BPI Direct BanKo, Inc., A Savings Bank

(Formerly BPI Direct Savings Bank, Inc.)

Financial Statements
As at and for the years ended December 31, 2018 and 2017

Independent Auditor's Report

To the Board of Directors and Shareholder of
BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)
G/F BanKo Center Building
Ortigas Avenue, North Greenhills
San Juan, Metro Manila

Report on the Audits of the Financial Statements

Our Opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of BPI Direct BanKo, Inc., A Savings Bank (formerly BPI Direct Savings Bank, Inc.) (the "Bank") as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with Philippine Financial Reporting Standards (PFRSs).

What we have audited

The financial statements of the Bank comprise:

- the statements of condition as at December 31, 2018 and 2017;
- the statements of income for the years ended December 31, 2018 and 2017;
- the statements of comprehensive income for the years ended December 31, 2018 and 2017;
- the statements of changes in capital funds for the years ended December 31, 2018 and 2017;
- the statements of cash flows for the years ended December 31, 2018 and 2017; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for Opinion

We conducted our audits in accordance with Philippine Standards on Auditing (PSAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Bank in accordance with the Code of Ethics for Professional Accountants in the Philippines (Code of Ethics), together with the ethical requirements that are relevant to our audit of the financial statements in the Philippines, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics.

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Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with PFRSs, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with PSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with PSAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Report on the Bureau of Internal Revenue Requirement

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information in Note 25 to the financial statements is presented for purposes of filing with the Bureau of Internal Revenue and is not a required part of the basic financial statements. Such supplementary information is the responsibility of management and has been subjected to the auditing procedures applied in our audits of the basic financial statements. In our opinion, the supplementary information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Isla Lipana & Co.

Ruth F. Blasco
Partner
CPA Cert. No. 112595
P.T.R. No. 0018519, issued on January 8, 2019, Makati City
SEC A.N. (individual) as general auditors 1653-A, Category A; effective until August 23, 2020
SEC A.N. (firm) as general auditors 0009-FR-5, Category A; effective until June 20, 2021
TIN 235-725-236
BIR A.N. 08-000745-133-2017, issued on June 8, 2017; effective until June 7, 2020
BOA/PRC Reg. No. 0142, effective until September 30, 2020

Makati City
March 29, 2019

Isla Lipana & Co.

Statement Required by Section 8-A, Revenue Regulations No. V-1

To the Board of Directors and Shareholder of
BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)
G/F BanKo Center Building
Ortigas Avenue, North Greenhills
San Juan, Metro Manila

None of the partners of the firm has any financial interest in BPI Direct BanKo, Inc., A Savings Bank (formerly BPI Direct Savings Bank, Inc.) or any family relationships with its president, manager, or principal shareholder.

The supplementary information on taxes and licenses is presented in Note 25 to the financial statements.

Isla Lipana & Co.

Ruth F. Blasco
Partner
CPA Cert. No. 112595
P.T.R. No. 0018519, issued on January 8, 2019, Makati City
SEC A.N. (individual) as general auditors 1653-A, Category A; effective until August 23, 2020
SEC A.N. (firm) as general auditors 0009-FR-5, Category A; effective until June 20, 2021
TIN 235-725-236
BIR A.N. 08-000745-133-2017, issued on June 8, 2017; effective until June 7, 2020
BOA/PRC Reg. No. 0142, effective until September 30, 2020

Makati City
March 29, 2019

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Isla Lipana & Co.

Statements Required by Rule 68
Securities Regulation Code (SRC)

To the Board of Directors and Shareholder of
BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)
G/F BanKo Center Building
Ortigas Avenue, North Greenhills
San Juan, Metro Manila

We have audited the financial statements of BPI Direct BanKo, Inc., A Savings Bank (formerly BPI Direct Savings Bank, Inc.) as at and for the year ended December 31, 2018, on which we have rendered the attached report dated March 29, 2019. The supplementary information shown in the Reconciliation of Retained Earnings Available for Dividend Declaration and Schedule of Philippine Financial Reporting Standards effective as at December 31, 2018, as additional components required by Rule 68 of the SRC, is presented for purposes of filing with the Securities and Exchange Commission and is not a required part of the basic financial statements. Such supplementary information is the responsibility of management and has been subjected to the auditing procedures applied in the audit of the basic financial statements. In our opinion, the supplementary information has been prepared in accordance with Rule 68 of the SRC.

Isla Lipana & Co.

Ruth F. Blasco
Partner
CPA Cert. No. 112595
P.T.R. No. 0018519, issued on January 8, 2019, Makati City
SEC A.N. (individual) as general auditors 1653-A, Category A; effective until August 23, 2020
SEC A.N. (firm) as general auditors 0009-FR-5, Category A; effective until June 20, 2021
TIN 235-725-236
BIR A.N. 08-000745-133-2017, issued on June 8, 2017; effective until June 7, 2020
BOA/PRC Reg. No. 0142, effective until September 30, 2020

Makati City
March 29, 2019

Isla Lipana & Co.

Statements Required by Rule 68, Part I, Section 3F,
Securities Regulation Code (SRC)

To the Board of Directors and Shareholder of
BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)
G/F BanKo Center Building
Ortigas Avenue, North Greenhills
San Juan, Metro Manila

We have audited the accompanying financial statements of BPI Direct BanKo, Inc., A Savings Bank (formerly BPI Direct Savings Bank, Inc.) (the "Bank") as at and for the year ended December 31, 2018, on which we have rendered the attached report dated March 29, 2019.

