(6,620,405)
Balance at end of year	17,993,156	860,082	18,853,238

(Forward)

	2013		
	Land	Building	Total
Accumulated Depreciation			
Balance at beginning of year	₱–	₱560,891	₱560,891
Depreciation	–	163,305	163,305
Disposals	–	(394,838)	(394,838)
Balance at end of year	–	329,358	329,358
Allowance for Impairment			
Losses			
Balance at beginning of year	7,432,213	–	7,432,213
Provisions	449,681	436,550	886,231
Balance at end of year	7,881,894	436,550	8,318,444
Net Book Value	₱10,111,262	₱94,174	₱10,205,436

	2012		
	Land	Building	Total
Cost			
Balance at beginning of year	₱26,380,042	₱4,002,485	₱30,382,527
Foreclosures	2,285,035	–	2,285,035
Disposals	(2,265,725)	(2,471,985)	(4,737,710)
Transfers (Note 10)	(3,748,530)	–	(3,748,530)
Balance at end of year	22,650,822	1,530,500	24,181,322
Accumulated Depreciation			
Balance at beginning of year	–	1,278,823	1,278,823
Depreciation	–	103,065	103,065
Disposals	–	(820,997)	(820,997)
Balance at end of year	–	560,891	560,891
Allowance for Impairment			
Losses			
Balance at beginning and end of year	7,432,213	–	7,432,213
Net Book Value	₱15,218,609	₱969,609	₱16,188,218

Fair value gain on initial recognition of foreclosed properties included under ‘Gain on initial recognition of investment properties’ amounted to ₱1.1 million and ₱1.7 million in 2013 and 2012, respectively.

Direct operating expenses on investment properties during the period, included under ‘Litigation and assets acquired’ in ‘Miscellaneous expense’ in the statement of income amounted to ₱0.7 million and nil in 2013 and 2012, respectively. Investment properties may be disposed through redemption, negotiated sale or lease purchase. In 2013 and 2012, all of the Bank’s investment properties are non-revenue generating.

As at December 31, 2013 and 2012, the fair value of investment properties amounted to ₱34.9 million and ₱20.4 million, respectively. Fair values have been determined based on valuations made by independent and in-house appraisers. The fair value of the properties is based on sales and listings of comparable property registered within the vicinity.

The Bank has determined the highest and best use of its investment properties. Eighteen properties with total appraisal value of ₱28.7 million and total carrying value of ₱14.4 million is for residential development into a single family dwelling unit. Ten properties with total appraisal value of ₱4.5 million and total carrying value of ₱3.4 million is for orchard-type agricultural use until such time it is ripe for any type of development. One property with total appraised value of ₱1.7 million and carrying value of ₱1.3 million is for low cost housing residential project offering single family dwelling units.

Furthermore, the Bank has identified that 16 out of the 29 properties are still idle and are not utilized according to their highest and best use for strategic purposes.

The Bank has program disposal of its investment properties to reduce the nonperforming assets in its books.

The following table summarizes the valuation techniques used and the significant unobservable inputs valuation for investment properties held by the Bank:

	Valuation Techniques	Significant Unobservable inputs
Land	Market Approach	Location, size, shape, utility/neighborhood, improvements and time element
Building	Modified Quantity Survey Approach	Depreciated replacement cost

Description of the valuation techniques and inputs and assumptions used to value the Bank's investment properties are as follows:

Valuation Techniques, Inputs and Assumptions	Description
Market Data Approach	The value of the property is based on sales and listings of comparable property registered within the vicinity. The technique of this approach requires the adjustments of comparable property by reducing reasonable comparative sales and listings to a common denominator. This was done by adjusting the differences between the subject property and those actual sales and listings regarded as comparable. The properties used as bases of comparison are situated within the immediate vicinity of the subject property. Comparison was premised on the factors of location, size and shape of the lot, and time element.
Modified Quantity Survey Approach	This method requires an analysis of the buildings, leasehold improvements, other land improvements by breaking floorings, walls, roofings, etc., using workable units as lineal meter, square meter, cubic meter or other appropriate basic unit. Equally given importance are the interior finishes, i.e. floor finishes, wall finishes, ceiling finishes, etc. Bills of quantities for each building component using the appropriate basic unit are prepared and related to the unit cost for each component developed on the basis of current costs of materials, labor, plant and equipment prevailing in the locality to arrive at the direct costs of the buildings, leasehold improvements and other land improvements, whereupon indirect costs such as contractor's profits, overhead, taxes, and fees and other related expenses are then added.

Valuation Techniques, Inputs and Assumptions	Description
Depreciated Replacement Cost	This is the cost of replacement less accrued depreciation as evidenced by the observed condition in comparison with new units of like kind tempered by consideration given to extent, character and utility of the property which is to be continued in its present use as part of a going concern but without specific relations to earnings.
Replacement Cost	This is defined as the estimated amount of money needed to replace in like kind and in new condition an asset or group of assets, taking into consideration current prices of materials, labor, contractor's overhead, profit and fees, and all other attendant costs associated with its acquisition and installation in place, without provision for overtime or bonuses for labor, and premiums for materials.
Size	Physical magnitude, extent or bulk, relative or proportionate dimensions. The value of the lot varies in accordance to the size of the lots. Basic rule of thumb is the bigger the lot size the lower the value, the smaller the lot size the higher the value.
Shape	Particular form or configuration. A highly irregular shape limits the usable area whereas an ideal lot configuration maximizes the usable area of the lot which is associated in designing an improvement which conforms to the highest and best use of the property.
Location	For a tract of land designated for a purpose or site occupied or available for occupancy, one of the key factors in land valuation is the location or area of preference.
Time Element	The measured or measurable period during action or condition exist. It is usually associated with the period in which the property can be sold in an open market within reasonable time.

12. Assets Held by Special Purpose Vehicle

Assets held by SPV represents foreclosed properties (land) which have been specifically identified for sale under a sale and purchase agreement (SPA) with an SPV and is presented net of allowance for impairment losses amounting to ₱3.4 million and ₱2.9 million as at December 31, 2013 and 2012, respectively. Provision for impairment losses amounted to ₱1.0 million and nil in 2013 and 2012, respectively.

Direct operating expenses on SPV during the period, included under 'Litigation and assets acquired' in 'Miscellaneous expense' in the statement of income amounted to ₱1.2 million and nil in 2013 and 2012, respectively.

Major provisions of the SPA follow:

- The proceeds of the sale shall be paid by the buyer to the Bank on or before November 20, 2018. The payment shall not be subject to any interest;
- The buyer covenants and undertakes that any and all proceeds from any subsequent sale, disposition or settlement of any asset shall be earmarked for the payment of the purchase price; and

- If on the due date, the amount of the net proceeds is lesser than the purchase price, the difference between the net proceeds and purchase price shall be applied against the unpaid balance.

