BREAKING BARRIERS

CARD SME BANK, INC.
ANNUAL REPORT 2014

ABOUT THE COVER

Most annual reports trumpet the success of a company. The numbers tell the story; the charts summarize growth. Our success goes beyond our financial data. We are proudest of the people who have succeeded through our financial programs. One of the thousands of people we have touched is Joveline Rafanan, owner of Ka Popoy's Chicharon in Pangil, Laguna.

We are a financial institution, but at its core, CARD SME Bank is a people institution. We empower, we support, and help them grow in ways that charts cannot measure. We help transform lives towards concrete success.

We are in the business of hope.

VISION

CARD SME Bank, Inc. supports CARD MRI's vision statement as a group of mutually reinforcing institutions that is dedicated to empower the poor by upholding the core values of competence, family spirit, integrity, stewardship, humility, culture of excellence, and simplicity. As one of the institutions that comprise CARD MRI and in support of its mission, CARD SME Bank 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.

MISSION

CARD SME Bank, Inc. is committed to:

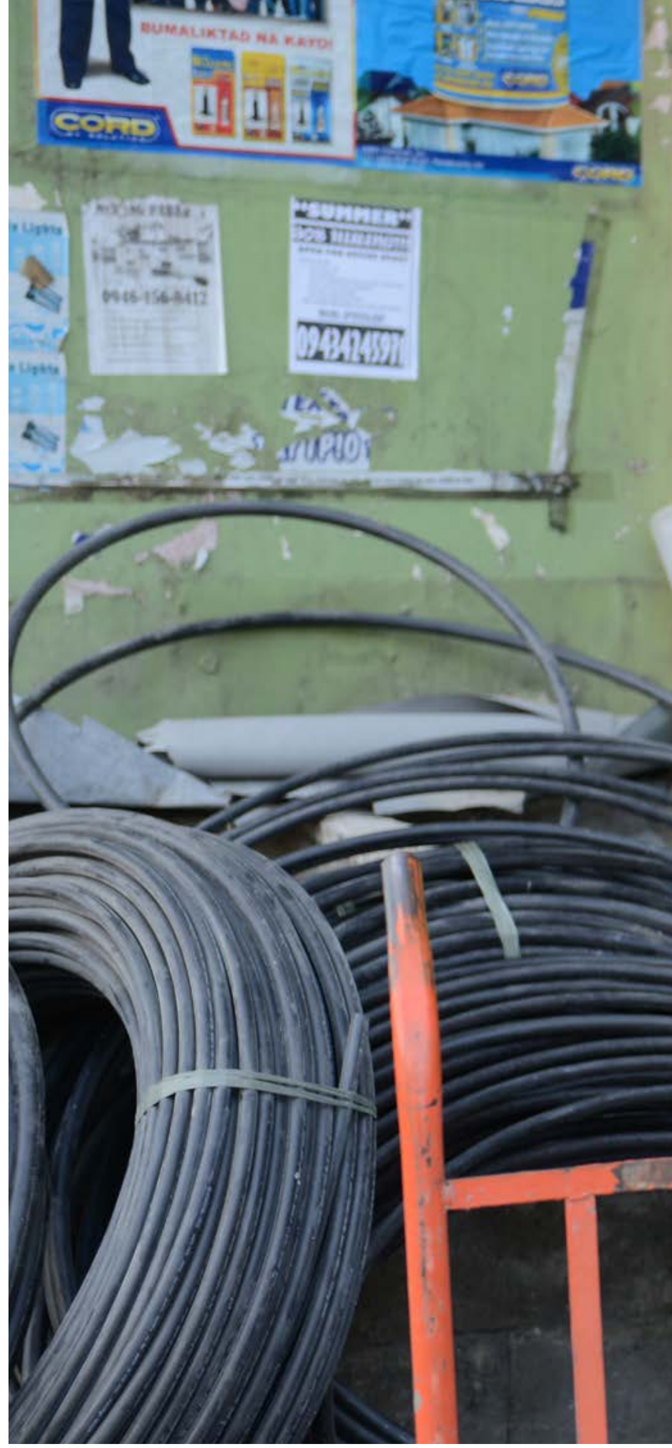
- provide banking services especially designed for landless rural workers by bringing bank services to community sites and accommodating the least financial transactions within their affordability;

- provide collateralized and non-collateralized loans to non-bankable but viable microfinance and SME projects; and

- grow the bank's SME lending to become the pre-eminent SME Bank in the Philippines to be able to reach more SME beneficiaries.

A LIGHT BULB MOMENT

Julito de Torres
Sto. Tomas, Batangas



I was a sales agent in a commercial company for light fixtures when I suddenly thought of starting my own business during my sales rounds. From having just a small shop, my business grew and flourished.

To open a small electrical supplies store, I pawned the land my mother gave me and raised P270,000. I kept my regular job while my wife manned the store, then I decided to focus on the business in 2008.

Your first capital is commitment

It was a huge risk to quit my job, but I knew it was time to expand. Just like any other member, I started with a meager loan of P5,000. I initially asked myself, what can P5,000 even do? But still, I continued to persevere. I always make sure I attend my center meetings every Monday.

Patience is indeed a virtue. After some time, I was granted a loan of P150,000. With this loan, I bought an elf truck—until then, I had only used a tricycle. I was finally able to take on bigger orders, and with another P300,000 loan, I opened a much bigger store within the Sto. Tomas town proper. I started selling gravel, sand and building materials.

After banking with CARD SME Bank for several years, I have proven that this bank is hard at work to ensure that it provides quality service to its clients and to remain relevant to its market.

As much as we trust our bank, we, their clients, know that they reciprocate their trust to us, too. They do not ask for any kind of collateral at all. This may be due to the fact that their advocacy is to eradicate poverty in the country. Their focus is to empower and develop people. This means profit often takes a backseat.

Despite putting their social cause on top of their priorities, CARD SME Bank remains a sustainable bank. In fact, it has already prepared itself for the ASEAN Integration in 2015. I am confident that my bank of choice is ready to compete amidst the heavy competition that may arise during the integration.

It is no doubt that CARD SME Bank stays true to its brand. It is a bank that grows with you.

ANYONE CAN APPROACH CARD SME BANK

Even owners of larger, established businesses can approach CARD SME Bank. We have the facility and the products to help both SMEs and bigger companies achieve their business goals. Depending on your needs – to bridge a cash flow gap, a planned expansion, additional working capital, even a plan to buy your dream home – CARD SME Bank is here to help you out. We are here to help you achieve your dreams.

READY TO SERVE YOU

Bigger banks have an acknowledged edge in terms of technology and this is something that we have not only recognized but is also addressing. We will be undertaking an extensive overhaul of our core banking system. After the improvements, all of our branches will be totally online, allowing us to better serve our clients – among them, being able to transact at any branches. We will also be rolling out ATMs, another result of this technological improvement.

But even with technological advancements, CARD SME Bank has one advantage over our competitors – we are familiar with the landscape of our trading areas and the people and communities we serve. Our strength always has been and will remain, our heartfelt person-to-person service.

A THREAD OF HOPE

Dolores Rivera de Ramos
Lumban, Laguna

I was born into a very poor family. When I was just 13 years old, I had to drop out of school to help put food on the table despite being a promising honor student. I became a seamstress at one of the many barong* factories in Lumban, the country's center of barong manufacturing. I learned how to embroider on jusi and piña, stopping only when I got married.

I still dreamed of a better future for my family. In 1999, I joined a paluwagan, an informal form of saving and lending, and used the P5,000 I saved to buy a roll of jusi. I showed embroidered samples to stores in Divisoria, collected orders, and worked late into the night to complete them.

Small but steady

My business was small but steady. When my husband lost his job in NAIA, he joined me in my business as a painter. However, we did not have the funds to buy more sewing machines and hire more seamstresses. When I got pregnant, I had to close my shop until I was strong enough to work.

In 2003, I rented a stall in San Pablo. A fellow vendor told me how he had gotten an P80,000 loan from CARD SME Bank. I went to the Lumban, Laguna branch and was able

*Barong is the national costume for Filipino men.

to get a P5,000 loan, just enough to buy the sewing machine I've always prayed for.

The big break

I worked hard to pay off the loan and was able to borrow larger amounts as my credit standing improved. My business blossomed but the workload prevented me from attending the weekly center meetings, a prerequisite for any loan approval. When my P10,000 loan was denied, I got so discouraged that I was tempted to quit. Any other bank would have simply let me go.

But CARD SME Bank is not just a bank, it is a support system. A friendly CARD SME Bank representative found out about my plans to leave and asked me what was wrong. After listening to my case and discovering that I already had a stall and delivered barongs to several Divisoria retailers, I was told that I was eligible for the CARD SME Bank loan program. I was able to borrow P30,000 and whenever I paid it off, CARD SME Bank allowed me to borrow larger amounts. I was able to open a stall in Divisoria and in 2009, borrowed P200,000 to buy 10 high speed sewing machines. Instead of just supplying the embroider, I could make a finished barong. I found that there is greater demand in ready-to-wear clothes than the ones being sewn. From that observation, I turned my business around it and it succeeded.

Sharing the success

I recently bought a lot where I can build a small factory and a home. I now have 30 employees. It is one of my aspirations to give each one of them a better future, too. I am happy that I was able to provide employment to my fellowmen and I will continue to do so. As much as possible, I do not want to fire anyone. I treat them as my family so I also share my success with them.

I got this inspiration when I heard the speech from a CARD SME Bank executive saying that the thrift bank exists for us, their clients. As we are being assisted by them, we should also find a way to help other people through our success.

WE SET THEM UP TO SUCCEED

CARD SME Bank is not just about money or money lending facility. We are borne out of a clear objective to help SMEs grow and thrive. We have developed various products and services that can serve as instruments for their success. From savings accounts, time deposits, to various loan products that address specific business needs, CARD SME Bank will help you gain your financial freedom.

RECIPE FOR SUCCESS

Popoy and Joveline Rafanan
Pangil, Laguna

My husband, Popoy, and I were facing our golden years with uncertainty. Popoy was about to retire from the Armed Forces of the Philippines (AFP), but his small salary had only been enough to provide for our family's daily needs. With no savings, we knew that we had to start a business from his pension.

A neighbor told my husband about chicharon*-making, which required very little starting capital. I borrowed P2,500 from a friend to buy 50 kilograms

*Chicharon is a Filipino snack made from pork rinds, which is deep fried until it becomes crispy.
**Kropek is a popular snack in the Philippines. It is a deep fried prawn cracker that is made from starch and prawn.

of pork skin. We paid off the debt but were unable to borrow any more. The neighbor we hired to cook the chicharon was often unreliable too. Undeterred, we bought more ingredients from our earnings and learned how to make chicharon ourselves. With the help of our relatives, we cut the skins, dried them, deep-fried the rinds. By the end of 2006, we made an average of 200 kilograms of chicharon a week.