In compliance with SRC Rule 68 and based on the certification received from the Bank's corporate secretary and the results of our work performed, as at December 31, 2018, the Bank has one (1) shareholder owning more than one hundred (100) shares.

Isla Lipana & Co.

Ruth F. Blasco
Partner
CPA Cert. No. 112595
P.T.R. No. 0018519, issued on January 8, 2019, Makati City
SEC A.N. (individual) as general auditors 1653-A, Category A; effective until August 23, 2020
SEC A.N. (firm) as general auditors 0009-FR-5, Category A; effective until June 20, 2021
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Makati City
March 29, 2019

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Statements of Condition
December 31, 2018 and 2017
(All amounts in Philippine Peso)

	Notes	2018	2017
RESOURCES			
Cash and other cash items	2	86,383,976	26,310,761
Due from other banks	2	884,795,667	967,092,652
Interbank loans receivable	2,3	300,158,333	165,255,798
Due from Bangko Sentral ng Pilipinas	2,4	3,853,846,029	8,793,748,200
Investment securities at fair value through other comprehensive income	5	100,065,545	-
Available-for-sale securities, net	5	-	102,960,515
Loans and advances, net	7	9,245,194,688	4,296,200,000
Assets held for sale		75,446,961	89,686,467
Bank premises, furniture, fixtures and equipment, net	8	460,599,271	208,156,620
Deferred income tax assets, net	9	237,456,216	241,518,073
Other resources, net	10	352,491,944	204,595,618
Total resources		15,596,438,630	15,095,524,704
LIABILITIES AND CAPITAL FUNDS			
Deposit liabilities	11	12,560,640,302	12,838,030,191
Accrued taxes, interest and other expenses	12	110,198,851	90,863,353
Other liabilities	13	560,122,334	55,152,000
Total liabilities		13,230,961,487	12,984,045,544
CAPITAL FUNDS	14		
Share capital		405,572,100	405,572,100
Other comprehensive income		2,959,183	6,111,307
Other reserves	1.2	(269,815,403)	(269,815,403)
Surplus		2,226,761,263	1,969,611,156
Total capital funds		2,365,477,143	2,111,479,160
		15,596,438,630	15,095,524,704

(The notes on pages 1 to 68 are an integral part of these financial statements.)

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Statements of Income
For the years ended December 31, 2018 and 2017
(All amounts in Philippine Peso)

	Notes	2018	2017
INTEREST INCOME			
Loans and advances	7	1,652,444,541	389,715,812
Deposits with BSP and other banks	2,4	126,588,155	190,664,194
Interbank loans receivable	3	37,118,508	47,505,587
Investment securities	5,6	6,210,369	29,534,589
		1,822,361,573	657,420,182
INTEREST EXPENSE ON DEPOSITS	11	103,622,893	94,089,205
NET INTEREST INCOME		1,718,738,680	563,330,977
PROVISION FOR IMPAIRMENT		402,811,564	1,937,788
NET INTEREST INCOME AFTER PROVISION FOR IMPAIRMENT		1,315,927,116	561,393,189
OTHER INCOME			
Service fee income		209,618,152	69,161,682
Profit on assets sold		13,193,833	5,453,227
Miscellaneous income	15	41,018,341	107,264,336
		263,830,326	181,879,245
OTHER EXPENSES			
Compensation and fringe benefits	18,19	433,626,042	158,215,824
Occupancy and equipment-related expenses	19	372,420,864	174,623,807
Other operating expenses	16	417,257,446	203,618,323
		1,223,304,352	536,457,954
INCOME BEFORE PROVISION FOR INCOME TAX		356,453,090	206,814,480
PROVISION FOR INCOME TAX	17		
Current		82,470,244	60,939,910
Deferred	9	4,992,461	61,330,547
		87,462,705	122,270,457
NET INCOME FOR THE YEAR		268,990,385	84,544,023

(The notes on pages 1 to 68 are an integral part of these financial statements.)

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Statements of Comprehensive Income
For the years ended December 31, 2018 and 2016
(All amounts in Philippine Peso)

	Note	2018	2017
NET INCOME FOR THE YEAR		268,990,385	84,544,023
OTHER COMPREHENSIVE (LOSS) INCOME	14		
Item that will be subsequently reclassified to profit or loss			
Net change in fair value reserve on investment securities at fair value through other comprehensive income, net of tax		(2,316,971)	-
Net change in fair value reserve AFS securities , net of tax		-	(830,390)
Item that will not be subsequently reclassified to profit or loss			
Remeasurement (loss) gain on retirement benefit obligation, net of tax		(822,742)	2,394,013
Total other comprehensive (loss) income		(3,139,713)	1,563,623
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		265,850,672	86,107,646

(The notes on pages 1 to 68 are an integral part of the financial statements.)