Under Republic Act No. 9182, *The Special Purpose Vehicle Act of 2002*, the sale of assets to the SPV under the SPA is a true sale, as approved by the BSP. However, under PFRS, the assets sold remain to be recognized by the Bank since the risks and rewards of ownership over the assets are not yet transferred to the SPV.

The Bank has determined the highest and best use of its assets held by special purpose vehicle. Five properties with total appraisal value of ₱5.2 million and total carrying value of ₱4.4 million is for orchard type agricultural use until such time it is ripe for any type of development. Two properties with total appraisal value of ₱10.1 million and total carrying value of ₱4.1 million is for residential development into a single family dwelling unit. One property with total appraised value of ₱0.3 million and carrying value of ₱0.4 million is for subdivision into smaller parcels and development into a single family dwelling unit.

Furthermore, the Bank has identified that three of the eight properties are not utilized according to their highest and best use because they are either idle or occupied by informal settlers.

Gain on sale of assets held by SPV amounted to ₱1.2 million and nil in 2013 and 2012, respectively.

13. Other Assets

This account consists of:

	2013	2012
Financial assets:		
Refundable deposit	₱312,000	₱256,668
Nonfinancial assets:		
Stationeries and supplies	5,788,589	3,999,685
Prepaid expenses	3,652,723	2,392,792
Miscellaneous	827,914	360,589
	10,269,226	6,753,066
	₱10,581,226	₱7,009,734

14. Deposit Liabilities

Savings deposits earn annual interest rate ranging from 1.5% to 5.5% and from 2.0% to 5.5% in 2013 and 2012, respectively.

Details of interest expense on deposit liabilities follow:

	2013	2012
Demand deposit	₱9,627,104	₱6,288,476
Savings deposit	9,067,329	10,618,623
	₱18,694,433	₱16,907,099

In 2011, under existing BSP regulations, deposit liabilities of the Bank are subject to liquidity reserves equivalent to 2.00% and statutory reserves equivalent to 6.0%. In March 2012, BSP issued Circular 753 effective April 6, 2012 unifying the liquidity and statutory reserves requirements to 6.0%, with cash in vault no longer eligible as reserve. Available reserves as at December 31, 2013 and 2012 amounted to ₱50.6 million and ₱31.4 million, respectively.

As at December 31, 2013 and 2012, the Bank is compliant with the applicable reserve requirements.

15. Bills Payable

Bills payable represent borrowings from financial institutions, which are subject to certain terms and conditions bearing annual interest rates ranging from 6.0% to 6.5% in 2013 and 2012.

During the year, the Bank settled its bills payable amounting to ₱26.5 million. As at December 31, 2013 and 2012, outstanding balance amounted to nil and ₱26.5 million, respectively.

Microfinance loans amounting to nil and ₱99.3 million secure the above borrowings as at December 31, 2013 and 2012, respectively (Note 9).

Interest expense on bills payable in 2013 and 2012 amounted to ₱0.04 million and ₱2.7 million, respectively.

16. Other Liabilities

This account consists of:

	2013	2012
Financial liabilities:		
Accrued expenses	₱16,174,497	₱10,868,399
Accounts payable (Note 21)	3,586,196	1,263,784
Accrued interest payable	2,020,693	2,126,144
Unearned service fee income	455,488	—
Dividends payable	40,148	—
	22,277,022	14,258,327
Nonfinancial liabilities:		
Accrued taxes	4,069,873	2,040,751
Others	2,042,628	631,775
	6,112,501	2,672,526
	₱28,389,523	₱16,930,853

Accrued expenses include accruals for vacation leave amounting to ₱6.8 million and ₱4.3 million as at December 31, 2013 and 2012, respectively. Accrued taxes include withholding, gross receipts and documentary stamp tax payable.

17. Maturity Analysis of Assets and Liabilities

The following table shows an analysis of assets and liabilities analyzed according to whether they are expected to be recovered or settled within one year and beyond from reporting date:

	2013			2012		
	Less than Twelve Months	Over Twelve Months	Total	Less than Twelve Months	Over Twelve Months	Total
Financial Assets						
Cash and other cash items	₱4,610,455	₱–	4,610,455	₱2,903,536	₱–	2,903,536
Due from BSP	50,603,710	–	50,603,710	31,379,001	–	31,379,001
Due from other banks	83,462,403	–	83,462,403	74,480,762	–	74,480,762
AFS investments	–	–	–	3,000,000	5,000,000	8,000,000
HTM investment	16,129,410	9,948,693	26,078,103	–	26,236,233	26,236,233
Loans and receivables - at gross	816,407,948	138,585,465	954,993,413	552,331,804	27,211,730	579,543,534
Refundable deposit	–	312,000	312,000	–	256,668	256,668
	971,213,926	148,846,158	1,120,060,084	664,095,103	58,704,631	722,799,734
Nonfinancial Assets						
Property and equipment – gross	–	59,987,573	59,987,573	–	46,885,378	46,885,378
Investment properties - gross	–	18,853,238	18,853,238	–	24,181,322	24,181,322
Assets held by SPV - gross	–	7,793,447	7,793,447	–	8,788,674	8,788,674
Deferred tax asset	–	25,418,282	25,418,282	–	24,410,765	24,410,765
Retirement asset	–	–	–	–	–	–
Other assets	10,269,226	–	10,269,226	6,753,066	–	6,753,066
	10,269,226	112,052,540	122,321,766	₱6,753,066	₱104,266,139	111,019,205
Less: Allowance for credit and impairment losses			(55,758,379)			(32,781,703)
Unearned interest			(1,175)			(828,994)
Accumulated depreciation and amortization			(22,649,620)			(15,740,475)
			<u>₱1,163,972,676</u>			<u>₱784,467,767</u>
Financial Liabilities						
Deposit liabilities						
Demand	₱441,307	₱–	₱441,307	₱730,357	₱–	₱730,357
Savings	828,013,759	–	828,013,759	403,629,254	98,069,681	501,698,935
Bills payable	–	–	–	26,476,877	–	26,476,877
Accrued expenses	16,174,497	–	16,174,497	10,868,399	–	10,868,399
Accrued interest payable	2,020,693	–	2,020,693	2,126,144	–	2,126,144
Accounts payable	3,586,196	–	3,586,196	1,263,784	–	1,263,784
Dividends payable	40,148	–	40,148	–	–	–
Unearned service income	455,488	–	455,488	–	–	–
	850,732,088	–	850,732,088	445,094,815	98,069,681	543,164,496
Nonfinancial Liabilities						
Income tax payable	10,305,392	–	10,305,392	4,577,903	–	4,577,903
Accrued taxes	4,069,873	–	4,069,873	2,040,751	–	2,040,751
Other liabilities	2,042,628	–	2,042,628	631,775	–	631,775
Retirement liability	–	29,089,823	29,089,823	–	45,991,003	45,991,003
	₱866,831,346	₱29,089,823	₱896,239,804	₱452,345,224	₱144,060,684	₱596,405,928

18. Equity

Capital Stock

As at December 31, 2013 and 2012, the Bank's capital stock consists of:

	2013		2012	
	Shares	Amount	Shares	Amount
Common stock – ₱100 par value, 5,000,000 authorized shares				
Issued and outstanding	1,597,188	₱159,718,800	1,500,897	₱150,089,700
Subscribed	3,402,812	340,281,200	3,499,103	349,910,300
Subscription receivable		(248,980,062)		(284,486,175)
		₱251,019,938		₱215,513,825

Capital Management

The Bank's capital management aims to ensure that it complies with regulatory capital requirements and it maintains strong credit ratings and healthy capital ratios in order to support and sustain its business growth towards maximizing the shareholders' value.