Finding capital and camaraderie

My daughter heard about CARD from her friend's mother. I found out that the institution did not just provide loans, but savings and insurance tools as well. Unfortunately, their nearest CARD center was at full capacity. I was encouraged to set up my own CARD center. I found other women who would be interested in the business seminars, which prepared members for loans.

I was able to get an initial loan of P2,500, a meager amount. It was the camaraderie and support that I got from my fellow CARD members that I valued most. It was encouraging to see my friends who are also striving to make their businesses flourish.

Strong foundations, not quick fixes

Our chicharon business slowly grew and I was able to borrow larger loans to fund wood burning stoves, a bigger cauldron, fuel, and of course, pork skins. During that time, we paid in cash because no one offers us to purchase in terms.

Bigger, richer competitors threatened to muscle us out by hiring several sales agents. My husband sold alone, and without a car, he would often walk to his customers. In the end, our hard work and steady business practices we learned from workshops won. Our competitor closed after two years because of mismanagement and his sales agent approached us for work. Suddenly, we had 30 people with established networks and an immense opportunity to expand.

MAKING CONNECTIONS, NOT JUST PROFITS

CARD's centers give small entrepreneurs a place to get solid business advice from experts, and find support and friendship from other members. For many, the weekly meetings are also a welcome respite from the stress of running a business, and a source of encouragement and inspiration.

The big break

Thanks to the credit history and solid business we had faithfully built over the years, I was able to get a CARD SME Bank loan. I bought a lot, built an environmentally-compliant chicharon factory, and a warehouse. All of the sales agent are still with us and we also have staff that helps produce six tons of chicharon a week. Ka Popoy's Chicharon is now distributed not just in Laguna, but also in Quezon, Cavite, Batangas, Rizal, and NCR. We have also begun to make and sell kropek**.

Success follows very simple principles: don't live or expand your business beyond your budget and always keep your word. Trust is worth its price in gold and a good name will open doors for you.

PRESIDENT'S REPORT

"Our advocacy has always been to eradicate poverty and we are doing that by empowering people. Our focus is on development, profit-taking takes a backseat. We know that if we are able to help the poor and give them the means and the help to develop as strong and successful businesspeople and entrepreneurs, then we have achieved our objective. This mindset is best reflected in our slogan "let's grow your business together."

There is heart in serving the people and this is what we are most proud of at CARD SME Bank."

Mary Jane A. Perreras
President and CEO
CARD SME Bank, Inc.

225,538 CLIENTS SERVED

216,389 CLIENTS INCLUDING SAVERS

141,664 ACTIVE CLIENTS WITH LOANS

PhP 1,358,231,502.70
AMOUNT OF LOANS OUTSTANDING

PhP 948,390,009.00
AMOUNT OF SAVINGS

99.26%
REPAYMENT RATE

122.36%
OSS*

119.92%
FSS**

729
Total number of staff

1 HEAD OFFICE
9 BRANCHES
117 MICRO BANKING OFFICES

*Operating Self Sufficiency/Revenue Cost Ratio
**Financial Self Sufficiency

Our operational status reflects how active our clients are and that we have their trust. With a repayment rate of 99.26%, we know that the trust we have given our clients is also well-placed. CARD SME Bank provides risk-based lending for its microfinance graduates (microfinance clients who are eligible to be categorized as SMEs) – we do not ask for collateral. That's the kind of trust that is the currency of our relationships with our clients.

Together with these institutions and organizations that share the same mission with us, we provide our clients with the best quality of service.

PARTNERSHIPS/COLLABORATION

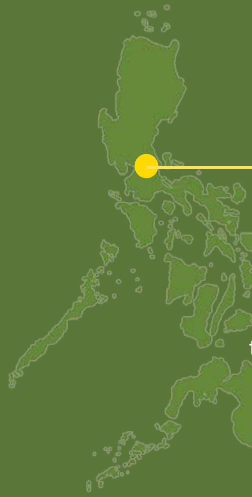
Allied Bank
Agricultural Guarantee Fund Pool
ANR Cooperative
Banco de Oro
Bank of the Philippine Islands (BPI)
Bellavita Land Corporation
BPI Globe Banko
ChinaBank Savings
Development Bank of the Philippines (DBP)
German Savings Bank Foundation, Germany
International Finance Corporation
Landbank of the 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 Talisay, Inc.
Savings Bank Foundation for International Cooperation (SBFIC), Germany
Bank of the Philippine Islands and Mitsui Sumitomo Insurance (BPI/MS)
Security Bank
SGV & Co.
Small Business Corporation
Social Security System
Sparkasse Essen, Germany
Sparkasse Rothenburg
Sparkassen International Development Trust
Triple A Security Agency Incorporation
Union Bank of the Philippines
United Coconut Planters Bank

REGULATORY BODIES

Bangko Sentral ng Pilipinas (BSP)
Philippine Deposit Insurance Corporation (PDIC)
Securities and Exchange Commision (SEC)

AFFILIATIONS

Bankers Institute of the Philippines, Inc. (BAIPHIL)
BancNet Inc.
BAP Credit Bureau
Chambers of Commerce, San Pablo Chapter
Chambers of Thrift Bank
Microfinance Data Sharing (MIDAS)
San Pablo Bankers' Association



Head Office
San Pablo City, Laguna

CARD SME Bank currently has 10 branches across the CALABARZON region, and we will be adding six more in Naga, Bulacan, Dagupan, Vigan, Bataan, and Subic to make our products and services accessible to SMEs in the northern part of Luzon. We will also consolidate our micro-banking offices – relocating them to commercial areas so that they can increase their reach and make our services more accessible to more people in these communities.

STO. TOMAS BRANCH
Sto. Tomas, Batangas
Tanauan City, Batangas
Malvar, Batangas
Talisay, Batangas
Laurel, Batangas

LIPA CITY BRANCH
Lipa City, Batangas
Mataas na kahoy, Batangas
Balete, Batangas
Ibaan, Batangas
Padre Garcia, Batangas
Rosario, Batangas
Cuenca, Batangas
San Jose, Batangas

BATANGAS CITY BRANCH
Batangas City
Lobo, Batangas
Bauan, Batangas
San Pascual, Batangas
Lemery, Batangas
Taal, Batangas
Sta. Teresita, Batangas

BALAYAN BRANCH
Balayan, Batangas
Agoncillo, Batangas
Calaca, Batangas
Calatagan, Batangas
San Luis, Batangas
Lian, Batangas
Nasugbu, Batangas
Tuy, Batangas

CAVITE CITY BRANCH
Cavite City
Noveleta, Cavite
Kawit, Cavite
Rosario, Cavite
Bacoor, Cavite

DASMARIÑAS CITY BRANCH
Dasmariñas City, Cavite
Imus, Cavite
Carmona, Cavite
General Trias, Cavite
Trece Martires, Cavite
GMA, Cavite

TAGAYTAY CITY BRANCH
Tagaytay City, Cavite
Silang, Cavite
Mendez, Cavite
Naic, Cavite
Indang, Cavite
Alfonso, Cavite
Tanza, Cavite
Maragondon, Cavite
Amadeo, Cavite

CALAMBA CITY BRANCH
Calamba City, Laguna

STA. ROSA CITY BRANCH
Sta. Rosa City, Laguna
Cabuyao, Laguna
Biñan, Laguna
San Pedro, Laguna

CARD has been known for providing microfinance for so many years but as it progresses and develops its microfinance clients into becoming SMEs, they needed an institution to take them to the next level. CARD SME Bank will take them there. We offer business or SME loans, apart from microfinance loans, to CARD's microfinance graduates to help them grow their business and enable them to compete in their respective industry.

As we migrate to a new and better Core Banking System, our products will likewise undergo major improvements that will provide more features that translate to enhanced benefits for our clients. This is our brand promise as reflected in our new and revitalized look.

MANAGEMENT COMMITTEE

Mary Jane A. Perreras
President and CEO

Cynthia B. Baldeo
Executive Vice President and COO

Anna Lorraine J. Maur
Assistant Vice President
Finance

Ronald A. Inciong
Assistant Vice President
Credit Risk

Cherry A. Boncajes
Assistant Vice President
Microfinance Operations

Manolo M. Martinez
Assistant Vice President
Marketing and Product Development

Dennis O. Dimaculangan
Assistant Vice President
Account Management Group

Jeffrey M. Rondina
Chief Compliance Officer

Allan D. Dimaano
Senior Program Manager

Noralyn D. Silvestre
Regional Director
Microfinance Operations

Anita F. Rapera
Regional Director
Microfinance Operations

Jerry V. Montejo
Regional Director
Account Management Group

Joy G. Palomique
Regional Director
Account Management Group

Mary Ann C. Resplandor
Assistant General Accounting Manager

Anna Therese A. de Leon
Internal Audit Manager

Angela A. Poonin
Senior Personnel Manager

Joven N. Robes
Pesonnel Manager

Peter C. Pasia
Legal Officer

Eduardo L. Dimaano Jr.
Information Security Officer

Ross Meinard C. Ramos
Sr. Information Technology Officer

BOARD OF DIRECTORS

Dr. Jaime Aristotle B. Alip
Chairperson

Ms. Flordeliza L. Sarmiento
Vice Chairperson

Milagros C. Rojas
Treasurer

Mary Jane A. Perreras
Member

Elma B. Valenzuela
Member

Ma. Elena M. Ruiz
Member

Felisa V. Lapitan
Independent Member

Dr. Gilbert M. Llanto
Independent Member

Atty. Wilfredo B. Domo-Ong
Independent Member

Edzel A. Ramos
Corporate Secretary

Atty. Edgardo R. Marilim
Legal Counsel

Benito R. Pagaspas
Consultant

FINANCIAL STATEMENTS

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

	December 31	
	2014	2013 (As restated - Note 2)
ASSETS		
Cash and Other Cash Items (Note 6)	**₱6,679,030**	₱4,610,455
Due from Bangko Sentral ng Pilipinas (Notes 6 and 13)	**81,135,679**	50,603,710
Due from Other Banks (Note 6)	**112,018,132**	83,462,403
Held-to-Maturity Investments (Note 7)	**11,077,148**	26,078,103
Loans and Receivables (Note 8)	**1,346,444,270**	910,974,414
Property and Equipment (Note 9)	**63,588,207**	37,667,311
Investment Properties (Note 10)	**16,602,232**	14,576,772
Intangible Assets (Note 11)	**4,772,600**	–
Retirement Asset (Note 18)	**33,636,973**	–
Deferred Tax Assets - net (Note 19)	**11,191,703**	25,418,282
Other Assets (Note 12)	**13,243,366**	10,581,226
TOTAL ASSETS	**₱1,700,389,340**	₱1,163,972,676
LIABILITIES AND EQUITY		
Liabilities		
Deposit Liabilities (Notes 13 and 20)		
Demand	**₱1,943,417**	₱441,307
Savings	**946,446,592**	828,013,759
	948,390,009	828,455,066
Bills Payable (Note 14)	**260,000,000**	–
Income Tax Payable (Note 19)	**18,526,629**	10,305,392
Retirement Liability (Note 18)	**–**	29,089,823
Other Liabilities (Note 15)	**41,255,248**	28,389,523
	1,268,171,886	896,239,804
Equity		
Common Stock (Note 17)	**296,943,600**	251,019,938
Surplus	**114,941,606**	41,823,625
Remeasurement Gains (Losses) on Retirement Plan	**20,332,248**	(25,110,691)
	432,217,454	267,732,872
TOTAL LIABILITIES AND EQUITY	**₱1,700,389,340**	₱1,163,972,676

See accompanying Notes to Financial Statements.