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Statements of Changes in Capital Funds
For the years ended December 31, 2018 and 2017
(All amounts in Philippine Peso)

	Share capital (Note 14)	Accumulated other comprehensive income (Note 14)	Other reserves	Surplus (Note 14)	Total
BALANCE, JANUARY 1, 2017	405,572,100	4,547,684	(269,815,403)	1,885,067,133	2,025,371,514
COMPREHENSIVE INCOME					
Net income for the year	-	-	-	84,544,023	84,544,023
Other comprehensive income	-	1,563,623	-	-	1,563,623
Total comprehensive income for the year	-	1,563,623	-	84,544,023	86,107,646
BALANCE, DECEMBER 31, 2017	405,572,100	6,111,307	(269,815,403)	1,969,611,156	2,111,479,160
Effect of adoption of PFRS 9	-	(12,411)	-	(11,840,278)	(11,852,689)
BALANCE, AS RESTATED	405,572,100	6,098,896	(269,815,403)	1,957,770,878	2,099,626,471
COMPREHENSIVE INCOME					
Net income for the year	-	-	-	268,990,385	268,990,385
Other comprehensive loss	-	(3,139,713)	-	-	(3,139,713)
Total comprehensive income (loss) for the year	-	(3,139,713)	-	268,990,385	265,850,672
BALANCE, DECEMBER 31, 2018	405,572,100	2,959,183	(269,815,403)	2,226,761,263	2,365,477,143

(The notes on pages 1 to 68 are an integral part of the financial statements.)

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Statements of Cash Flows
For the years ended December 31, 2018 and 2017
(All amounts in Philippine Peso)

	Notes	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES			
Income before provision for income tax		356,453,090	206,814,480
Adjustments for:			
Interest income		(1,909,929,193)	(681,112,038)
Interest expense	11	103,622,893	94,089,205
Gain on sale of held-to-maturity security		-	(78,749,152)
Write-off of long outstanding payables		-	(15,835,156)
Depreciation	8	106,546,180	19,036,408
Gain on sale of legacy loans		-	(11,044,617)
Profit on assets sold		(14,160,636)	(5,863,685)
Retirement benefit expense	18	19,921,446	3,554,963
Provision for impairment	7,10,22	402,811,564	1,937,788
Amortization of premium	6	-	181,522
Interest received		1,797,415,783	690,246,205
Interest paid		(84,227,336)	(93,172,948)
Operating income before changes in operating resources and liabilities		778,453,791	130,082,975
Changes in operating resources and liabilities			
(Increase) decrease in:			
Loans and advances		(5,273,631,051)	753,099,498
Assets held for sale		28,400,142	(18,054,057)
Other resources		(215,392,266)	(39,485,069)
Increase (decrease) in:			
Deposit liabilities		(277,389,887)	(461,421,653)
Accrued taxes, interest and other expenses		22,485,518	(13,239,276)
Other liabilities		504,970,334	5,907,619
Net cash (used in) from operations		(4,432,103,419)	356,890,037
Retirement plan contributions	18	(755,645)	(948,356)
Income tax paid		(35,375,511)	(55,910,760)
Net cash (used in) from operating activities		(4,468,234,575)	300,030,921
CASH FLOWS GENERATED FROM INVESTING ACTIVITIES			
Proceeds from sale of held-to-maturity security		-	440,315,921
Additions to bank premises, furniture, fixture, and equipment	8	(358,988,831)	(205,223,761)
Net cash (used in) from investing activities		(358,988,831)	235,092,160
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS		(4,827,223,406)	535,123,081
CASH AND CASH EQUIVALENTS			
January 1		9,952,407,411	9,417,284,330
December 31		5,125,184,005	9,952,407,411

(The notes on pages 1 to 68 are an integral part of these financial statements.)

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Notes to the Financial Statements
As at and for the years ended December 31, 2018 and 2017
(All amounts are shown in Philippine Peso, unless otherwise stated)

Note 1 - General information

1.1 Business information

BPI Direct BanKo, Inc., A Savings Bank (the "Bank"), formerly known as BPI Direct Savings, Inc. ("BPI Direct"), was incorporated in the Philippines and registered with the Securities and Exchange Commission (SEC) on September 26, 1986 primarily to engage in and carry on the general business of savings and mortgage banking.

The Bank is a wholly-owned subsidiary of Bank of the Philippine Islands (BPI or the "Parent Bank"), a domestic commercial bank with an expanded banking license, which is also its ultimate parent.

The Bank's registered office address, which is also its principal place of business, is BanKo Center Building, Ortigas Avenue, North Greenhills, San Juan, Metro Manila. The Bank has 1,851 regular employees as at December 31, 2018 (2017 - 951).

1.2 Common control business combination

On February 24, 2016, the Board of Directors of the Bank approved the merger with BPI Globe BanKo, Inc. ("BanKo"), a fellow subsidiary, with the Bank as the surviving entity. BanKo was incorporated in the Philippines and registered with the SEC on June 26, 1998 primarily to engage in, and carry on, the general business of savings and mortgage banking. BanKo was a wholly-owned subsidiary of BPI effective September 20, 2016.

The merger is aimed at integrating the banking operations of BanKo into the Bank and at bringing efficiency and scale to the surviving entity. The merged business is expected to leverage on a bigger customer base and will benefit from cost-savings and operational synergies.

The plan of merger was cleared by the BanKo Sentral ng Pilipinas (BSP) on December 15, 2016. On December 29, 2016, the SEC likewise approved the merger including the amendment to the Bank's articles of incorporation changing the name of the Bank from BPI Direct Savings Bank, Inc. to BPI Direct BanKo, Inc., A Savings Bank.