The Bank manages its capital structure and appropriately effect adjustment according to the changes in economic conditions and the risk level it recognizes at every point of time in the course of its business operations. In order to maintain or adjust for good capital structure, the Bank carefully measures the amount of dividend payment to shareholders, call payment due from the capital subscribers or issue capital securities as necessary. No changes were made in the objectives, policies and processes from the previous years.

Regulatory Qualifying Capital

The determination of the Bank's compliance with the regulatory requirements and ratios is based on the amount of the Bank's unimpaired capital (regulatory net worth) reported to the BSP, determined on the basis of regulatory accounting policies which differ from PFRS in some respects.

In addition, the Capital Asset Ratio (CAR) of a bank, expressed as a percentage of qualifying capital to risk-weighted assets, should not be less than 10.0%. Qualifying capital and risk-weighted assets are computed based on BSP regulations. Risk-weighted assets consist of total assets less cash on hand, due from BSP, loans covered by hold-out on or assignment of deposits, loans or acceptances under letters of credit to the extent covered by margin deposits and other non-risk items determined by the Monetary Board (MB) of the BSP.

Under BSP Circular No. 360, effective July 1, 2003, the CAR is to be inclusive of a market risk charge. As at December 31, 2013 and 2012, the Bank's CAR is in compliance with the regulatory requirement. The CAR of the Bank as at December 31, 2013 and 2012, as reported to the BSP, is shown in the table below (amounts in thousands):

	2013	2012
Tier 1	₱264,256	₱197,354
Tier 2	8,341	5,724
Total qualifying capital	₱272,597	₱203,078
Risk-weighted assets	₱834,069	₱609,567
Tier 1 capital ratio	31.7%	32.4%
Tier 2 capital ratio	1.0%	0.9%
CAR	32.7%	33.3%

On March 4, 2011, the BSP issued BSP Circular No. 715 which amends the provisions of the Manual of Regulations for Banks on the minimum capitalization of banks and on the prerequisites for the grant of authority to establish a branch. Under the circular, for a thrift bank with head office located in areas other than Metro Manila and cities of Cebu and Davao, the required minimum capitalization (a) upon establishment of a new bank, (b) upon conversion of an existing bank from a lower to a higher category and vice versa, and (c) upon relocation of its head office in an area of higher classification, shall be ₱250.0 million from ₱52.0 million.

Financial Performance

The following basic ratios measure the financial performance of the Bank:

	2013	2012
Return on average equity	19.4%	18.81%
Return on average assets	4.0	4.17
Net interest margin	31	34.9

19. Retirement Benefits

The Bank, CARD MRI Development Institute, Inc. (CMDI), CARD Mutual Benefit Association (MBA), Inc., CARD Bank, Inc., CARD MRI Insurance Agency (CAMIA), Inc., CARD Business Development Service Foundation (BDSF), Inc., CARD MRI Information Technology, Inc. (CMIT), BotiCARD, Inc., and CARD, Inc. maintain a funded and formal noncontributory defined benefit retirement plan - the CARD MRI Multi-Employer Retirement Plan (MERP) - covering all of their regular employees. MERP has a projected unit cost format and is financed solely by the Bank and its related parties. MERP complies with the requirement of Republic Act No. 7641 (The Philippine Retirement Law). MERP provided lump sum benefits equivalent to at least one half (1/2) month salary for every year of service, a fraction of at least six months being considered as one whole year upon retirement, death, total and permanent disability, or early retirement after completion of at least ten (10) years of service with the participating companies. However, starting 2011, MERP provides lump sum benefits equivalent to 120.0% of final salary for every year of credited service, a fraction of at least six (6) months being considered as one whole year upon retirement, death, total and permanent disability, or early retirement after completion of at least one year of service with the participating companies.

Changes in net defined benefit liability of funded funds in 2013 are as follow:

	Net benefit cost in statement of income				Remeasurements in other comprehensive income							
	January 1, 2013 (As restated - Notes 2 and 25)	Current service cost	Net interest	Subtotal	Benefits Paid	Transfer (from) to plan net interest)	Return on plan assets (excluding amount included in net interest)	Actuarial changes arising from changes in demographic assumptions	Actuarial changes arising from changes in financial assumptions	Subtotal	Contribution by employer	December 31, 2013
Present value of defined benefit obligation	₱78,838,200	₱16,767,031	₱4,887,968	₱21,654,999	(₱224,527)	₱35,011,261	₱-	₱-	(₱13,186,715)	(₱13,186,715)	₱-	₱122,093,218
Fair value of plan Assets	(32,847,197)	-	(3,787,391)	(3,787,391)	224,527	(35,011,261)	110,707	-	-	110,707	(21,692,780)	(93,003,395)
Net defined benefit liability (asset)	₱45,991,003	₱16,767,031	₱1,100,577	₱17,867,608	₱-	₱-	₱110,707	₱-	(₱13,186,715)	(₱13,076,008)	(₱21,692,780)	₱29,089,823

Changes in net defined benefit liability of funded funds in 2012 are as follow:

	Net benefit cost in statement of income				Remeasurements in other comprehensive income							
	January 1, 2012 (As restated - Notes 2 and 25)	Current service cost	Net interest	Subtotal	Benefits Paid	Transfer (from) to plan	Return on plan assets (excluding amount included in net interest)	Actuarial changes arising from changes in demographic assumptions	Actuarial changes arising from changes in financial assumptions	Subtotal	Contribution by employer	December 31, 2012
Present value of defined benefit obligation	₱40,847,700	₱7,804,954	₱2,892,017	₱10,696,971	-	₱2,489,970	₱-	₱	₱24,803,559	₱24,803,559	₱-	₱78,838,200
Fair value of plan assets	(14,486,105)	-	(2,245,078)	(2,245,078)	-	(2,489,970)	2,679,398	-	-	2,679,398	(16,305,442)	(32,847,197)
Net defined benefit liability (asset)	₱26,361,595	₱7,804,954	₱646,939	₱8,451,893	₱-	₱-	₱2,679,398	₱-	₱24,803,559	₱27,482,957	(₱16,305,442)	₱45,991,003

The maximum economic benefit available is a combination of expected refunds from the plan and reductions in future contributions. The fair value of plan assets by each class as of the end of the reporting period are as follow:

	2013	2012
Cash and cash equivalents	₱50,417,140	₱19,799,822
Investments		
Debt securities		
Government securities	33,890,437	9,553,366
Other bonds	–	1,153,661
Equity securities	585,921	2,002,224
Mutual funds	1,283,447	–
Receivables	5,747,610	338,124
Other assets	1,078,840	–
Fair value of plan assets	₱93,003,395	₱32,847,197

All plan assets do not have quoted prices in active market except government bonds. Cash and cash equivalents are with reputable financial institutions and related parties and are deemed to be standard grade. Equity securities, mutual funds, receivables and other assets are unrated.