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

	Years Ended December 31	
	2014	2013
INTEREST INCOME ON		
Loans and receivables (Note 8)	**₱546,672,021**	₱346,292,876
Investments securities (Note 7)	**1,368,430**	1,688,598
Due from other banks (Note 6)	**1,289,378**	2,411,461
	549,329,829	350,392,935
INTEREST EXPENSE ON		
Deposit liabilities (Notes 13 and 20)	**21,451,361**	18,694,433
Bills payable (Note 14)	**1,247,715**	39,755
Others	**156,760**	58,880
	22,855,836	18,793,068
NET INTEREST INCOME	**526,473,993**	331,599,867
OTHER INCOME		
Gain (loss) on sale of assets - net (Notes 9 and 10)	**2,284,799**	(1,901,246)
Miscellaneous (Note 10)	**2,290,920**	3,231,215
TOTAL OPERATING INCOME	**531,049,712**	332,929,836
OPERATING EXPENSES		
Compensation and fringe benefits (Notes 18 and 20)	**174,402,398**	126,380,839
Taxes and licenses	**34,520,504**	20,100,917
Transportation and travel (Note 20)	**32,196,507**	20,865,086
Employee trainings (Note 20)	**20,197,087**	10,589,404
Occupancy (Notes 20 and 21)	**17,063,839**	12,843,986
Stationery and office supplies	**16,208,497**	13,051,048
Provision for credit and impairment losses (Notes 8 and 10)	**16,105,130**	11,882,068
Depreciation and amortization (Notes 9 and 10)	**10,727,405**	8,438,281
Security, messengerial and janitorial	**8,312,008**	5,432,429
Information technology (Note 20)	**7,121,032**	5,901,205
Meetings and seminars (Note 20)	**7,064,745**	11,408,788
Insurance	**6,309,991**	4,475,760
Representation and entertainment (Note 19)	**5,799,346**	2,940,466
Power, light and water	**4,103,508**	3,051,621
Repairs and maintenance	**3,560,496**	3,671,091
Postage, telephone and cable	**3,100,328**	2,040,029
Professional fees	**1,985,187**	1,673,142
Fines, penalties & other charges	**1,575,116**	1,502,438
Program monitoring	**1,098,556**	1,288,229
Miscellaneous (Note 10)	**13,161,969**	5,682,512
TOTAL OPERATING EXPENSES	**384,613,649**	273,219,339
INCOME BEFORE INCOME TAX	**146,436,063**	59,710,497
PROVISION FOR INCOME TAX (Note 19)	**44,284,204**	18,643,593
NET INCOME	**₱102,151,859**	₱41,066,904

See accompanying Notes to Financial Statements.

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

	Years Ended December 31	
	2014	2013
NET INCOME	**₱102,151,859**	₱41,066,904
OTHER COMPREHENSIVE INCOME		
Other comprehensive gain (loss) not recycled to profit or loss in subsequent periods:		
Gain on remeasurement of retirement plan (Note 18)	**64,918,484**	13,076,008
Income tax effect (Note 19)	**(19,475,545)**	(3,922,803)
OTHER COMPREHENSIVE INCOME, NET OF TAX	**45,442,939**	9,153,205
TOTAL COMPREHENSIVE INCOME	**₱147,594,798**	₱50,220,109

See accompanying Notes to Financial Statements.

CARD SME BANK, INC., A THRIFT BANK
STATEMENTS OF CHANGES IN EQUITY

	Common Stock (Note 17)	Surplus	Remeasurement Gain (Loss) on Retirement Plan (Note 18)	Total
Balance at January 1, 2014	**₱251,019,938**	**₱41,823,625**	**(₱25,110,691)**	**₱267,732,872**
Collection of subscriptions receivable	**45,923,662**	**–**	**–**	**45,923,662**
Total comprehensive income for the year	**–**	**102,151,859**	**45,442,939**	**147,594,798**
Cash dividends declared (Note 17)	**–**	**(29,033,878)**	**–**	**(29,033,878)**
Balance at December 31, 2014	**₱296,943,600**	**₱114,941,606**	**₱20,332,248**	**₱432,217,454**
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 (Note 17)	–	(6,055,189)	–	(6,055,189)
Balance at December 31, 2013	₱251,019,938	₱41,823,625	(₱25,110,691)	₱267,732,872

See accompanying Notes to Financial Statements.

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

	Years Ended December 31	
	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Income before income tax	**₱146,436,063**	₱59,710,497
Adjustments for:		
Retirement expense (Note 18)	**19,004,870**	17,867,608
Provision for credit and impairment losses (Notes 8 and 10)	**16,105,130**	11,882,068
Depreciation and amortization (Notes 9 and 10)	**10,727,405**	8,438,281
Loss (gain) on disposal of assets	**(2,059,238)**	1,901,246
Amortization of debt securities carried at amortized cost	**238,800**	158,130
Fair value gain on foreclosure of investment properties (Note 10)	**–**	(1,142,321)
Changes in operating assets and liabilities:		
Increase in the amounts of:		
Loans and receivables	**(456,977,954)**	(344,132,661)
Deposit liabilities	**119,934,943**	326,025,774
Other assets	**(2,662,140)**	(3,571,492)
Other liabilities	**12,615,537**	11,454,605
Net cash generated from (used in) operations	**(136,636,584)**	88,591,735
Income taxes paid	**(41,311,933)**	(17,846,424)
Contributions to the retirement fund (Note 18)	**(16,813,182)**	(21,692,780)
Net cash provided by (used in) operating activities	**(194,761,699)**	49,052,531
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisitions of:		
Property and equipment (Note 9)	**(36,749,553)**	(14,315,760)
Intangible assets (Note 11)	**(4,772,600)**	–
Unquoted debt securities (Note 8)	**(3,014,795)**	(20,000,000)
Proceeds from sale or maturities of:		
Held-to-maturity investments	**14,820,155**	–
Investment properties (Note 10)	**5,222,947**	4,202,451
Unquoted debt securities (Note 8)	**3,271,846**	–
Available-for-sale investments	**–**	8,000,000
Net cash used in investing activities	**(21,222,000)**	(22,113,309)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash dividends paid	**(28,783,690)**	(6,055,189)
Availments of bills payable	**285,000,000**	–
Settlement of bills payable	**(25,000,000)**	(26,476,877)
Collections of subscriptions receivable (Note 17)	**45,923,662**	35,506,113
Net cash provided by financing activities	**277,139,972**	2,974,047

(Forward)

	Years Ended December 31	
	2014	2013
NET INCREASE IN CASH AND CASH EQUIVALENTS	**₱61,156,273**	₱29,913,269
CASH AND CASH EQUIVALENTS AT BEGINNING 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
CASH AND CASH EQUIVALENTS AT END OF YEAR		
Cash and other cash items	**6,679,030**	4,610,455
Due from Bangko Sentral ng Pilipinas	**81,135,679**	50,603,710
Due from other banks	**112,018,132**	83,462,403
	₱199,832,841	₱138,676,568

OPERATIONAL CASH FLOWS FROM INTEREST		
Interest received	**₱555,943,376**	₱347,558,820
Interest paid	**23,050,898**	18,898,519

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 Multi-purpose Cooperative, Inc. acquired the majority of its voting stock. The rehabilitation court and the Bangko Sentral ng Pilipinas 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 formally started its operations as a thrift bank.

As a thrift bank, the Bank can (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'*.

Borrowers with good credit standing with the Bank can avail the CARD Scholarship Program of the CARD MRI and can be prioritized during hiring of personnel.

2. **Significant Accounting Policies**

Basis of Preparation
The accompanying financial statements have been prepared on a historical cost basis. The financial statements are presented in Philippine peso, the Bank's functional currency. All values are rounded to the nearest peso unless otherwise indicated.

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 16.

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.

Changes in Accounting Policies and Disclosures
Except for these new and amended standards and interpretations which were adopted as at January 1, 2014, the accounting policies adopted are consistent with those of the previous financial year. Unless otherwise indicated, these new and amended standards and interpretations have no impact to the Bank.

New and amended standards and interpretations

- Investment Entities (Amendments to PFRS 10, *Consolidated Financial Statements*, PFRS 12, *Disclosure of Interests in Other Entities*, and Philippine Accounting Standards (PAS) 27, *Separate Financial Statements*)
- PAS 32, *Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities* (Amendments)
- PAS 36, *Impairment of Assets* - *Recoverable Amount Disclosures for Non-Financial Assets* (Amendments)
- PAS 39, *Financial Instruments: Recognition and Measurement - Novation of Derivatives and Continuation of Hedge Accounting* (Amendments)
- Philippine Interpretation IFRIC 21, *Levies* (IFRIC 21)

Annual Improvements to PFRSs (2011 - 2012 cycle)
- PFRS 13, *Fair Value Measurement*

Annual Improvements to PFRSs (2011 - 2013 cycle)
- PFRS 1, *First-time Adoption of PFRS*

Change of Presentation

The Company reclassified certain accounts in the 2013 financial statements to conform to the 2014 presentation, which takes into account the fundamental nature and significance of the transactions as well as the general financial statement presentation.

Assets previously presented in the 2013 financial statement as 'Assets held by Special Purpose Vehicle' were reclassified as 'Investment properties' to conform with the 2014 financial statements, as shown below:

	December 31, 2013		
	As previously reported	Prior-period adjustments	As restated
Assets Held by Special Purpose Vehicle	₱4,371,336	(₱4,371,336)	₱–
Investment Properties	10,205,436	4,371,336	14,576,772

Summary of Significant Accounting Policies

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, 2014 and 2013, the Bank has no AFS investments and financial assets and financial liabilities at FVPL.

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 Effective Interest Rate (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 '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.

This accounting policy applies to 'Due from BSP', 'Due from other banks', 'Loans and receivables' and refundable deposits under 'Other assets'

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', 'Accounts payable' and 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.

Derecognition of Financial Assets and Liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a Bank 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 ate whether there is objective evidence that a financial asset or Bank of financial assets is impaired. A financial asset or a Bank 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 Bank of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a Bank 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 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 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 Bank of financial assets is impaired.

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 nonrefundable 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.

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

Furniture, fixtures and equipment	1-3 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 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 'Miscellaneous income' 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.