As the transaction is outside the scope of PFRS 3, *Business Combinations*, the merger was accounted for using the pooling of interests method following the guidance under the PIC Q&A No. 2011-02 and PIC Q&A 2012-01. In applying the pooling of interests method, all resources and liabilities of BanKo are taken into the merged business at their carrying values with no restatement of comparative 2015 figures. Likewise, no goodwill was recognized in the business combination.

Details of BanKo's assets and liabilities as at December 28, 2016 are as follows:

	Amount
Resources acquired	
Cash and other cash items	5,250,717
Due from other banks	22,449,138
Due from Bangko Sentral ng Pilipinas	73,483,568
Loans and advances, net	102,699,171
Bank premises, furniture, fixtures and equipment, net	21,955,667
Other resources	82,585,931
	308,424,192
Liabilities assumed	
Deposit liabilities	441,251,566
Accrued taxes, interest and other expenses	66,669,507
Other liabilities	39,279,722
	547,200,795
Excess of total liabilities over total resources	(238,776,603)

The plan of merger provides that the Bank shall issue 0.02351 of its own common share for every common share held by BanKo shareholders. Accordingly, the Bank issued a total of 310,388 common shares in exchange for BanKo's resources and liabilities at December 28, 2016 giving rise to Other reserves (with debit balance) which is presented as a deduction in the total equity of the Bank as follows:

	Note	Amount
Equity instruments issued (13,200,000 BanKo shares x 0.02351)	14	310,388
Par value per share		100
Total value of common shares issued		31,038,800
Net liabilities assumed		(238,776,603)
Other reserves (deduction in equity)		269,815,403

Had the business combination occurred on January 1, 2016, total interest income and net income of the Bank for the year ended December 31, 2016 still would have been P652,421,959 and P267,827,753, respectively.

The acquisition of BanKo's operations contributed interest income of P198,821 and net loss of P1,158,211 to the Bank for the period from December 29 to 31, 2016. Acquisition-related costs of P155,194 that were not directly attributable to the issue of shares were included in other operating expenses in the statement of income.

1.3 Approval of the Bank's financial statements

These financial statements have been approved and authorized for issuance by the Board of Directors (BOD) on March 27, 2019. There are no material events that occurred subsequent to March 27, 2019 until March 29, 2019.

Note 2 - Cash and cash equivalents

The account as at December 31 consists of:

	Notes	2018	2017
Cash and other cash items		86,383,976	26,310,761
Due from other banks		884,795,667	967,092,652
Interbank loans receivable	3	300,158,333	165,255,798
Due from BSP	4	3,853,846,029	8,793,748,200
		5,125,184,005	9,952,407,411

For the year ended December 31, 2018, interest income earned on Due from other banks amounts to P2,879,215 (2017 - P2,744,934).

Cash and cash equivalents are classified as current.

Note 3 - Interbank loans receivable

The account at December 31 consists of transactions with:

	2018	2017
BSP	300,000,000	165,214,494
Accrued interest receivable	158,333	41,304
	300,158,333	165,255,798

Interbank loans receivable maturing within 90 days from the date of acquisition are classified as cash equivalents in the statement of cash flows (Note 2).

Government bonds are pledged by the BSP as collaterals under reverse repurchase agreements. The face value of securities pledged is equivalent to the total balance of outstanding placements as at reporting date. All collateral agreements mature within 12 months.

Average interest rate on interbank loans receivable as at December 31, 2018 is 3.26% (2017 - 3.03%). Total interest earned on interbank loans receivable amounts to 37,118,508 for the year ended December 31, 2018 (2017 - P47,505,587).

Interbank loans receivable are classified as current.

Note 4 - Due from Bangko Sentral ng Pilipinas (BSP)

The account as at December 31 consists of:

	2018	2017
Special deposit account	2,800,000,000	7,700,000,000
Clearing account	1,053,846,029	1,093,748,200
	3,853,846,029	8,793,748,200

Special deposit accounts classified as cash equivalents are fixed-term demand Philippine Peso deposits maintained in compliance with the simplified minimum reserve requirements of the BSP (Note 11).

Clearing accounts represent temporary deposit accounts wherein funds flow from cleared checks are credited against or debited for.

As at December 31, 2018, Due from BSP in 2018 includes special deposit placements of P2.8 billion (2017 - P7.7 billion) with maturities of not more than 28 days. Average interest rate on due from BSP at December 31, 2018 is 2.89% (2017 - 3.47%). Total interest earned on due from BSP amounts to P123,708,940 for the year ended December 31, 2018 (2017 - P187,919,260).

Due from BSP are classified as current.

Note 5 - Investment securities at fair value through other comprehensive income (FVOCI) (2017 - Available-for-sale securities, net)

The account at December 31 consists of:

	2018	2017
Corporate bond	99,640,000	102,530,000
Listed equity security	7,338	24,720
	99,647,338	102,554,720
Accrued interest receivable on corporate bond	418,207	418,207
	100,065,545	102,972,927
Allowance for impairment	-	(12,412)
	100,065,545	102,960,515

	2018	2017
Current	418,207	418,207
Non-current	99,647,338	102,554,720
	100,065,545	102,972,927

For the years ended December 31 2018 and 2017, interest rate on corporate bond is 6.27%.