The plan assets have diverse investments and do not have any concentration risk.

Included in the fund assets are transactions with the Bank such as time deposits, investment in subordinated debts and investment in shares of stock.

The management performed an Asset-Liability Matching Study (ALM) annually. The overall investment policy and strategy of the Bank's defined benefit plans is guided by the objective of achieving an investment return which, together with contributions, ensures that there will be sufficient assets to pay pension benefits as they fall due while also mitigating the various risk of the plans.

The cost of defined benefit retirement plan as well as the present value of the defined benefit obligation (DBO) is determined using actuarial valuations. The actuarial valuation involves making various assumptions. The principal assumptions used in determining pension for the defined benefit plans are shown below:

	2013 %	2012 %
Discount rates	6.38%	6.20%
Future salary increases	12.00%	12.00%

The sensitivity analysis below has been determined based on reasonably possible changes of each significant assumption on the defined benefit obligation (DBO) as of the end of the reporting period, assuming if all other assumptions were held constant:

	Increase (Decrease) in Basis Points (bps)	Increase (Decrease) in Present Value of Obligation
Discount rates		
Decrease in DBO due to 250 bps increase in discount rate	+250 bps	(P55,603,986)
Increase in DBO due to 100 bps decrease in discount rate	-100 bps	35,309,918
Future salary increases		
Increase in DBO due to 200 bps increase in salary increase rate	+250 bps	71,732,827
Decrease in DBO due to 100 bps decrease in salary increase rate	-100 bps	(25,004,294)

The Bank plans to contribute P26.2 million to the defined benefit retirement plan in 2014.

The average duration of the defined benefit obligation at the end of the reporting period is 28.3 years.

Shown below is the maturity analysis of the undiscounted benefit payments:

	2013	2012
Less than 1 year	P—	P285,836
More than 1 year to 5 years	1,473,293	5,715,953
More than 5 years to 10 years	—	21,543,351
More than 10 years to 15 years	28,537,763	188,717,612
More than 15 years to 20 years	25,537,763	497,146,081
More than 20 years to 25 years	4 49,154,596	1,142,783,138
More than 25 years	7,202,210,038	1,307,323,520

20. Income Taxes

Under Philippine tax laws, the Bank is subject to percentage and other taxes as well as income taxes. Percentage and other taxes paid consist principally of gross receipts tax (GRT) and documentary stamp taxes presented as 'Taxes and licenses' in the statement of income.

Income taxes include final income tax which is paid at the rate of 20.0%. This is generally withheld on gross interest income from government securities and other deposit substitutes.

RA No. 9337, *An Act Amending National Internal Revenue Code* provides that the regular corporate income tax (RCIT) rate shall be 30.0%. Interest allowed as a deductible expense shall be reduced by 33.0% of interest income subject to final tax.

The law also provides for minimum corporate income tax (MCIT) of 2.0% on modified gross income which is paid if determined to be higher than RCIT. The excess of the MCIT over the RCIT can be carried-over and applied against the RCIT liability for the next three years.

Net operating loss carryover (NOLCO) is allowed as a deduction against the taxable income for RCIT purposes for a three-year period from the year of inception.

Current tax regulations also provide for the ceiling on the amount of entertainment, amusement and representation (EAR) expense that can be claimed as a deduction against taxable income. Under the regulation, EAR expense allowed as a deductible expense for a service company like the Bank is limited to the actual EAR paid or incurred but not to exceed 1.0% of net revenue. EAR expenses of the Bank amounted to ₱2.9 million and ₱2.2 million in 2013 and 2012, respectively.

Provision for income tax consists of:

	2013	2012
RCIT	₱22,747,099	₱10,739,949
Final tax	826,814	1,536,310
	23,573,913	12,276,259
Deferred	(4,930,320)	(8,018,679)
	₱18,643,593	₱4,257,580

Components of deferred tax assets - net are as follows:

	2013	2012 (As restated - Notes 2 and 25)
Deferred tax asset on:		
Allowance for credit and impairment losses	₱12,828,087	₱9,834,511
Accumulated vacation leave	2,051,186	1,279,798
Unamortized past service cost	3,496,447	2,442,573
Accumulated depreciation - investment Properties	98,807	168,267
Remeasurement loss on retirement plan	8,726,947	13,797,301
	27,201,474	27,522,450
Deferred tax liability on:		
Fair value adjustment on investment properties	1,783,192	3,111,685
	1,783,192	3,111,685
	₱25,418,282	₱24,410,765

The reconciliation between the statutory income tax and effective income tax follows:

	2013	2012
Statutory income tax	₱17,913,149	₱ 9,355,513
Income tax effects of:		
Change in unrecognized deferred tax assets	(4,103,506)	(4,418,090)
Nondeductible operating expenses	5,156,369	84,662
Interest income subject to final tax and nontaxable income	(1,290,018)	(704,504)
Nontaxable income	967,599	(60,000)
Provision for income tax	₱18,643,593	₱4,257,581

21. Related Party Transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. The Bank's related parties include:

- key management personnel, close family members of key management personnel and entities which are controlled, significantly influenced by or for which significant voting power is held by key management personnel or their close family members,
- post-employment benefit plans for the benefit of the Bank's employees, and
- entities under common significant influence (CARD MRI entities).

The Bank has several business relationships with related parties. Transactions with such parties are made in the ordinary course of business and on substantially same terms, including interest and collateral, as those prevailing at the time for comparable transactions with other parties. These transactions also did not involve more than the normal risk of collectability or present other unfavorable conditions.

Transactions with retirement plans

Under PFRS, certain post-employment benefit plans are considered as related parties. CARD MERP is managed by the CARD Employee EMPC. The plan assets are invested in time deposits and special savings accounts and government bonds (Note 19).

Remunerations of Directors and other Key Management Personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly. The Bank considers the members of the board of directors and senior management to constitute key management personnel for purposes of PAS 24.

The compensation of key management personnel included under 'Compensation and fringe benefits' in the statement of income follows (in millions):

	2013	2012
Short-term employee benefits	₱7.8	₱5.9
Post employment benefits	4.3	3.2
	₱12.1	₱9.1

The Bank also provides banking services to directors and other key management personnel and persons connected to them.

Other related party transactions

Transactions between the Bank and its key management personnel meet the definition of related party transactions. Transactions between the Bank and its affiliates within the CARD MRI, also qualify as related party transactions.

Loans receivables

As at December 31, 2013 and 2012, the Bank has no loan outstanding that was granted to related parties.