Intangible Assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses. Internally generated intangibles, excluding capitalized development costs, are not capitalized and the related expenditure is reflected in profit or loss in the period in which the expenditure is incurred. The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired.
The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the statement of profit or loss in the expense category that is consistent with the function of the intangible assets.

Intangible assets consist of software costs which are amortized on a straight-line basis over three years.

Impairment of Property and Equipment, Investment Properties and Software Costs

At each reporting date, the Bank assesses whether there is any indication that its nonfinancial assets 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 group 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 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 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. This is recognized under ‘Miscellaneous income in the statement of income.

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 on remeasurement of retirement plan' 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. 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, carry forward 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 carry forward 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.

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.

PFRS 9, *Financial Instruments* – Classification and Measurement (2010 version)
PFRS 9 (2010 version) reflects the first phase on the replacement of PAS 39 and applies to the classification and measurement of financial assets and liabilities as defined in PAS 39, *Financial Instruments: Recognition and Measurement*. 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 FVO liabilities, 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 profit or loss, unless presentation of the fair value change in respect of the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. All other PAS 39 classification and measurement requirements for financial liabilities have been carried forward into PFRS 9, including the embedded derivative separation 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.

PFRS 9 (2010 version) is effective for annual periods beginning on or after January 1, 2015. This mandatory adoption date was moved to January 1, 2018 when the final version of PFRS 9 was adopted by the Philippine Financial Reporting Standards Council (FRSC). Such adoption, however, is still for approval by the Board of Accountancy (BOA).

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 interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as construction contract to be accounted for under PAS 11 or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and reward of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion. The SEC and the 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.

Effective January 1, 2015
PAS 19, *Employee Benefits – Defined Benefit Plans: Employee Contributions* (Amendments)
PAS 19 requires an entity to consider contributions from employees or third parties when accounting for defined benefit plans. Where the contributions are linked to service, they should be attributed to periods of service as a negative benefit. These amendments clarify that, if the amount of the contributions is independent of the number of years of service, an entity is permitted to recognize such contributions as a reduction in the service cost in the period in which the service is rendered, instead of allocating the contributions to the periods of service. It is not expected that this amendment would be relevant to the Bank, the Bank has defined benefit plans with contributions from employees or third parties.

Annual Improvements to PFRSs (2010-2012 cycle)
The Annual Improvements to PFRSs (2010-2012 cycle are not expected to have a material impact on the Bank. They include:

PFRS 2, *Share-based Payment – Definition of Vesting Condition*
This improvement is applied prospectively and clarifies various issues relating to the definitions of performance and service conditions which are vesting conditions, including:

- A performance condition must contain a service condition
- A performance target must be met while the counterparty is rendering service
- A performance target may relate to the operations or activities of an entity, or to those of another entity in the same Group
- A performance condition may be a market or non-market condition
- If the counterparty, regardless of the reason, ceases to provide service during the vesting period, the service condition is not satisfied.

PFRS 3, *Business Combinations – Accounting for Contingent Consideration in a Business Combination*
The amendment which is applied prospectively, clarifies that a 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 PAS 39, *Financial Instruments: Recognition and Measurement*. 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 are applied retrospectively and clarify that:

- An entity must disclose the judgments made by management in applying the aggregation criteria in the standard, including a brief description of operating segments that have been aggregated and the economic characteristics (e.g., sales and gross margins) used to assess whether the segments are 'similar'.
- The reconciliation of segment assets to total assets is only required to be disclosed if the reconciliation is reported to the chief operating decision maker, similar to the required disclosure for segment liabilities.

PAS 16, *Property, Plant and Equipment*, and PAS 38, *Intangible Assets – Revaluation Method – Proportionate Restatement of Accumulated Depreciation and Amortization*
The amendment is applied retrospectively and clarifies in PAS 16 and PAS 38 that the asset may be revalued by reference to the observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortization is the difference between the gross and carrying amounts of the asset.

PAS 24, *Related Party Disclosures – Key Management Personnel*
The amendment is applied retrospectively and clarifies that a management entity, which is an entity that provides key management personnel services, is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services.

Annual Improvements to PFRSs (2011-2013 cycle)
The Annual Improvements to PFRSs (2011-2013 cycle) and are not expected to have a material impact on the Bank. They include:

PFRS 3, *Business Combinations – Scope Exceptions for Joint Arrangements*
The amendment is applied prospectively and clarifies the following regarding the scope exceptions within PFRS 3:

- Joint arrangements, not just joint ventures, are outside the scope of PFRS 3.
- This scope exception applies only to the accounting in the financial statements of the joint arrangement itself.

PFRS 13, *Fair Value Measurement – Portfolio Exception*
The amendment is applied prospectively and clarifies that the portfolio exception in PFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of PAS 39.

PAS 40, *Investment Property*
The amendment is applied prospectively and clarifies that PFRS 3, and not the description of ancillary services in PAS 40, is used to determine if the transaction is a purchase of an asset or a business combination. The description of ancillary services in PAS 40 only differentiates between investment property and owner-occupied property (i.e., property, plant and equipment).

Effective January 1, 2016
PAS 16, *Property, Plant and Equipment*, and PAS 38, *Intangible Assets – Clarification of Acceptable Methods of Depreciation and Amortization* (Amendments)
The amendments clarify the principle in PAS 16 and PAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortize intangible assets. The amendments are effective prospectively, with early adoption permitted. These amendments are not expected to have any impact to the Bank given that the Bank has not used a revenue-based method to depreciate its non-current assets.

PAS 16, *Property, Plant and Equipment*, and PAS 41, *Agriculture – Bearer Plants* (Amendments)
The amendments change the accounting requirements for biological assets that meet the definition of bearer plants. Under the amendments, biological assets that meet the definition of bearer plants will no longer be within the scope of PAS 41, PAS 16 will apply. After initial recognition, bearer plants will be measured under PAS 16 at accumulated cost (before maturity) and using either the cost model or revaluation model (after maturity). The amendments also require that produce that grows on bearer plants will remain in the scope of PAS 41 measured at fair value less costs to sell. For government grants related to bearer plants, PAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*, will apply. The amendments are retrospectively effective for annual periods beginning on or after January 1, 2016, with early adoption permitted. These amendments are not expected to have any impact to the Bank as the Bank does not have any bearer plants.

PAS 27, *Separate Financial Statements – Equity Method in Separate Financial Statements* (Amendments)
The amendments will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. Entities already applying PFRS and electing to change to the equity method in its separate financial statements will have to apply that change retrospectively. For first-time adopters of PFRS electing to use the equity method in its separate financial statements, they will be required to apply this method from the date of transition to PFRS. Early adoption of the amendments is permitted. These amendments will not have any impact on the Bank's financial statements.

PFRS 10, *Consolidated Financial Statements* and PAS 28, *Investments in Associates and Joint Ventures – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*
These amendments address an acknowledged inconsistency between the requirements in PFRS 10 and those in PAS 28 (2011) in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The amendments require that a full gain or loss is recognized when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary.

PFRS 11, *Joint Arrangements – Accounting for Acquisitions of Interests in Joint Operations* (Amendments)
The amendments to PFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business must apply the relevant PFRS 3 principles for business combinations accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation while joint control is retained. In addition, a scope exclusion has been added to PFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party.

The amendments apply to both the acquisition of the initial interest in a joint operation and the acquisition of any additional interests in the same joint operation and are prospectively effective with early adoption permitted. These amendments are not expected to have any impact to the Bank.

PFRS 14, *Regulatory Deferral Accounts*
PFRS 14 is an optional standard that allows an entity, whose activities are subject to rate-regulation, to continue applying most of its existing accounting policies for regulatory deferral account balances upon its first-time adoption of PFRS. Entities that adopt PFRS 14 must present the regulatory deferral accounts as separate line items on the statement of financial position and present movements in these account balances as separate line items in the statement of profit or loss and other comprehensive income. The standard requires disclosures on the nature of, and risks associated with, the entity's rate-regulation and the effects of that rate-regulation on its financial statements. Since the Bank is an existing PFRS preparer, this standard would not apply.

Annual Improvements to PFRSs (2012-2014 cycle)
The Annual Improvements to PFRSs (2012-2014 cycle) are not expected to have a material impact on the Bank. They include:

PFRS 5, *Non-current Assets Held for Sale and Discontinued Operations – Changes in Methods of Disposal*
The amendment is applied prospectively and clarifies that changing from a disposal through sale to a disposal through distribution to owners and vice-versa should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in PFRS 5. The amendment also clarifies that changing the disposal method does not change the date of classification.

PFRS 7, *Financial Instruments: Disclosures – Servicing Contracts*
PFRS 7 requires an entity to provide disclosures for any continuing involvement in a transferred asset that is derecognized in its entirety. The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and arrangement against the guidance in PFRS 7 in order to assess whether the

disclosures are required. The amendment is to be applied such that the assessment of which servicing contracts constitute continuing involvement will need to be done retrospectively. However, comparative disclosures are not required to be provided for any period beginning before the annual period in which the entity first applies the amendments.

PFRS 7 - *Applicability of the Amendments to PFRS 7 to Condensed Interim Financial Statements*
This amendment is applied retrospectively and clarifies that the disclosures on offsetting of financial assets and financial liabilities are not required in the condensed interim financial report unless they provide a significant update to the information reported in the most recent annual report.

PAS 19, *Employee Benefits – regional market issue regarding discount rate*
This amendment is applied prospectively and clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used.

PAS 34, *Interim Financial Reporting – disclosure of information 'elsewhere in the interim financial report'*
The amendment is applied retrospectively and clarifies that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the greater interim financial report (e.g., in the management commentary or risk report).

Effective January 1, 2018
PFRS 9, *Financial Instruments* – Hedge Accounting and amendments to PFRS 9, PFRS 7 and PAS 39 (2013 version)
PFRS 9 (2013 version) already includes the third phase of the project to replace PAS 39 which pertains to hedge accounting. This version of 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 derivative instrument as the hedging instrument and accounted for as costs of hedging. PFRS 9 also requires more extensive disclosures for hedge accounting.

PFRS 9 (2013 version) has no mandatory effective date. The mandatory effective date of January 1, 2018 was eventually set when the final version of PFRS 9 was adopted by the FRSC. The adoption of the final version of PFRS 9, however, is still for approval by BOA.

The adoption of PFRS 9 will have an effect on the classification and measurement of the Bank's financial assets but will have no impact on the classification and measurement of the Bank's financial liabilities. The Bank is currently assessing the impact of adopting this standard.

PFRS 9, *Financial Instruments* (2014 or final version)
In July 2014, the final version of PFRS 9, *Financial Instruments*, was issued. PFRS 9 reflects all phases of the financial instruments project and replaces PAS 39, *Financial Instruments: Recognition and Measurement*, and all previous versions of PFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. PFRS 9 is

effective for annual periods beginning on or after January 1, 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of PFRS 9 is permitted if the date of initial application is before January 1, 2015.