The movements in investment securities as at December 31, 2017 and 2018 are as follows:

	Available-for-sale securities
At January 1, 2017	103,998,905
Fair value adjustment	(1,038,390)
At December 31, 2017	102,960,515

	Investment securities at FVOCI
Reclassification due to adoption of PFRS 9 on January 1, 2018	102,960,515
Fair value adjustment	(2,894,970)
At December 31, 2018	100,065,545

Note 6 - Held-to-maturity security

The movements in the account for the year ended December 31, 2017 are summarized as follows:

	Amount
Balance, January 1	367,241,694
Amortization of premium	(181,523)
Net change in accrued interest receivable	(4,744,444)
Disposal	(362,315,727)
Balance, December 31	-

In November 2017, the Bank sold its held-to-maturity (HTM) security to its Parent Bank for P440,315,921, resulting in a gain on sale of P78,749,152. Interest income earned on held-to-maturity security amounted to P23,324,220 for the year ended December 31, 2017.

Note 7 - Loans and advances, net

The account as at December 31 consists of:

	2018	2017
Corporate entities		
Large corporate customers	206,567,033	253,164,984
Small and medium enterprises	18,512,754	43,951,021
Retail customers		
Real estate mortgages	2,947,854,716	3,751,692,238
Auto loans	864,427	5,052,492
Others	6,594,079,926	422,153,895
	9,767,878,856	4,476,014,630
Accrued interest receivable	147,797,691	22,543,373
Unearned discount	(115,397)	(115,397)
	9,915,561,150	4,498,442,606
Allowance for impairment	(670,366,462)	(202,242,606)
	9,245,194,688	4,296,200,000

Average effective interest rate on loans and advances is 11.85% at December 31, 2018 (2017 - 8.89%). Interest income from loans and advances amounts to P1,652,444,541 for the year ended December 31, 2018 (2017 - P389,715,812).

	2018	2017
Current	9,043,912,244	2,759,797,362
Non-current	871,648,906	1,738,645,244
	9,915,561,150	4,498,442,606

Loans and advances that are classified as current are those which are expected to be realized within 12 months after reporting date while non-current balances pertain to those expected to be collected beyond 12 months after reporting date.

Non-performing loans, net of allowance for credit losses are as follows:

	2018	2017
Non-performing loans (NPL)	709,385,859	299,266,183
Accounts with specific allowance for credit losses	(413,812,248)	(185,626,823)
Net NPL	295,573,611	113,639,360

BSP Circular 941, Amendments to Regulations on Past Due and Non-Performing Loans, states that loans, investments, receivables, or any financial asset shall be considered non-performing, even without any missed contractual payments, when it is considered impaired under existing accounting standards, classified as doubtful or loss, in litigation, and if there is an evidence that full repayment of principal and interest is unlikely without foreclosure of collateral. All other loans, even if not considered impaired, shall be considered non-performing if any principal and/or interest are unpaid for more than ninety (90) days from contractual due date, or accrued interests for more than ninety (90) days have been capitalized, refinanced, or delayed by agreement. Microfinance and other small loans with similar credit characteristics shall be considered non-performing after contractual due date or after it has become past due. Restructured loans shall be considered non-performing. However, if prior to restructuring, the loans were categorized as performing, such classification shall be retained.

The movements in allowance for impairment are as follows:

	Note	2018	2017
Balance, January 1		202,242,606	307,134,488
Transitional adjustment due to PFRS 9		11,852,689	-
Provision for loan impairment		401,046,050	10,964,223
Transfer of allowance due to purchase of personal loans		203,398,723	-
Write-offs		(146,928,273)	(3,849,453)
Transfers to assets held for sale		(1,245,333)	(2,606,916)
Sale of legacy loans		-	(109,399,736)
Balance, December 31		670,366,462	202,242,606

In 2018, the Bank purchased the personal loan portfolio of its Parent Bank amounting to P7,837,684,431.

In 2017, the Bank sold its legacy loans with carrying value of P5,415,739 to a third party at P16,460,356, resulting in a gain on sale of P11,044,617 (Note 15).

Details of the loans and advances portfolio as at December 31 are as follows:

As to industry or economic sector (in %)

	2018	2017
Private household with employed persons	73.26	76.89
Wholesale and retail trade	22.10	10.30
Real estate, renting and other related activities	3.76	10.65
Manufacturing	0.02	0.16
Others	0.86	2.00
	100.00	100.00

BSP considers that concentration of credit risk exists when the loan exposure to a particular industry or sector exceeds 30% of the loan portfolio. The Bank has a high concentration of credit risk on loans extended to those which belong to private household with employed persons.