Deposit liabilities, accounts receivable and accounts payable

The table below shows the deposit liabilities, accounts receivable and accounts payable held by the Bank for key management personnel and affiliates as at December 31, 2013 and (in thousands):

	December 31, 2013		
Category	Amount / Volume	Outstanding Balance	Nature, Terms and Conditions
Key Management Personnel			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 4.0%
Deposits	₱791	₱1,307	
Withdrawals	(135)		
CARD, Inc. (shareholder)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 4.0%.
Deposits	92,443	62,094	
Withdrawals	(67,372)		
Accounts receivables			The amount represents the CARD, Inc.'s share of expenses still payable to the Bank.
Share of expenses	1,066	–	
Collections	(1,066)		
Accounts payable			This represents payment of loans from members under CARD Inc.
Share of expenses	2,373.	16	
Remittances	(2,607)		
CMDI (other related party)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 2.0% to 4.0%.
Deposits	17,881	9,742	
Withdrawals	(9,594)		
Accounts receivables			The amount represents the CMDI's share of expenses still payable to the Bank.
Charges	3,250	–	
Remittances	(3,250)		
Accounts payable			The amount represents the Bank's share of expenses still payable to CMDI.
Charges	6,468	443	
Payments	(7,300)		
CARD MBA (other related party)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 2.0% to 5.5%.
Deposits	327,787	90,858	
Withdrawals	(243,622)		
Accounts receivables			The amount represents the CARD MBA's share of expenses payable to the Bank.
Charges	10,252	3,519	
Collections	(14,053)		
Accounts payable			These are savings accounts with annual interest rates ranging from 2.0% to 4.0%
Premium collections	504	–	
Remittances	(504)		
CAMIA (other related party)			
Deposit liabilities			These are savings account with annual interest rates ranging from 1.5% to 4.0%.
Deposits	3,290	3,340	
Withdrawals	(2,950)		
Accounts payable			This pertains to insurance for the employees of the Bank.
Charges	2,606	–	
Payments	(2,606)		
CARD BDSF (other related party)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 4.0%.
Deposits	7,854	7,448	
Withdrawals	(6,485)		
Accounts receivable			The amount represents the CARD BDSF's share of expenses payable to the Bank.
Charges	31	–	
Payments	(31)		
Accounts payable			The amount represents the Bank's share of expenses still payable to CARD BDSF
Charges	662	2	
Payments	(744)		

(Forward)

December 31, 2013

Category	Amount / Volume	Outstanding Balance	Nature, Terms and Conditions
CARD MERP			
(retirement plan)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 4.0%.
Deposits	₱20,538	₱115,878	
Withdrawals	(926)		
Accounts payable			These amount is payment for retirement of employees
Charges	21,692,780	–	
Payments	(21,692,780)		
CMIT (other related party)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 4.0%.
Deposits	4,610	20,564	
Withdrawals	(10,122)		
Accounts payable			These payments are for system maintenance and enhancement of system.
Premium collections	5,268	–	
Remittances	(5,268)		
BotiCARD			
(other related party)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 4.0%.
Deposits	6,997	2,631	
Withdrawals	(4,693)		
Account receivable			The amount represents share of expenses payable to the Bank.
Charges	24	–	
Payments	(24)		
Account payable		21,600	The amount represents the Bank's share of expenses still payable to BotiCARD.
Charges	305,103		
Payments	(283,503)		
CARD EMPC (shareholder)			
Deposit liabilities			These are savings accounts with annual interest rates ranging from 1.5% to 2.0%.
Deposits	7,120	710	
Withdrawals	(12,764)		
Account receivable			The amount represents share of expenses payable to the Bank.
Charges	240	–	
Payments	(240)		
Account payable			The amount represents the Bank's share of staff monthly contribution.
Charges	3,084	3,084	
Payments	–		
CARD LEASING			
(other related party)			
Accounts payable			These are billings for issuance of supplies and operating lease transactions.
Charges	7,841	–	
Payments	(7,841)		
Key Management Personnel			
Deposit liabilities		651	These are savings accounts with annual interest rates ranging from 2.0% to 3.0%.
Deposits	1,861		
Withdrawals	(1,379)		
CARD, Inc. (shareholder)			
Deposit liabilities		37,023	These are savings accounts with annual interest rates ranging from 2.0% to 4.5%.
Deposits	155,781		
Withdrawals	(149,439)		
Accounts receivables		–	The amount represents the CARD, Inc.' share of expenses still payable to the Bank.
Share of expenses	574,640		
Collections	(574,640)		
Accounts payable:		250	This represents payment of loans from members under CARD Inc.
Share of expenses	523,		
Remittances	(278)		

(Forward)



December 31, 2013

Category	Amount / Volume	Outstanding Balance	Nature, Terms and Conditions
CMDI (other related party)			
Deposit liabilities		1,455	These are savings accounts with annual interest rates ranging from 2.0% to 4.0%.
Deposits	13,556		
Withdrawals	(1,213)		
Accounts receivables		–	The amount represents the CMDI's share of expenses still payable to the Bank.
Charges	9,168		
Remittances	(9,168)		
Accounts payable:		1,275	The amount represents the Bank's share of expenses still payable to CMDI.
Charges	614,248		
Payments	(771,664)		
CARD MBA (other related party)			
Deposit liabilities		6,693	These are savings accounts with annual interest rates ranging from 2.0% to 5.5%.
Deposits	169,875		
Withdrawals	(163,566)		
Accounts receivables		282	The amount represents the CARD MBA's share of expenses payable to the Bank.
Charges	364		
Collections	(82)		
Accounts payable		–	These are savings accounts with annual interest rates ranging from 2.0% to 4.0%.
Premium collections	123,883,860		
Remittances	(127,924,629)		
CAMIA (other related party)			
Deposit liabilities		3,000	These are savings account with annual interest rates ranging from 2.0% to 3.8%.
Deposits	3,000		
Withdrawals	–		
Accounts payable		–	This pertains to insurance for the employees of the Bank.
Charges	1,753,983		
Payments	(1,754,983)		
CARD BDSF (other related party)			
Deposit liabilities		6,079	These are savings accounts with annual interest rates ranging from 2.0% to 4.5%.
Deposits	13,114		
Withdrawals	(8,138)		
Accounts receivable		–	The amount represents the CARD BDSF's share of expenses payable to the Bank.
Charges	1,941		
Payments	(1,941)		
Accounts payable		84	The amount represents the Bank's share of expenses still payable to CARD BDSF
Charges	462		
Payments	(559)		
CARD MERP (retirement plan)			
Deposit liabilities		96,266	These are savings accounts with annual interest rates ranging from 2.0% to 5.5%.
Deposits	84,323		
Withdrawals	(36,149)		
Accounts payable		–	These amount is payment for retirement of employees
Charges	10,806,128		
Payments	(10,806,128)		
CMIT (other related party)			
Deposit liabilities		26,076	These are savings accounts with annual interest rates ranging from 2.0% to 4.5%.
Deposits	5,710		
Withdrawals	(6,379)		
Accounts payable		–	These payment is for system maintenance and enhancement of system
Premium collections	6,571,913		
Remittances	(6,571,913)		
BotiCARD (other related party)			
Deposit liabilities		327	These are savings accounts with annual interest rates ranging from 2.0% to 2.5%.
Deposits	827		
Withdrawals	(500)		
CARD EMPC (shareholder)			
Deposit liabilities		6,354	These are savings accounts with annual interest rates ranging from 2.5% to 3.8%.
Deposits	6,392		
Withdrawals	(38)		