The adoption of PFRS 9 will have an effect on the classification and measurement of the Bank's financial assets and impairment methodology for financial assets, but will have no impact on the classification and measurement of the Bank's financial liabilities. The Bank is currently assessing the impact of adopting this standard.

The following new standard issued by the IASB has not yet been adopted by the FRSC

IFRS 15 Revenue from Contracts with Customers
IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach to measuring and recognizing revenue. The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after January 1, 2017 with early adoption permitted. The Bank is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date once adopted locally.

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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.

<u>Judgments</u>

(a) *Operating leases - Bank as lessee*
The Bank has entered into commercial property and equipment leases with various entities. The Bank has determined, based on the evaluation of the terms and conditions of the lease agreement (i.e., the lease does not transfer ownership of the asset to the lessee by the end of the lease term and lease term is not for the major part of the asset's economic life), that the lessor retains all the significant risks and rewards of ownership of these properties 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.

(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) *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.

(f) *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, 2014 and 2013, the carrying values of loans and receivables and related allowance for credit losses are disclosed in Note 8.

(b) *Estimated useful lives of property and equipment, investment properties and software costs*
The Bank estimates the useful lives of its property and equipment, investment properties and software costs 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, investment properties and software costs are disclosed in Note 2.

(c) *Impairment of nonfinancial assets*
The Bank assesses impairment on property and equipment, investment properties and intangible assets whenever events or changes in circumstances indicate that their carrying amount 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 amounts exceed their recoverable amounts. The carrying values of property and equipment, investment properties and intangible assets and the related allowance for impairment are disclosed in Notes 9, 10 and 11.

(d) *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 18.

(e) *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, 2014 and 2013, the carrying values of deferred tax assets are disclosed in Note 19.

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, 2014 and 2013, the Bank has no financial instruments carried at fair value.

The following table summarizes the carrying amounts and the fair values by level of the fair value hierarchy of the Bank's assets and liabilities as at December 31, 2014 and 2013 for which fair values are required to be disclosed. Financial instruments which fair values are required to be disclosed, but the carrying values equal their fair values are not shown:

			2014		
	Carrying Value	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Assets for which fair values are disclosed:					
Financial assets					
HTM investments	**₱11,077,148**	**₱–**	**₱11,503,138**	**₱–**	**₱11,503,138**
Loans and receivables					
SME loans	**139,468,642**	**–**	**–**	**135,565,698**	**135,565,698**
Unquoted debt securities	**20,797,337**	**–**	**–**	**20,734,104**	**20,734,104**
Non-financial asset					
Investment properties	**16,602,232**	**–**	**–**	**44,192,550**	**44,192,550**

			2013		
	Carrying Value	Level 1	Level 2	Level 3	Total Fair Value
Assets for which fair values are disclosed:					
Financial assets					
Held-to-Maturity investments	₱26,078,103	₱–	₱27,499,089	₱–	₱27,499,089
Loans and receivables					
SME loans	86,794,808	–	–	110,157,371	110,157,371
Unquoted debt securities	21,112,388	–	–	21,050,960	21,050,960
Non-financial asset					
Investment properties	14,576,772	–	–	50,477,170	50,477,170

There were no transfers between Level 1 and Level 2 fair value measurements and no transfers into and out of Level 3 fair value measurements in 2014 and 2013.

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, unquoted debt securities 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.

Fair value of the investment properties has been determined based on valuations made by external appraiser on the basis of recent sales transactions of similar properties in the same areas as the properties and taking into account the economic conditions prevailing at the time the valuations were made. Market data approach is used. It involves correlation and analysis of comparable lots, either recently sold or offered for sale in the market, upon which the market value of subject property is estimated. The inputs considered by the appraisers in the valuation include price per square meter, size and shape of property, location and time element of the appraisal.
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 Data 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	A process of comparing the subject property being appraised to similar comparable properties recently sold or being offered for sale.
Modified Quantity Survey Approach	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.

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 Credit Risk Management Committee (CRMC) 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. <u>Credit risk</u>
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 is 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, 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 Internal Auditors.

All past due or impaired accounts are reported on a daily, weekly and monthly bases. Consistent monitoring for this Bank 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.

	2014			
	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	**₱1,196,073,423**	**₱182,784,552**	**₱182,784,552**	**₱1,013,288,871**
SME loans	**114,775,066**	**66,461,859**	**34,247,614**	**80,527,452**
REM loans	**–**	**–**	**–**	**–**

	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	₱786,146,076	₱121,454,937	₱121,454,937	₱664,691,139
SME loans	91,636,495	36,636,715	21,261,194	70,375,301
REM loans	102,960	331,872	101,785	1,175

Credit enhancement for microfinance loans pertains to deposit hold-out from center fund savings equivalent to 15.0% of the loaned amount of the member as at December 31, 2014 and 2013. Credit enhancement for Real Estate Mortgage (REM) and Small and Medium-sized Enterprises (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, 2014 and 2013. 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, 2014 and 2013:

	2014				
	Loans and Receivables	**Due from BSP and Other Banks**	**Held-to-Maturity Investments**	**Refundable Deposits**	**Total**
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods	**₱803,285,492**	**₱–**	**₱–**	**₱–**	**₱803,285,492**
Others	**190,530,600**	–	–	**372,396**	**190,902,996**
Agriculture, hunting and forestry	**184,406,914**	–	–	–	**184,406,914**
Other community, social and personal service activities	**145,272,252**	–	–	–	**145,272,252**
Financial intermediaries	**748,252**	**112,018,132**	–	–	**112,766,384**
Government	**20,049,085**	**81,135,679**	**11,077,148**	–	**112,261,912**
Manufacturing	**49,810,169**	–	–	–	**49,810,169**
	1,394,102,764	**193,153,811**	**11,077,148**	**372,396**	**1,598,706,119**
Allowance for credit losses	**(46,739,126)**	–	–	–	**(46,739,126)**
Unearned interest and discount	**(919,368)**	–	–	–	**(919,368)**
Total	**₱1,346,444,270**	**₱193,153,811**	**₱11,077,148**	**₱372,396**	**₱1,551,047,625**

	2013				
	Loans and Receivables	Due from BSP and Other Banks	Held-to-Maturity Investments	Refundable Deposits	Total
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods	₱343,247,369	₱–	₱–	₱–	₱343,247,369
Others	184,289,636	–	–	312,000	184,601,636
Agriculture, hunting and forestry	157,476,129	–	–	–	157,476,129
Manufacturing	137,445,837	–	–	–	137,445,837
Other community, social and personal service activities	98,423,965	–	–	–	98,423,965
Government	20,092,290	50,603,710	26,078,103	–	96,774,103
Financial intermediaries	1,020,098	83,462,403	–	–	84,482,501
	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

Credit quality

Loans and receivables 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, 2014 and 2013:

	2014				
	Neither Past Due Nor Impaired				
	High Grade	Standard Grade	Past Due but not Impaired	Individually Impaired	Total
Due from BSP	**₱81,135,679**	**₱–**	**₱–**	**₱–**	**₱81,135,679**
Due from other banks	**112,018,132**	–	–	–	**₱112,018,132**
HTM investments	**11,077,148**	–	–	–	**₱11,077,148**
Loans and receivables:	–	–	–	–	–
Loans and discounts:					
Microfinance	–	**1,206,335,159**	**2,372,894**	**9,855,628**	**1,218,563,681**
SME	**48,239,487**	**70,196,165**	**11,265,275**	**9,767,715**	**139,468,642**
REM	–	–	–	**199,179**	**199,179**
Unquoted debt securities	**20,797,337**	–	–	–	**20,797,337**
Other receivables:					
Accrued interest receivable	**788,462**	**12,975,619**	–	–	**13,764,081**
Accounts receivable	–	–	–	**642,651**	**642,651**
Sales contract receivable	–	**481,000**	–	**186,193**	**667,193**
Other assets - refundable deposits	–	**372,396**	–	–	**372,396**
	₱274,056,245	**₱1,290,360,339**	**₱13,638,169**	**₱20,651,366**	**₱1,598,706,119**

	2013				
	Neither Past Due Nor Impaired				
	High Grade	Standard Grade	Past Due but not Impaired	Individually Impaired	Total
Due from BSP	₱50,603,710	₱–	₱–	₱–	₱50,603,710
Due from other banks	83,462,403	–	–	–	83,462,403
HTM investments	26,078,103	–	–	–	26,078,103
Loans and receivables:	–	–	–	–	–
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	594,976	7,122,918	–	–	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
	₱210,416,876	₱866,753,849	₱3,369,603	₱21,911,212	₱1,102,451,540

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, 2014 and 2013.

	2014			
	Less than 30 Days	**31 to 60 Days**	**61 to 90 Days**	**Total**
Microfinance	**₱791,911**	**₱783,503**	**₱797,480**	**₱2,372,894**
SME	**2,443,571**	**2,897,223**	**5,924,481**	**11,265,275**
	₱3,235,482	**₱3,680,726**	**₱6,721,961**	**₱13,638,169**

	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

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 Held-to-maturity investments'.

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 in December 31 2014 and 2013. 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 voluntary savings that earns 1.5% to 5.0% and 1.5% to 2.0% per annum for the years ended December 31, 2014 and 2013, respectively. Special savings deposits earn 1.8% to 4.5% and 2.3% to 7.0% per annum for the years December 31, 2014 and 2013, respectively. The bulk of Special savings deposit accounts are concentrated on 30 days to one year maturity with interest rate of less than 1.5%.

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, 2014 and 2013:

	2014				
	On demand	**1 to 6 months**	**6 to 12 months**	**Beyond 1 year**	**Total**
Financial Assets					
Due from BSP	**₱81,135,679**	**₱–**	**₱–**	**₱–**	**₱81,135,679**
Due from other banks	**112,018,132**	**–**	**–**	**–**	**112,018,132**
HTM investments	**–**	**441,294**	**431,774**	**10,204,080**	**11,077,148**
Loans and receivables*:					
Loans and discounts	**–**	**1,425,058,673**	**113,894,354**	**42,929,934**	**1,581,882,961**
Unquoted debt securities	**–**	**5,630**	**17,460,018**	**3,407,009**	**20,872,657**
Other receivables:					
Accrued interest receivable	**–**	**13,764,081**	**–**	**–**	**13,764,081**
Accounts receivable	**–**	**642,651**	**–**	**–**	**642,651**
Sales contract receivable	**–**	**374,194**	**187,999**	**105,000**	**667,193**
Refundable deposit	**–**	**–**	**–**	**372,396**	**372,396**
	193,153,811	**1,440,286,523**	**131,974,145**	**57,018,419**	**1,822,432,898**
Financial Liabilities					
Deposit liabilities:					
Demand	**1,943,417**	**–**	**–**	**–**	**1,943,417**
Savings	**678,020,045**	**209,067,560**	**61,482,539**	**–**	**948,570,144**
Bills Payable	**–**	**33,962,500**	**238,301,250**	**–**	**272,263,750**
Other liabilities					
Accrued expenses	**–**	**22,624,427**	**–**	**–**	**22,624,427**
Accounts payable	**–**	**9,043,889**	**–**	**–**	**9,043,889**
Accrued interest payable	**–**	**2,215,755**	**–**	**–**	**2,215,755**
Dividends payable	**–**	**290,336**	**–**	**–**	**290,336**
	679,963,462	**277,204,467**	**299,783,789**	**–**	**1,256,951,718**
Net undiscounted financial assets (liabilities)	**(₱486,809,651)**	**₱1,163,082,056**	**(₱167,809,644)**	**₱57,018,419**	**565,481,180**

* Includes nonperforming loans and receivables.