As to collateral

	2018	2017
Secured loans		
Real estate mortgage	2,449,805,397	2,671,423,777
Chattel mortgage	756,567	4,951,517
	2,450,561,964	2,676,375,294
Unsecured loans	7,464,999,186	1,822,067,312
	9,915,561,150	4,498,442,606

Note 8 - Bank premises, furniture, fixtures and equipment, net

The movements in the account are summarized as follows:

	2018				
	Furniture, fixtures, and equipment	Leasehold rights and improvement	Computer equipment	Leasehold rights and improvements in progress	Total
Cost					
January 1, 2018	69,662,967	200,496,767	18,649,413	2,814,547	291,623,694
Additions	174,957,620	170,952,690	13,078,521	-	358,988,831
Transfers	-	2,356,007	-	(2,356,007)	-
December 31, 2018	244,620,587	373,805,464	31,727,934	458,540	650,612,525
Accumulated depreciation					
January 1, 2018	26,312,710	39,774,345	17,380,019	-	83,467,074
Depreciation	50,528,052	51,526,111	4,492,017	-	106,546,180
December 31, 2018	76,840,762	91,300,456	21,872,036	-	190,013,254
Net book value, December 31, 2018	167,779,825	282,505,008	9,855,898	458,540	460,599,271

	2017				
	Furniture, fixtures, and equipment	Leasehold rights and improvement	Computer equipment	Leasehold rights and improvements in progress	Total
Cost					
January 1, 2017	21,277,203	46,738,129	18,539,054	-	86,554,386
Additions	48,491,368	153,758,638	159,209	2,814,547	205,223,762
Disposals	(105,604)	-	(48,850)	-	(154,454)
December 31, 2017	69,662,967	200,496,767	18,649,413	2,814,547	291,623,694
Accumulated depreciation					
January 1, 2017	19,699,726	30,442,964	14,442,430	-	64,585,120
Depreciation	6,718,588	9,331,381	2,986,439	-	19,036,408
Disposals	(105,604)		(48,850)	-	(154,454)
December 31, 2017	26,312,710	39,774,345	17,380,019	-	83,467,074
Net book value, December 31, 2017	43,350,257	160,722,422	1,269,394	2,814,547	208,156,620

Depreciation is included in Occupancy and equipment-related expenses in the statement of income.

Bank premises, furniture, fixtures and equipment are all considered non-current assets.

Note 9 - Deferred income tax assets, net

Deferred income tax assets and liabilities at December 31 consist of:

	2018	2017
Deferred income tax assets		
Net operating loss carry over (NOLCO)	-	129,395,042
Allowance for impairment	230,053,121	110,236,789
Expense accruals and provisions	3,745,360	5,021,508
Amortization of past service cost	5,539,913	1,341,884
Fair value loss on investment securities at FVOCI	72,000	-
	239,410,394	245,995,223
Deferred income tax liabilities		
Fair value gain on available-for-sale securities	-	506,000
Retirement benefit asset	1,954,178	3,971,150
	1,954,178	4,477,150
Deferred income tax assets, net	237,456,216	241,518,073

The movement in the net deferred income tax assets are summarized below:

	Note	2018	2017
At January 1		241,518,073	303,666,626
Amounts charged to statement of income		(4,992,461)	(61,330,547)
Amounts credited (charged) to other comprehensive income	14	930,604	(818,006)
At December 31		237,456,216	241,518,073

The deferred tax charge (credit) in the statement of income for the years ended December 31 comprises the following temporary differences:

	2018	2017
Allowance for impairment	(119,816,332)	34,113,943
NOLCO	129,395,042	29,521,674
Others	(4,586,249)	(2,305,070)
	4,992,461	61,330,547

NOLCO utilized for the year ended December 31, 2018 consists of:

Year of Incurrence	Year of Expiration	Amount
2018	2020	61,687,251
2017	2019	181,386,859
2015	2018	188,242,698
		431,316,808
NOLCO utilized during the year		(431,316,808)
		-

Note 10 - Other resources, net

The account as at December 31 consists of:

	Notes	2018	2017
E-money		261,349,884	59,728,672
Tax credits		7,320,626	54,730,554
Rental deposits	19,21	20,775,526	11,281,329
Computer software		20,169,133	30,396,317
Prepaid expenses		15,611,386	3,190,305
Accrued interest receivable		7,295,512	20,042,426
Pension asset	18	6,513,922	13,237,166
Injunction bond		5,029,573	4,668,142
Accounts receivable		4,503,121	4,407,863
Membership shares		2,500,000	2,500,000
Miscellaneous		3,882,578	1,864,173
		354,951,261	206,046,947
Allowance for impairment		(2,459,317)	(1,451,329)
		352,491,944	204,595,618

	2018	2017
Current	34,110,102	79,827,459
Non-current	320,841,159	126,219,488
	354,951,261	206,046,947

E-money represents cash deposited in G-Cash facility, which is used to finance accounts of the Bank's clients accessible through mobile phones, stored value cards and other access devices.

Accounts receivables include employee cash advances, commissions and receivables from ATM cards.

Miscellaneous assets include returned checks and float items which are expected to clear in one to two days.

Allowance for impairment pertains to accounts receivables that are doubtful of collection.

The changes in the allowance for impairment as at December 31 are as follows:

	2018	2017
At January 1	1,451,329	10,661,488
Provision for (reversal of) impairment	1,007,988	(9,210,159)
At December 31	2,459,317	1,451,329

Note 11 - Deposit liabilities

The account as at December 31 consists of:

	2018	2017
Demand	673,700,533	703,190,343
Savings	11,085,518,055	11,278,207,113
Time	801,421,714	856,632,735
	12,560,640,302	12,838,030,191

Related interest expense on deposit liabilities for the year ended December 31 is broken down as follows:

	2018	2017
Demand	2,390,297	2,604,202
Savings	90,951,678	81,350,439
Time	10,280,918	10,134,564
	103,622,893	94,089,205

Under current and existing BSP regulations, the Bank should comply with a simplified minimum reserve requirement. Further, BSP requires all reserves be kept at the central bank. The Bank is in full compliance with the simplified reserve requirement.