Others

Other related party transactions of the Bank are as follows:

	2013	2012	Nature, Terms and Conditions
Statement of Income (in volume)			
CARD, Inc. (shareholder)			
Occupancy	₱60,000	₱60,000	An establishment owned by CARD, Inc. is being leased to the Bank. Lease contract is renewable annually.
Interest expense	1,580,298	2,381	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 4.5%.
CMDI (other related party)			
Seminars and trainings expense	6,467,769	18,724,951	The Bank engaged CMDI for training and development of its members and employees (shown as part of 'Employee trainings' in the statement of income).
Interest expense	145,022	2,380	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 4.5%.
CARD MBA (other related party)			
Interest expense	1,229,097	1,514	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 5.0%.
CAMIA (other related party)			
Interest expense	1,203,87	18	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 3.8%.
CARD BDSF (other related party)			
Transportation and travel expense	823,800	–	Relates to the lease of motorcycles with a term of three years. All contracts were pre-terminated in the beginning of 2012.
Interest expense	217,660	309,800	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 4.0%.
CARD MERP (retirement plan)			
Retirement expense	17,867,608	72,353,121	This pertains to the funded and formal noncontributory defined benefit retirement plan of the Bank that is handled by CARD MERP (Note 19).
CMIT (other related party)			
Information technology	–	3,680,300	This pertains to the CMIT's rendered services in relation to upgrade of the Bank's core banking system (CBS).
System maintenance services	5,901,205	6,571,913	This represents information technology-related support services to the Bank including software maintenance of the Bank's CARD e-System, hardware maintenance, set-up of network and centers and technical support, among others
Interest expense	609,892	2,810	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 6.0%.
BotiCARD (other related party)			
Interest expense	99,018	155,502	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 3.5%.
CARD EMPC (shareholder)			
Interest expense	250,590	198	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 3.5%.
CARD MERP (other related party)			
Retirement expense	17,867,608	8,451,893	This pertains to the funded and formal noncontributory defined benefit retirement plan of the Bank that is handled by CARD MERP (Note 19).
Interest expense	4,868,143	2,810	Pertains to interest on savings accounts with annual rates ranging from 2.0% to 6.0%.

Regulatory Reporting

As required by BSP, the Bank discloses loan transactions with investees and with certain directors, officers, stockholders and related interests (DOSRI). Existing banking regulations limit the amount of individual loans to DOSRI, 70.00% of which must be secured, to the total of their respective deposits and book value of their respective investments in the lending company within the Bank.

In the aggregate, loans to DOSRI generally should not exceed total equity or 15.00% of total loan portfolio, whichever is lower. As at December 31, 2013 and 2012, the Bank is in compliance with the regulatory requirements.

BSP Circular No. 423 dated March 15, 2004 amended the definition of DOSRI accounts. On October 8, 2010, BSP Circular No. 695 is issued to provide guidance on the definition of Related Interest.

As at December 31, 2013 and 2012, there were no loans, other credit accommodations and guarantees classified as DOSRI accounts under the existing regulations as shown in the table below:

	2013	2012
Total outstanding DOSRI accounts	₱—	₱—
Percent of DOSRI accounts granted prior to effectivity of BSP Circular No. 423 to total loans	0.00%	0.00%
Percent of DOSRI accounts granted after effectivity of BSP Circular No. 423 to total loans	0.00%	0.00%
Percent of DOSRI accounts to total loans	0.00%	0.00%
Percent of unsecured DOSRI accounts to total DOSRI accounts	0.00%	0.00%
Percent of past due DOSRI accounts to total DOSRI accounts	0.00%	0.00%
Percent of nonaccruing DOSRI accounts to total DOSRI accounts	0.00%	0.00%

22. Lease Contracts

As lessee

The Bank leases the premises occupied by some of its branches in which lease payments are subjected to escalation clauses ranges from 3.0% to 10.0%. The lease contracts are for the periods ranging from one to ten years and are renewable upon mutual agreement between the Bank and the lessors such as CARD, Inc., employees and third-party lessors.

The future aggregate minimum lease payments under non-cancelable operating leases follow:

	2013	2012
Within one year	₱4,948,382	₱1,839,500
Beyond one year but not more than five years	7,895,604	5,085,706
	₱12,843,986	₱6,925,206

23. Commitments and Contingencies

There are commitments and contingent liabilities that arise in the normal course of the Bank's operations which are not reflected in the accompanying financial statements. As at December 31, 2013 and 2012, management is of the opinion that losses, if any, from these commitments and contingencies will not have a material effect on the Bank's financial statements.

24. Notes to Statements of Cash Flows

Noncash activities of the Bank consist of the following:

	2013	2012
Noncash investing activities:		
Foreclosure of investment properties	₱150,000	₱585,000
Transfer from investment properties to property and equipment	—	(3,748,530)

25. Restatement in the 2012 and 2011 Financial Statements

Change in accounting policy

In 2013, the Bank made certain adjustments to apply the change in accounting policy on the accounting for retirement obligation in accordance with amended PAS 19, *Employee Benefits* (effective January 1, 2013) with retrospective application that requires the restatement of the latest comparative period and the beginning balance of the latest comparative period.

The Bank reviewed its existing employee benefits and determined that the amended standard has significant impact on its accounting for retirement benefits. The Bank obtained the services of an external actuary to compute the impact to the financial statements upon adoption of the standard. The Bank chose to close to 'Remeasurement gain (loss) on retirement plan' the net effect of all transition adjustments as at January 1, 2012 (the transition date) upon retrospective application of PAS 19 (Revised).

The effects of the change in accounting policy made are detailed below:

	As at December 31, 2012		
	As previously reported	Change in accounting policy (Note 2)	As restated
Statement of Financial Position			
<u>Assets</u>			
Retirement asset	₱1,450,585	(₱1,450,585)	₱—
Deferred tax asset	10,178,288	14,232,477	24,410,765
<u>Liabilities and equity</u>			
Retirement liability	—	45,991,003	45,991,003
Surplus	5,757,125	1,054,784	6,811,909

For the year ended December 31, 2012			
	As previously reported	Change in accounting policy (Note 2)	As restated
Statement of Comprehensive Income			
<u>Net income (loss)</u>			
Compensation and fringe benefits	₱80,068,681	(₱2,354,235)	₱77,714,446
<u>Other comprehensive income</u>			
Loss on remeasurement of retirement plan	–	(19,238,070)	(19,238,070)
As at January 1, 2012			
	As previously reported	Change in accounting policy (Note 2)	As restated
Statement of Financial Position			
<u>Assets</u>			
Deferred tax asset	₱2,159,609	₱6,693,860	₱8,853,469
<u>Liabilities and equity</u>			
Retirement liability	4,048,729	22,312,866	26,361,595
Surplus	(19,522,372)	(593,180)	(20,115,552)

26. Approval for the Release of Financial Statements

The accompanying financial statements were approved and authorized for issue by the BOD on April 12, 2014.