	2013				
	On demand	1 to 6 months	6 to 12 months	Beyond 1 year	Total
Financial Assets					
Due from BSP	₱50,603,710	₱–	₱–	₱–	₱50,603,710
Due from other banks	49,064,893	34,397,510	–	–	83,462,403
HTM investments	–	15,602,051	527,359	11,816,294	27,945,704
Loans and receivables*:					
Loans and discounts	–	1,070,350,198	79,081,203	845,336	1,150,276,737
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
Refundable deposits	–	–	–	312,000	312,000
	111,069,891	1,135,255,208	82,720,872	31,065,760	1,360,111,731
Financial Liabilities					
Deposit liabilities:					
Demand	441,307	–	–	–	441,307
Savings	504,031,133	257,755,504	69,037,157	–	830,823,794
Other liabilities					
Accrued expenses	–	16,174,497	–	–	16,174,497
Accrued interest payable	–	2,020,693	–	–	2,020,693
Accounts payable	–	3,586,196	–	–	3,586,196
Dividends payable	–	40,148	–	–	40,148
	504,472,440	279,577,038	69,037,157	–	853,086,635
Net undiscounted financial assets (liabilities)	(₱393,402,549)	₱855,678,170	₱13,683,715	₱31,065,760	₱507,025,096

* Includes nonperforming loans and receivables.

As of December 31, 2014, the Bank had a total of ₱430.0 million credit lines with local banks. Out of which, ₱260.0 million had been drawn as of yearend.

6. **Cash and Cash Equivalents**

The composition of this account follows:

	2014	2013
Cash and other cash items	**₱6,679,030**	₱4,610,455
Due from BSP	**81,135,679**	50,603,710
Due from other banks	**112,018,132**	83,462,403
	₱199,832,841	₱138,676,568

Due from BSP comprises demand deposit with BSP. The account is maintained in compliance with the BSP requirements to maintain regular and liquidity reserves on deposits. As at December 31, 2014 and 2013, the Bank is compliant with the applicable reserve requirements.

Due from other banks consists of:

	2014	2013
Demand deposit	**₱105,121,631**	₱42,106,728
Savings deposit	**6,896,501**	6,958,165
Time certificate of deposit	**–**	34,397,510
	₱112,018,132	₱83,462,403

Due from other banks consist of funds deposited in domestic banks which are used as part of the Bank's working capital. These deposits bear annual interest rates ranging from 0.1% to 0.8% and from 0.8% to 1.8% for the years ended December 31, 2014 and 2013, respectively. In 2014 and 2013, interest income on due from other banks amounted to ₱1.3 million and ₱2.4 million, respectively.

7. **Held-to-Maturity Investments**

As at December 31, 2014 and 2013, HTM investments amounted to ₱11.1 million and ₱26.1 million. This account represents investment in government securities bearing annual interest rates of 7.0% and 6.3% to 7.0% in 2014 and 2013, respectively.

Interest income earned on HTM investments amounted to ₱1.4 million and ₱1.7 million in 2014 and 2013, respectively.

8. **Loans and Receivables**

This account consists of:

	2014	2013
Loans and discounts:		
Microfinance (Note 14)	**₱1,218,563,681**	₱809,699,581
SME	**139,468,642**	97,994,442
REM	**199,179**	721,965
	1,358,231,502	908,415,988
Unearned interest income	**(919,368)**	(1,175)
	1,357,312,134	908,414,813
Unquoted debt securities	**20,797,337**	21,112,388
Other receivables:		
Accrued interest receivable	**13,764,081**	7,717,894
Sales contracts receivable	**667,193**	738,689
Accounts receivable (Note 20)	**642,651**	4,010,365
	1,393,183,396	941,994,149
Less allowance for credit losses	**(46,739,126)**	(31,019,735)
	₱1,346,444,270	₱910,974,414

Loans and discounts earn interest at rates ranging from 32.8% to 58.8% in 2014 and 2013.

Unquoted debt securities includes Micro, Small and Medium Enterprise Notes and Agrarian Reform Bonds of which interest rates range from 0.9% to 1.3% and with maturity ranging from 360 to 1,094 days in 2014 and 2013, respectively.

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

	2014	2013
Loans and discounts:		
Microfinance	**₱519,834,268**	₱324,319,196
SME	**26,774,471**	21,759,817
REM	**59,800**	175,638
Unquoted debt securities	**3,482**	38,225
	₱546,672,021	₱346,292,876

No interest income is accreted on individually impaired loans in 2014 and 2013.

The movements in allowance for credit losses follow:

	2014			
	Loans and discounts	**Accounts receivable**	**Sales contract receivables**	**Total**
Balance at beginning of year	**₱30,530,457**	**₱489,278**	**₱–**	**₱31,019,735**
Provisions	**21,193,047**	**–**	**–**	**21,193,047**
Write-offs	**(5,073,666)**	**(399,990)**	**–**	**(5,473,656))**
Transfers	**(186,193)**		**186,193**	**–**
Balance at end of year	**₱46,463,645**	**₱89,288**	**₱186,193**	**₱46,739,126**
Individually impaired	**₱13,342,561**	**₱89,288**	**₱186,193**	**₱13,618,042**
Collectively impaired	**33,121,084**	**–**	**–**	**33,121,084**
	₱46,463,645	**₱89,288**	**₱186,193**	**₱46,739,126**
Gross amounts of loans individually determined to be impaired, before deducting any individually assessed impairment losses	**₱19,822,521**	**₱642,651**	**₱186,193**	**₱20,651,365**

	2013			
	Loans and discounts	Accounts receivable	Sales contract receivables	Total
Balance at beginning of year	₱21,533,222	₱910,148	₱–	₱22,443,370
Provisions	10,010,896	7,210	–	10,018,106
Write-offs	(1,013,661)	(428,080)	–	(1,441,741)
Balance at end of year	₱30,530,457	₱489,278	₱–	₱31,019,735
Individually impaired	₱12,049,124	₱489,278	₱–	₱12,538,402
Collectively impaired	18,481,333	–	–	18,481,333
	₱30,530,457	₱489,278	₱–	₱31,019,735
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

Regulatory Reporting

In accordance with BSP regulations, the Bank considers as part of its portfolio-at-risk (PAR) loans with one day past due. As at December 31, 2014 and 2013, the Bank's PAR amounted to ₱33.5 million and ₱21.3 million, respectively. The allowance for credit losses recognized for past due loans amounted to ₱23.9 million and ₱18.3 million as at December 31, 2014 and 2013, respectively.

As at December 31, 2014 and 2013, nonperforming loans (NPLs) reported to the BSP amounted to ₱28.1 million and ₱19.8 million, respectively.

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, 2014 and 2013:

	2014	2013
Secured portion		
Deposit hold-out	**₱182,784,552**	₱121,454,937
REM	**35,744,015**	14,793,372
Chattel mortgage	**12,694,651**	14,162,016
	231,223,218	150,410,325
Unsecured portion	**1,127,008,284**	758,005,663
	₱1,358,231,502	₱908,415,988

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

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:

	2014		2013	
	Amount	**%**	Amount	%
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods	**₱803,285,492**	**57.658.5**	₱343,247,369	36.5
Agriculture, hunting and forestry	**184,406,914**	**13.213.4**	157,476,129	16.7
Other community, social and personal service activities	**145,272,252**	**10.46**	98,423,965	10.4
Manufacturing	**49,810,169**	**3.6**	137,445,837	14.6
Government	**20,049,085**	**1.4**	20,092,290	2.1
Financial intermediaries	**748,2523**	**0.1**	1,020,098	0.1
Others	**190,530,600**	**13.7**	184,289,636	19.6
	₱1,394,102,764	**100.0**	₱941,995,324	100.0

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.

9. Property and Equipment

The composition of and movements in this account follow:

2014	**Furniture, Fixtures and Equipment**	**Leasehold Improvements**	**Transportation Equipment**	**Building**	**Construction in Progress**	**Land**	**Total**
Cost							
Balance at beginning of year	**₱19,750,490**	**₱11,917,457**	**₱6,983,599**	**₱8,272,578**	**₱1,520,000**	**₱11,543,449**	**₱59,987,573**
Acquisition	**7,482,604**	**2,604,746**	**–**	**7,776,598**		**18,885,605**	**36,749,553**
Disposals/transfers	**(558,634)**	**–**	**(189)**	**1,520,000**	**(1,520,000)**	**–**	**(558,823)**
Balance at end of year	**26,674,460**	**14,522,203**	**6,983,410**	**17,569,176**	**–**	**30,429,054**	**96,178,303**
Accumulated Depreciation and Amortization							
Balance at beginning of year	**11,089,079**	**4,840,772**	**3,981,966**	**2,408,445**	**–**	**–**	**22,320,262**
Depreciation and amortization	**5,719,617**	**2,487,762**	**1,291,364**	**1,104,353**	**–**	**–**	**10,603,096**
Disposals/transfers	**(333,073)**	**–**	**(189)**	**–**	**–**	**–**	**(333,262)**
Balance at end of year	**16,475,623**	**7,328,534**	**5,273,141**	**3,512,798**	**–**	**–**	**32,590,096**
Net Book Value	**₱10,198,837**	**₱7,193,669**	**₱1,710,269**	**₱14,056,378**	**₱–**	**₱30,429,054**	**₱63,588,207**

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/transfers	(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

Loss on stolen/disposal of property and equipment amounted to ₱0.2 million and ₱0.1 million in 2014 and 2013, respectively.

The total cost of fully depreciated assets still in use is ₱10.8 million and ₱9.0 million as at December 31, 2014 and 2013

There are no restrictions on titles on property and equipment and the Bank does not have any contractual commitments for acquisition of property and equipment as of December 31, 2014 and 2013.