The required reserve as reported to BSP as at December 31, 2018 amounts to P991,255,096 (2017 - P993,931,781), which is included in Due from BSP (Note 4).

Deposit liabilities are classified as current.

Note 12 - Accrued taxes, interest and other expenses

The account as at December 31 consists of:

	2018	2017
Accrued expenses	66,751,098	78,307,058
Accrued taxes and licenses	36,000,229	6,120,442
Accrued interest	7,447,214	6,375,482
Accrued income tax	310	60,371
	110,198,851	90,863,353

Accrued expenses mainly pertain to accruals for utilities, penalties and outsourced services by the Bank.

The above accrued expenses are all considered current.

Note 13 - Other liabilities

The account at December 31 consists of:

	2018	2017
Accounts payable	528,142,261	47,251,982
Withholding taxes payable	7,611,306	5,362,576
Miscellaneous	24,368,767	2,537,442
Total	560,122,334	55,152,000

Miscellaneous liabilities include mandatory contributions payable to SSS, Medicare and Philhealth and unclaimed automated manager's checks.

In 2017, the Bank has written off certain long outstanding payables amounting to P15,835,156 (Note 15).

Other liabilities are all considered current.

Note 14 - Capital funds

Details of share capital at December 31 2018 and 2017 are as follows:

	Authorized		Issued and Outstanding	
	Number of Shares	Amount	Number of Shares	Amount
Common shares, at P100 par value per share				
Class A	3,500,000	350,000,000	3,455,721	345,572,100
Class B	600,000	60,000,000	600,000	60,000,000
	4,100,000	410,000,000	4,055,721	405,572,100
Preferred shares, at P100 par value per share, 12% cumulative, participating and redeemable				
Class A	200,000	20,000,000	-	-
Class B	400,000	40,000,000	-	-
	600,000	60,000,000	-	-
	4,700,000	470,000,000	4,055,721	405,572,100

On September 14, 2016, in preparation for the merger, the BOD approved the change in authorized capital structure of the Bank as follows:

- Increase in authorized Class A common shares from P330 million consisting of 3.3 million common shares at P100 par value per share to P350 million consisting of 3.5 million shares at P100 par value per share; and
- Decrease in authorized Preferred Class A common shares from P40 million consisting of 400 thousand shares at P100 par value per share to P20 million consisting of 20 thousand shares at P100 par value per share

The above changes, which were approved by the SEC on December 29, 2016, did not affect the total authorized capital stock of the Bank which remained at P470 million.

The Class A (common and preferred) shares are available only to Philippine nationals while the Class B (common and preferred) shares may be issued to non-Filipinos. The Bank, at its option, may redeem the preferred shares after ten years from issue date.

Surplus

As at December 31, 2018, the Bank has surplus in excess of its paid-up capital amounting to P1,821,189,163 (2017 - P1,564,039,056). The Bank intends to use its excess surplus for future branch expansions which are expected to materialize within the next twelve months after year end.

Other comprehensive income

The movements in the account for the years ended December 31 are summarized below:

	Amount
Fair value reserve on available-for-sale securities	
At January 1, 2017	2,862,698
Unrealized fair value loss before tax	(1,038,390)
Deferred income tax effect	208,000
At December 31, 2017	2,032,308
Effect of adoption of PFRS 9	(12,411)
Reclassified to fair value reserve on investment securities at FVOCI	(2,019,897)
At January 1, 2018	-

	Amount
Fair value reserve on investment securities at FVOCI	
Reclassified from fair value reserve on available-for-sale securities	2,019,897
Unrealized fair value loss before tax	(2,894,970)
Deferred income tax effect	577,999
At December 31, 2018	(297,074)

	2018	2017
Remeasurement loss on defined benefit plan, net		
At January 1	4,078,999	1,684,986
Remeasurement (loss) gain before tax	(1,175,346)	3,420,019
Deferred income tax effect	352,604	(1,026,006)
At December 31	3,256,257	4,078,999

Note 15 - Miscellaneous income

The account for the years ended December 31 consists of:

	Notes	2018	2017
Recoveries		32,201,344	-
Foreign exchange gains		9,686,739	8,565,309
Gain on sale of HTM security	6	-	78,749,152
Write-off of long outstanding payables	13	-	15,835,156
Gain on sale of legacy loans	7	-	11,044,617
Other income		2,240,845	345,439
Gross receipts tax		(3,110,587)	(7,275,337)
		41,018,341	107,264,336

The Bank was able to recover collections on personal loans portfolio acquired from the Parent Bank and the amounts received were recognized as income.

Note 16 - Other operating expenses

The account for the years ended December 31 consists of:

	Note	2018	2017
Shared operating costs	19	212,788,850	40,470,590
Travel and communications		68,602,146	36,527,474
Insurance		47,040,398	48,869,507
Advertising and publicity		22,703,247	16,869,003
Stationery and supplies used		20,540,260	9,399,695
Fines, penalties, and other charges		8,041,093	8,600,945
Litigation expenses		7,287,859	6,216,919
Taxes and licenses		5,990,859	9,864,643
Membership fees		4,118,163	4,025,973
Regulatory examination fees		2,244,893	2,991,043
Others		17,899,678	19,782,531
		417,257,446	203,618,323

Other operating expenses pertain mainly to professional fees, representation and entertainment, freight expenses and other outsourced service costs.