27. Supplementary Information Required under Revenue Regulations 15-2010

On November 25, 2010, the BIR issued RR 15-2010 prescribing the manner of compliance in connection with the preparation and submission of financial statements accompanying the tax returns. It includes provisions for additional disclosure requirements in the notes to the financial statements, particularly on taxes, duties and licenses paid or accrued during the year.

The components of 'Taxes and licenses' in 2013 follow:

Gross receipts tax	17,898,932
Business permits and licenses	1,331,745
Documentary stamp tax (DST)	259,254
Real property tax	226,101
Others	384,885
	₱20,100,917

In 2013, withholding taxes lodged under 'Accrued taxes' account are categorized into:

Paid:

Withholding taxes on compensation and benefits	₱4,191,459
Final withholding tax on interest expense	2,095,380
Expanded withholding tax	773,981
	<u>₱7,060,820</u>

Accrued:

Withholding taxes on compensation and benefits	₱1,073,398
Final withholding tax on interest expense	650,822
Expanded withholding tax	310,330
	<u>₱2,034,550</u>

CARD SME BANK, INC., A THRIFT BANK

INDEX TO THE FINANCIAL STATEMENTS AND SUPPLEMENTARY SCHEDULES

- Schedule 1: Schedule of all Philippine Financial Reporting Standards (PFRS) effective as at December 31, 2013 [which consist of PFRSs, Philippine Accounting Standards (PAS) and Philippine Interpretations]
- Schedule 2: Schedule of Financial Soundness Indicators

CARD SME Bank, Inc., A Thrift Bank**SUPPLEMENTARY SCHEDULE OF ALL PHILIPPINE FINANCIAL REPORTING STANDARDS (PFRSs) [which consist of PFRSs, Philippine Accounting Standards (PAS) and Philippine Interpretations] effective as at December 31, 2013**

List of Philippine Financial Reporting Standards (PFRSs) [which consists of PFRSs, Philippine Accounting Standards (PASs) and Philippine Interpretations] effective as at December 31, 2013, unless otherwise indicated:

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS Effective as of December 31, 2013		Adopted	Not Adopted	Not Applicable
Framework for the Preparation and Presentation of Financial Statements Conceptual Framework Phase A: Objectives and qualitative characteristics		X		
PFRSs Practice Statement Management Commentary		X		
Philippine Financial Reporting Standards				
PFRS 1 (Revised)	First-time Adoption of Philippine Financial Reporting Standards	X		
	Amendments to PFRS 1 and PAS 27: Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate			X
	Amendments to PFRS 1: Additional Exemptions for First-time Adopters			X
	Amendment to PFRS 1: Limited Exemption from Comparative PFRS 7 Disclosures for First-time Adopters			X
	Amendments to PFRS 1: Severe Hyperinflation and Removal of Fixed Date for First-time Adopters			X
	Amendments to PFRS 1: Government Loans			X
	Improvement to PFRS 1: Borrowing Costs			X
	Improvement to PFRS 1: Meaning of 'Effective PFRSs'			X
PFRS 2	Share-based Payment			X
	Amendments to PFRS 2: Vesting Conditions and Cancellations			X
	Amendments to PFRS 2: Group Cash-settled Share-based Payment Transactions			X
	Improvement to PFRS 2: Definition of Vesting Condition			X
PFRS 3	Business Combinations			X

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS Effective as of December 31, 2013		Adopted	Not Adopted	Not Applicable
(Revised)	Improvement to PFRS 3: Accounting for Contingent Consideration in a Business Combination			X
	Improvement to PFRS 3: Scope Exceptions for Joint Arrangements			X
PFRS 4	Insurance Contracts			X
	Amendments to PAS 39 and PFRS 4: Financial Guarantee Contracts			X
PFRS 5	Non-current Assets Held for Sale and Discontinued Operations			X
PFRS 6	Exploration for and Evaluation of Mineral Resources			X
PFRS 7	Financial Instruments: Disclosures	X		
	Amendments to PFRS 7: Transition	X		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets	X		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets - Effective Date and Transition	X		
	Amendments to PFRS 7: Improving Disclosures about Financial Instruments	X		
	Amendments to PFRS 7: Disclosures - Transfers of Financial Assets	X		
	Amendments to PFRS 7: Disclosures - Offsetting Financial Assets and Financial Liabilities	X		
	Amendments to PFRS 7: Mandatory Effective Date of PFRS 9 and Transition Disclosures		X*	
PFRS 8	Operating Segments			X
	Improvement to PFRS 8: Aggregation of Operating Segments and Reconciliation of Total of the Reportable Segments' Assets to the Entity's Assets			X
PFRS 9	Financial Instruments		X*	
	Amendments to PFRS 9: Mandatory Effective Date of PFRS 9 and Transition Disclosures		X*	
PFRS 10	Consolidated Financial Statements			X
	Amendment to PFRS 10: Investment Entities			X
PFRS 11	Joint Arrangements			X
PFRS 12	Disclosure of Interests in Other Entities			X

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS Effective as of December 31, 2013		Adopted	Not Adopted	Not Applicable
	Amendment to PFRS 12: Investment Entities			X
PFRS 13	Fair Value Measurement	X		
	Improvement to PFRS 13: Short-term Receivables and Payables	X*		
	Improvement to PFRS 13: Portfolio Exception			X
Philippine Accounting Standards				
PAS 1 (Revised)	Presentation of Financial Statements	X		
	Amendment to PAS 1: Capital Disclosures	X		
	Amendments to PAS 32 and PAS 1: Puttable Financial Instruments and Obligations Arising on Liquidation			X
	Amendments to PAS 1: Presentation of Items of Other Comprehensive Income	X		
	Improvement to PAS 1: Clarification of the Requirements for Comparative Information	X		
PAS 2	Inventories			X
PAS 7	Statement of Cash Flows	X		
PAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	X		
PAS 10	Events after the Balance Sheet Date	X		
PAS 11	Construction Contracts			X
PAS 12	Income Taxes	X		
	Amendment to PAS 12 - Deferred Tax: Recovery of Underlying Assets	X		
PAS 16	Property, Plant and Equipment	X		
	Improvement to PAS 16: Classification of Servicing Equipment			X
	Improvement to PAS 16: Revaluation Method - Proportionate Restatement of Accumulated Depreciation			X
PAS 17	Leases	X		
PAS 18	Revenue	X		
PAS 19 (Amended)	Employee Benefits	X		
	Amendments to PAS 19: Actuarial Gains and Losses, Group Plans and Disclosures	X		
	Amendments to PAS 19: Defined Benefit Plans:	X		