10. **Investment Properties**

The composition of and movements in this account follow:

		2014		
	Land	**Building**	**Assets held by SPV**	**Total**
Cost				
Balance at beginning of year	**₱17,993,156**	**₱860,082**	**₱7,793,447**	**₱26,646,685**
Disposals/transfers	**(421,400)**	**(122,081)**	**(2,442,034)**	**(2,985,515)**
Balance at end of year	**17,571,756**	**738,001**	**5,351,413**	**23,661,170**
Accumulated Depreciation				
Balance at beginning of year	–	**329,358**	–	**329,358**
Depreciation	–	**124,309**	–	**124,309**
Disposals/transfers	–	**(47,367)**	–	**(47,367)**
Balance at end of year	–	**406,300**	–	**406,300**
Allowance for Impairment Losses				
Balance at beginning of year	**7,881,894**	**436,550**	**3,422,111**	**11,740,555**
Reversals/transfers	**(3,074,655)**	**(145,667)**	**(1,867,595)**	**(5,087,917)**
Balance at end of year	**4,807,239**	**290,883**	**1,554,516**	**6,652,638**
Net Book Value	**₱12,764,517**	**₱40,818**	**₱3,796,897**	**₱16,602,232**

		2013		
	Land	Building	Assets held by SPV	Total
Cost				
Balance at beginning of year	₱22,650,822	₱1,530,500	₱8,788,674	₱32,969,996
Foreclosures	1,292,321	–	–	1,292,321
Disposals/transfers	(5,949,987)	(670,418)	(995,227)	(7,615,632)
Balance at end of year	17,993,156	860,082	7,793,447	26,646,685
Accumulated Depreciation				
Balance at beginning of year	–	560,891	–	560,891
Depreciation	–	163,305	–	163,305
Disposals/transfers	–	(394,838)	–	(394,838)
Balance at end of year	–	329,358	–	329,358
(Forward)				
Allowance for Impairment Losses				
Balance at beginning of year	₱7,432,213	₱–	₱2,906,120	₱10,338,333
Provisions	449,681	436,550	568,735	1,454,966
Reversals/transfers	–	–	(52,744)	(52,744)
Balance at end of year	7,881,894	436,550	3,422,111	11,740,555
Net Book Value	₱10,111,262	₱94,174	₱4,371,336	₱14,576,772

Fair value gain on initial recognition of foreclosed properties included under 'Miscellaneous income' amounted to nil and ₱1.1 million in 2014 and 2013, respectively.

Direct operating expenses on investment properties during the period, included under 'Miscellaneous expense' in the statements of income amounted to ₱0.5 million and ₱1.9 million in 2014 and 2013, respectively. Investment properties may be disposed through redemption, negotiated sale or lease purchase. In 2014 and 2013, all of the Bank's investment properties are non-revenue generating.

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

Gain on sale of investment properties amounted to ₱2.3 million in 2014 and loss of ₱1.9 million in 2013.

Assets held by a Special Purpose Vehicle
Assets held by a Special Purpose Vehicle (SPV) represents foreclosed properties (land) which have been specifically identified for sale under a sale and purchase agreement (SPA) with an SPV.

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.

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.

11. Intangible Asset

Intangible assets pertain to the licenses purchased by the Bank in relation to the core banking system to be implemented in 2015. The cost and the related amortization in 2014 amounted to ₱4.8 million and nil, respectively.

12. Other Assets

This account consists of:

	2014	2013
Financial assets:		
Refundable deposit	**₱372,396**	₱312,000
Nonfinancial assets:		
Stationeries and supplies	**7,156,994**	5,788,589
Prepaid expenses	**4,985,976**	3,652,723
Miscellaneous	**728,000**	827,914
	12,870,970	10,269,226
	₱13,243,366	₱10,581,226

13. Deposit Liabilities

Demand and savings deposits earn annual interest rate ranging from 1.5% to 5.0% and from 1.5% to 5.5% in 2014 and 2013, respectively.

Details of interest expense on deposit liabilities follow:

	2014	2013
Savings deposit	**₱12,036,065**	₱9,627,104
Special savings deposit	**9,415,296**	9,067,329
	₱21,451,361	₱18,694,433

In March 2014, the BSP issued Circular 830 effective March 27, 2014 unifying the liquidity and statutory reserves requirements to 7.0%, with cash in vault no longer eligible as reserve.

In May 2014, the BSP issued Circular 832, effective May 2014 which increased reserve requirement of thrift Banks by an additional 1.0%. Available reserves (which formed part of Due from BSP balance) as at December 31, 2014 and 2013 amounted to ₱81.1 million and ₱50.6 million, respectively, which will mature in 2015.

As at December 31, 2014 and 2013, the Bank is compliant with the applicable reserve requirements.

14. Bills Payable

Bills payable represent borrowings from financial institutions, which are subject to certain terms and conditions, payable within one year and bear annual interest rates ranging from 4.0% to 4.5% and 6.0% to 6.5% in 2014 and 2013, respectively.

As at December 31, 2014 and 2013, outstanding balance of bills payable amounted to ₱260.0 million and nil, respectively.

Microfinance loans amounting to ₱311.7 million and nil secure the above borrowings as at December 31, 2014 and 2013, respectively (Note 8).

Interest expense on bills payable in 2014 and 2013 amounted to ₱1.2 million and ₱39,755, respectively.

15. Other Liabilities

This account consists of:

	2014	2013
Financial liabilities:		
Accrued expenses	**₱22,624,427**	₱16,174,497
Accounts payable (Note 20)	**9,043,889**	3,586,196
Accrued interest payable	**2,215,755**	2,020,693
Dividends payable	**290,336**	40,148
	34,174,407	21,821,534
Nonfinancial liabilities:		
Accrued taxes	**4,625,867**	4,069,873
Unearned service fee income	**–**	455,488
Others	**2,454,974**	2,042,628
	7,080,841	6,567,989
	₱41,255,248	₱28,389,523

Accrued expenses include accruals for operating expenses and employee bonuses and benefits.

Accrued taxes include withholding, gross receipts and documentary stamp tax payable.

16. 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:

	2014			2013		
	Less than Twelve Months	**Over Twelve Months**	**Total**	Less than Twelve Months	Over Twelve Months	Total
Financial Assets						
Cash and other cash items	**₱6,679,030**	**₱–**	**₱6,679,030**	₱4,610,455	₱–	₱4,610,455
Due from BSP	**81,135,679**	**–**	**81,135,679**	50,603,710	–	50,603,710
Due from other banks	**112,018,132**	**–**	**112,018,132**	83,462,403	–	83,462,403
HTM investment	**873,068**	**10,204,080**	**11,077,148**	16,129,410	9,948,693	26,078,103
Loans and receivables - at gross	**1,358,016,595**	**36,086,169**	**1,394,102,764**	816,407,948	138,585,465	954,993,413
Refundable deposit	**–**	**372,396**	**372,396**	–	312,000	312,000
	1,558,722,504	**46,662,645**	**1,605,385,149**	971,213,926	148,846,158	1,120,060,084
Nonfinancial Assets						
Property and equipment - gross	**–**	**96,178,303**	**96,178,303**	–	59,987,573	59,987,573
Investment properties - gross	**–**	**23,384,508**	**23,384,508**	–	26,646,685	26,646,685
Deferred tax asset	**–**	**11,191,703**	**11,191,703**	–	25,418,282	25,418,282
Retirement asset	**–**	**33,636,973**	**33,636,973**	–	–	–
Intangible Assets	**–**	**4,772,600**	**4,772,600**	–	–	–
Other assets	**10,049,510**	**2,821,460**	**12,870,970**	10,269,226	–	10,269,226
	10,049,510	**171,985,547**	**182,035,057**	10,269,226	112,052,540	122,321,766
Less: Allowance for credit and impairment losses			**(₱53,115,102)**			(₱55,758,379)
Unearned interest			**(919,368)**			(1,175)
Accumulated depreciation and amortization			**(32,996,396)**			(22,649,620)
			(87,030,866)			(78,409,174)
			₱1,700,389,340			₱1,163,972,676

(Forward)

	2014			2013		
	Less than Twelve Months	**Over Twelve Months**	**Total**	Less than Twelve Months	Over Twelve Months	Total
Financial Liabilities						
Deposit liabilities						
Demand	**₱1,943,417**	**₱–**	**₱1,943,417**	₱441,307	₱–	₱441,307
Savings	**946,446,592**	**–**	**946,446,592**	828,013,759	–	828,013,759
Bills payable	**260,000,000**	**–**	**260,000,000**	–	–	–
Accrued expenses	**22,624,427**	**–**	**22,624,427**	16,174,497	–	16,174,497
Accrued interest payable	**2,215,755**	**–**	**2,215,755**	2,020,693	–	2,020,693
Accounts payable	**9,043,889**	**–**	**9,043,889**	3,586,196	–	3,586,196
Dividends payable	**290,336**	**–**	**290,336**	40,148	–	40,148
Other liabilities	**–**	**–**	**–**	455,488	–	455,488
	1,242,564,416	**–**	**1,242,564,416**	850,732,088	–	850,732,088
Nonfinancial Liabilities						
Income tax payable	**18,526,629**	**–**	**18,526,629**	10,305,392	–	10,305,392
Accrued taxes	**4,625,868**	**–**	**4,625,868**	4,069,873	–	4,069,873
Other liabilities	**2,454,973**	**–**	**2,454,973**	2,042,628	–	2,042,628
Retirement liability	**–**	**–**	**–**	–	29,089,823	29,089,823
	25,607,470	**–**	**25,607,470**	**16,417,893**	29,089,823	45,507,716
	₱1,268,171,886	**₱–**	**₱1,268,171,886**	₱867,149,981	₱29,089,823	₱896,239,804

17. Equity

Capital Stock

As at December 31, 2014 and 2013, the Bank's capital stock consists of:

	2014		2013	
	Shares	**Amount**	Shares	Amount
Common stock - ₱100 par value, 5,000,000 authorized shares				
Issued and outstanding	**1,375,755**	**₱137,575,500**	1,266,847	₱126,684,700
Subscribed	**3,624,245**	**362,424,500**	3,733,153	373,315,300
Subscription receivable		**(203,056,400)**		(248,980,062)
		₱296,943,600		₱251,019,938

The Bank issued 108,908 shares and 56,608 shares in 2014 and 2013, respectively.

Dividends

On May 10, 2014, the BOD approved the declaration cash dividends amounting to ₱12.6 million to stockholders of record as of April 30, 2014. The BSP approved the dividend declaration on July 3, 2014.

On September 13, 2014, the BOD approved the declaration of cash dividends amounting to ₱16.5 million to stockholders of record as of August 31, 2014. The BSP approved the dividend declaration on November 3, 2014.

On October 12, 2013, the BOD approved the declaration of cash dividends amounting to ₱6.1 million to stockholders of record as of September 30, 2013. The BSP approved the dividend declaration on December 17, 2013.

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, 2014 and 2013, the Bank's CAR is in compliance with the regulatory requirement. The CAR of the Bank as at December 31, 2014 and 2013, as reported to the BSP, is shown in the table below (amounts in thousands):

	2014	2013
Tier 1	**₱380,589**	₱264,256
Tier 2	**12,439**	8,341
Total qualifying capital	**₱393,028**	₱272,597
Risk-weighted assets	**₱1,595,469**	₱834,069
Tier 1 capital ratio	**23.9%**	31.7%
Tier 2 capital ratio	**0.7%**	1.0%
CAR	**24.6%**	32.7%

On October 9, 2014, the BSP issued BSP Circular No. 854 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. Based on this circular, the Bank is required to maintain a minimum capitalization of ₱300.0 million.