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS Effective as of December 31, 2013		Adopted	Not Adopted	Not Applicable
	Employee Contributions			
PAS 20	Accounting for Government Grants and Disclosure of Government Assistance			X
PAS 21	The Effects of Changes in Foreign Exchange Rates			X
	Amendment: Net Investment in a Foreign Operation			X
PAS 23	Borrowing Costs	X		
PAS 24	Related Party Disclosures	X		
	Improvement to PAS 24: Key Management Personnel	X		
PAS 26	Accounting and Reporting by Retirement Benefit Plans	X		
PAS 27 (Amended)	Separate Financial Statements			X
	Amendment to PAS 27: Investment Entities			X
PAS 28 (Amended)	Investments in Associates and Joint Ventures			X
PAS 29	Financial Reporting in Hyperinflationary Economies			X
PAS 32	Financial Instruments: Disclosure and Presentation	X		
	Amendments to PAS 32 and PAS 1: Puttable Financial Instruments and Obligations Arising on Liquidation			X
	Amendment to PAS 32: Classification of Rights Issues			X
	Improvement to PAS 32: Tax Effect of Distribution to Holders of Equity Instruments			X
	Amendments to PAS 32: Offsetting Financial Assets and Financial Liabilities		X*	
PAS 33	Earnings per Share			X
PAS 34	Interim Financial Reporting			X
	Improvement to PAS 34: Interim Financial Reporting and Segment Information for Total Assets and Liabilities			X
PAS 36	Impairment of Assets	X		
	Amendments to PAS 36: Recoverable Amount Disclosures for Non-Financial Assets	X*		
PAS 37	Provisions, Contingent Liabilities and Contingent Assets	X		
PAS 38	Intangible Assets			X
	Improvement to PAS 38: Revaluation Method - Proportionate Restatement of Accumulated Amortization			X

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS Effective as of December 31, 2013		Adopted	Not Adopted	Not Applicable
PAS 39	Financial Instruments: Recognition and Measurement	X		
	Amendments to PAS 39: Transition and Initial Recognition of Financial Assets and Financial Liabilities	X		
	Amendments to PAS 39: Cash Flow Hedge Accounting of Forecast Intragroup Transactions			X
	Amendments to PAS 39: The Fair Value Option			X
	Amendments to PAS 39 and PFRS 4: Financial Guarantee Contracts			X
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets			X
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets – Effective Date and Transition			X
	Amendments to Philippine Interpretation IFRIC 9 and PAS 39: Embedded Derivatives			X
	Amendment to PAS 39: Eligible Hedged Items			X
	Amendments to PAS 39: Novation of Derivatives and Continuation of Hedge Accounting		X*	
PAS 40	Investment Property	X		
	Improvement to PAS 40: Interrelationship of PFRS 3 and PAS 40 when Classifying Property as Investment Property or Owner-Occupied Property	X		
PAS 41	Agriculture			X
Philippine Interpretations				
IFRIC 1	Changes in Existing Decommissioning, Restoration and Similar Liabilities			X
IFRIC 2	Members' Share in Co-operative Entities and Similar Instruments			X
IFRIC 4	<i>Determining Whether an Arrangement Contains a Lease</i>	X		
IFRIC 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds			X
IFRIC 6	<i>Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment</i>			X
IFRIC 7	<i>Applying the Restatement Approach under PAS 29 Financial Reporting in Hyperinflationary Economies</i>			X
IFRIC 8	<i>Scope of PFRS 2</i>			X

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS Effective as of December 31, 2013		Adopted	Not Adopted	Not Applicable
IFRIC 9	Reassessment of Embedded Derivatives			X
	Amendments to Philippine Interpretation IFRIC-9 and PAS 39: Embedded Derivatives			X
IFRIC 10	<i>Interim Financial Reporting and Impairment</i>			X
IFRIC 11	PFRS 2- Group and Treasury Share Transactions			X
IFRIC 12	Service Concession Arrangements			X
IFRIC 13	Customer Loyalty Programmes			X
IFRIC 14	The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction			X
	Amendments to Philippine Interpretations IFRIC- 14, Prepayments of a Minimum Funding Requirement			X
IFRIC 16	Hedges of a Net Investment in a Foreign Operation			X
IFRIC 17	Distributions of Non-cash Assets to Owners			X
IFRIC 18	Transfers of Assets from Customers			X
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments			X
IFRIC 20	Stripping Costs in the Production Phase of a Surface Mine			X
IFRIC 21	Levies			X
SIC-7	Introduction of the Euro			X
SIC-10	Government Assistance - No Specific Relation to Operating Activities			X
SIC-15	Operating Leases - Incentives			X
SIC-21	Income Taxes - Recovery of Revalued Non-Depreciable Assets			X
SIC-25	Income Taxes - Changes in the Tax Status of an Entity or its Shareholders			X
SIC-27	Evaluating the Substance of Transactions Involving the Legal Form of a Lease	X		
SIC-29	Service Concession Arrangements: Disclosures			X
SIC-31	Revenue - Barter Transactions Involving Advertising Services			X
SIC-32	Intangible Assets - Web Site Costs			X

*Note: The Bank has not early adopted standards and amendments which are not yet effective as at January 1, 2013.

CARD SME BANK INC., A THRIFT BANK

**SUPPLEMENTARY SCHEDULE OF FINANCIAL SOUNDNESS RATIOS
AS AT DECEMBER 31, 2013 AND 2012**

Liquidity ratio

	2013	2012
Liquid assets	₱138,676,568	₱116,763,299
Total deposits	828,455,066	502,429,292
Ratio of liquid assets to total deposits	16.7%	23.2%

Liquid assets consist of cash, due from BSP and other banks and available for sale investments.

Debt to equity ratio

	2013	2012
Average total liabilities	₱665,442,179	₱412,160,010
Average total equity	227,862,073	157,409,755
Ratio of debt to equity	292.0%	261.8%

Assets-to-equity ratio

	2013	2012
Average total assets	₱974,220,222	₱673,232,907
Average total equity	227,897,356	157,409,755
Ratio of total assets to equity	427.5%	427.7%

Interest rate coverage ratio

	2013	2012
Income before income tax	₱59,710,497	₱31,185,042
Interest expense	18,793,068	19,652,886
Interest coverage ratio	317.7%	158.7%

Profitability ratios

	2013	2012
Net income	₱41,066,904	₱27,633,732
Average total equity	227,897,356	157,409,755
Return on average equity	18.0%	17.6%
Net income	₱41,066,904	₱27,633,732
Average total assets	974,220,222	673,232,907
Return on average assets	4.2%	4.1%
Net financial margin	₱331,257,743	₱208,258,507
Average interest earning assets	1,071,118,630	596,696,600
Net interest margin on average earning assets	30.9%	34.9%



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