Financial Performance

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

	2014	2013
Return on average equity	**29.2%**	19.4%
Return on average assets	**7.1%**	4.2%
Net interest margin	**34.0%**	30.9%

18. **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 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 retirement liability (assets) in 2014 are as follows:

		Net benefit cost recognized in the statement of income					Remeasurements in other comprehensive income						
	January 1, 2014	Current service cost	Net interest	Net Pension Expense*	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	Changes in the effect of limiting net defined benefit asset to the asset ceiling	Subtotal	Contribution by employer	December 31, 2014
Present value of defined benefit obligation	₱122,093,218	₱17,867,000	₱7,789,547	₱25,656,547	(₱319,498)	₱6,016,049	₱–	(₱20,610,491)	(₱52,493,860)	₱–	(₱73,104,351)	₱–	₱80,341,965
Fair value of plan Assets	(93,003,395)	–	(6,651,677)	(6,651,677)	319,498	(6,016,049)	4,505,211	–	–	–	4,505,211	(16,813,182)	(117,659,594)
Effect of Asset Ceiling	–	–	–	–	–	–	–	–	–	3,680,656	3,680,656	–	3,680,656
Net defined benefit liability (asset)	₱29,089,823	₱17,867,000	₱1,137,870	₱19,004,870	₱–	₱–	₱4,505,211	(₱20,610,491)	(₱52,493,860)	₱3,680,656	(₱64,918,484)	(₱16,813,182)	(₱33,636,973)

* Presented under 'Compensation and fringe benefits' in the statements of income.

Changes in retirement liability (assets) in 2013 are as follows:

		Net benefit cost recognized in the statement of income					Remeasurements in other comprehensive income					
	January 1, 2013	Current service cost	Net interest	Net Pension Expense*	Benefits Paid	Transfer (from) to plan	Return on plan assets (excluding amount included in net interest)	Actuarial changes arising from changes in demographic assumptions	Changes in the effect of limiting a net defined benefit asset to the asset ceiling	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	₱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

* Presented under 'Compensation and fringe benefits' in the statements of income.

Transfer from (to) of plan assets represents transfer of obligation and plan assets to the respective CARD MRI entity as a result of movements in employees among the CARD MRI entities.

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:

	2014	2013
Cash and cash equivalents	**₱46,263,752**	₱50,417,140
Investments		
Debt securities		
Government securities	**53,970,456**	33,890,437
Equity securities	**–**	585,921
Mutual funds	**1,106,000**	1,283,447
Receivables	**13,036,683**	5,747,610
Other assets	**3,282,703**	1,078,840
Fair value of plan assets	**₱117,659,594**	₱93,003,395

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.

The management performed an Asset-Liability Matching Study 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 latest actuarial valuation study of the retirement plan was made as of December 31, 2014. The principal actuarial assumptions as of December 31, 2014 and 2013 used in determining the retirement obligation for the Bank's retirement plan are shown below:

	2014	2013
Discount rates	**4.5%**	6.4%
Future salary increases	**7.0%**	12.0%

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:

	2014		2013	
	Increase of 1.0%	**Decrease of 1.0%**	Increase of 2.5%	Decrease of 1.0%
Discount rate	**(₱16,550,931)**	**₱21,529,488**	(₱55,603,986)	₱71,732,827
Salary rate	**19,844,993**	**(15,773,410)**	35,309,918	(25,004,294)

The Bank plans to contribute ₱15.6 million to the defined benefit retirement plan in 2015.

As at December 31, 2014 and 2013, the average duration of the defined benefit obligation is 27.5 years and 28.3 years, respectively.

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

	2014	2013
Less than 1 year	**₱–**	₱–
More than 1 year to 5 years	**1,315,940**	1,473,293
More than 5 years to 10 years	**8,246,945**	21,543,351

19. **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 ₱5.7 million and ₱2.9 million in 2014 and 2013, respectively.

Provision for income tax consists of:

	2014	2013
RCIT	**₱49,004,462**	₱22,747,099
Final tax	**528,708**	826,814
	49,533,170	23,573,913
Deferred	**(5,248,966)**	(4,930,320)
	₱44,284,204	₱18,643,593

Deferred tax recognized in other comprehensive income amounted to ₱19.5 million and ₱3.9 million for the years ended December 31, 2014 and 2013, respectively.

Components of deferred tax assets - net are as follows:

	2014	2013
Deferred tax asset on:		
Allowance for credit and impairment losses	**₱16,017,529**	₱12,828,087
Unamortized past service cost	**4,000,471**	3,496,447
Accumulated vacation leave	**2,829,011**	2,051,186
Accumulated depreciation - investment Properties	**121,890**	98,807
Retirement liability	**–**	8,726,947
	22,968,901	27,201,474
Deferred tax liability on:		
Retirement asset	**10,091,092**	–
Fair value adjustment on investment properties	**1,686,106**	1,783,192
	11,777,198	1,783,192
	₱11,191,703	₱25,418,282

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

	2014	2013
Statutory income tax	**₱43,930,819**	₱17,913,149
Income tax effects of:		
Nondeductible operating expenses	**622,018**	5,156,369
Interest income subject to final tax and nontaxable income	**(268,633)**	(1,290,018)
Change in unrecognized deferred tax assets	**–**	(4,103,506)
Nontaxable income	**–**	967,599
Provision for income tax	**₱44,284,204**	₱18,643,593

20. 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. MERP is managed by the CARD Employee EMPC. MERP has savings deposit amounting to ₱125.1 million and ₱0.1 million in 2014 and 2013, respectively.

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):

	2014	2013
Short-term employee benefits	**₱8.1**	₱7.8
Post-employment benefits	**2.0**	4.3
	₱10.1	₱12.1

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, 2014 and 2013, 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, 2014 and 2013 (in thousands):

	December 31, 2014		
Category	**Amount/Volume**	**Outstanding Balance**	**Nature, Terms and Conditions**
Key Management Personnel			
Deposit liabilities		**₱1,180,377**	These are savings accounts with annual interest rates ranging from 1.5% to 5.0%.
Interest expense	**₱4,845**		Pertains to interest on deposit liabilities.
Shareholders			
Accounts receivable		**1,110**	The amount represents the shareholders’ share of expenses payable to the Bank.
Deposit liabilities		**37,028,329**	These are savings accounts with annual interest rates ranging from 1.5% to 5.0%.
Accounts payable		**1,030**	The amount represents the Bank’s share of staffs’ monthly contribution.
Interest expense	**1,830,888**		Pertains to interest on deposit liabilities.
Other related parties			
Deposit liabilities		**54,320,425**	These are savings accounts with annual interest rates ranging from 1.5% to 5.0%.

(Forward)

	December 31, 2014		
Category	**Amount/Volume**	**Outstanding Balance**	**Nature, Terms and Conditions**
Accounts receivable		**₱104,680**	The amount represents the affiliates' share of expenses payable to the Bank.
Accounts payable		**2,882,827**	The amount represents the Bank's share of expenses payable to affiliates.
Interest expense	**₱7,752,797**		Pertains to interest on deposit liabilities.
Seminars and trainings expense	**8,939,377**		The Bank engaged CMDI for training and development of its members and employees (shown as part of 'Employee trainings' and 'Meetings and seminars' in the statement of income).
Information technology	**6,835,346**		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.

	December 31, 2013		
Category	Amount/Volume	Outstanding Balance	**Nature, Terms and Conditions**
Key Management Personnel			
Deposit liabilities		₱1,307,000	These are savings accounts with annual interest rates ranging from 1.5% to 5.5%
Shareholder			
Deposit liabilities		772,163	These are savings accounts with annual interest rates ranging from 1.5% to 5.5%.
Accounts payable		3,100	This represents loan collection from members on behalf of the shareholders.
Occupancy	₱60,000		An establishment owned by CARD, Inc. is being leased to the Bank. lease contracts renewable annually.
Interest expense	1,580,298		Pertains to interest on savings accounts with annual rates ranging from 1.5% to 5.5%.
Other related parties			
Deposit liabilities		132,252,074	These are savings accounts with annual interest rates ranging from 1.5% to 5.5%.
Accounts receivable		3,519,400	The amount represents the affiliate's share of expenses payable to the Bank.
Accounts payable		2,906	The amount represents the Bank's share of expenses payable to affiliates.
Seminars and trainings expense	6,467,769		The Bank engaged CMDI for training and development of its members and employees (shown as part of 'Employee trainings' and 'Meetings and seminars' in the statement of income).
Interest expense	7,419,422		Pertains to interest on savings accounts with annual rates ranging from 1.5% to 5.5%.
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 2014.
Information technology	5,901,205		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.

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, 70.0% 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 15.0% of total loan portfolio, whichever is lower. As at December 31, 2014 and 2013, 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, 2014 and 2013, there were no loans, other credit accommodations and guarantees classified as DOSRI accounts under the existing regulations as shown in the table below:

	2014	2013
Total outstanding DOSRI accounts	**₱–**	₱–
Percent of DOSRI accounts granted prior to effectivity of BSP Circular No. 423 to total loans	**0.0%**	0.0%
Percent of DOSRI accounts granted after effectivity of BSP Circular No. 423 to total loans	**0.0%**	0.0%
Percent of DOSRI accounts to total loans	**0.0%**	0.0%
Percent of unsecured DOSRI accounts to total DOSRI accounts	**0.0%**	0.0%
Percent of past due DOSRI accounts to total DOSRI accounts	**0.0%**	0.0%
Percent of nonaccruing DOSRI accounts to total DOSRI accounts	**0.0%**	0.0%

21. 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. and third-party lessors.

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

	2014	2013
Within one year	**₱1,181,460**	₱4,948,382
Beyond one year but not more than five years	**3,014,569**	7,895,604
	₱4,196,029	₱12,843,986

22. 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, 2014 and 2013, 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.

23. Notes to Statements of Cash Flows

Noncash activities of the Bank consist of the following:

	2014	2013
Noncash investing activities:		
Foreclosure of investment properties	₱–	₱150,000

24. Approval of the Release of Financial Statements

The accompanying financial statements were approved and authorized for issue by the BOD on March 14, 2015.

25. 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 2014 follow:

Gross receipts tax	₱28,276,794
Business permits and licenses	2,564,464
Documentary stamp tax (DST)	1,848,782
Real property tax	35,225
Others	1,795,239
	₱34,520,504

In 2014, withholding taxes lodged under 'Accrued taxes' account are categorized into:

Paid:	
Withholding taxes on compensation and benefits	₱6,694,176
Expanded withholding tax	3,087,261
Final withholding tax on interest expense	2,734,875
	₱12,516,312
Accrued:	
Final withholding tax on interest expense	₱713,632
Withholding taxes on compensation and benefits	370,541
Expanded withholding tax	166,499
	₱1,250,672

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