Note 17 - Income taxes

A reconciliation between the provision for income tax at the statutory income tax rate to the actual provision for income tax for the years ended December 31 is presented below:

	2018		2017	
	Amount	%	Amount	%
Statutory income tax	106,935,927	30.00	62,044,344	30.00
Effect of items not subject to statutory tax rate				
Income subject to lower tax rates	(19,735,973)	(5.53)	(27,707,231)	(13.40)
Others	262,751	0.07	87,933,344	42.52
Actual provision for income tax	87,462,705	24.54	122,270,457	59.12

Others mainly consist of permanent non-deductible expenses such as fines, penalties and interest expense above the allowed ceiling.

Note 18 - Retirement plan

BPI and its subsidiaries, which include the Bank, have a trusteed, non-contributory retirement benefit plans covering all qualified officers and employees.

Effective January 1, 2016, the Bank implemented a defined contribution plan which is accounted for as a defined benefit plan with minimum guarantee. The description of the plans follows:

Under the BPI plan, the normal retirement age is 60 years. Normal retirement benefit consists of a lump sum benefit equivalent to 200% of the basic monthly salary of the employee at the time of his retirement for each year of service, if he has rendered at least 10 years of service, or to 150% of his basic monthly salary, if he has rendered less than 10 years of service. For voluntary retirement, the benefit is equivalent to 112.50% of the employee's basic monthly salary for a minimum of 10 years of service with the rate factor progressing to a maximum of 200% of basic monthly salary for service years of 25 or more. Death or disability benefit, on the other hand, shall be determined on the same basis as in voluntary retirement.

For the defined contribution plan, the defined benefit minimum guarantee is equivalent to a certain percentage of the monthly salary payable to an employee at normal retirement age with the required credited years of service based on the provisions of Republic Act (RA) No. 7641. All non-unionized employees hired on or after October 1, 2016 are automatically under the new defined contribution (DC) plan. Employees hired prior to October 1, 2016 shall have the option to elect to become members of the new DC plan.

The net defined benefit cost and contributions to be paid by the Bank are determined by an independent actuary.

Plan assets are held in trusts, governed by local regulations and practice in the Philippines.

Following are the amounts recognized that relate to the Bank based on the recent actuarial valuation reports:

Defined benefit retirement plan

(a) Pension asset as at December 31 recognized in the statement of condition follows:

	2018	2017
Fair value of plan assets	38,953,726	39,715,739
Present value of defined benefit obligation	9,614,795	10,766,182
Surplus	29,338,931	28,949,557
Effect of the asset ceiling	(22,825,009)	(15,712,391)
Pension asset recognized in the statement of condition	6,513,922	13,237,166

Retirement benefit asset is shown as part of Other resources, net (Note 10).

The movement in plan assets is summarized as follows:

	2018	2017
At January 1	39,715,739	37,841,773
Asset return at net interest cost	2,265,545	1,940,623
Contributions	623,114	833,141
Benefits paid	-	(2,728,750)
Remeasurement (gain) loss	(3,650,672)	1,828,952
At December 31	38,953,726	39,715,739

The carrying value of the plan assets as at December 31, 2018 is equivalent to its fair value of P39.0 million (2017 - P39.7 million).

The plan assets at December 31 are comprised of the following:

	2018		2017	
	Amount	%	Amount	%
Debt securities	16,360,565	42	17,077,768	43
Equity securities	17,139,639	44	15,091,981	38
Others	5,453,522	14	7,545,990	19
	38,953,726	100	39,715,739	100

Pension plan assets of the unified retirement plan include investment in BPI's common shares with carrying amount of P251 million (2017 - P222 million) and fair value of P451 million at December 31, 2018 (2017 - P510 million). Realized and unrealized gains coming from BPI's common shares amount to P7 million and P200 million in 2018, respectively (2017 - P10 million and P288 million, respectively). The actual return on plan assets of the Bank was P434 million in 2018 (2017 - P992 million). An officer of the Parent Bank exercises the voting rights over the plan's investment in BPI's common shares.

The movement in the present value of defined benefit obligation is summarized as follows:

	2018	2017
At January 1	10,766,182	24,854,914
Current service cost	647,651	610,638
Interest cost	609,366	1,235,602
Benefits paid	-	(2,728,750)
Remeasurement gain		
Changes in financial assumptions	(4,005,441)	(516,823)
Experience adjustments	1,597,037	(12,689,399)
At December 31	9,614,795	10,766,182

The Bank has no other transactions with the plan other than the contributions and benefit payments for the years ended December 31, 2018 and 2017.

(b) Retirement (benefit) expense recognized in the statement of income for the years ended December 31:

	2018	2017
Current service cost	647,651	610,638
Net interest income	(794,942)	(514,984)
Total	(147,291)	95,654

The principal assumptions used for the actuarial valuations of the defined benefit plan of the Bank are as follows:

	2018	2017
Discount rate	8.37%	5.66%
Salary increase rate	5.00%	5.00%

Discount rate

The discount rate is determined by reference to yields on long-term Philippine Treasury Bonds and adjusted to reflect the term similar to the estimated term of the benefit obligation as determined by the actuary as at the end of the reporting period as there is no deep market in high quality corporate bonds in the Philippines.

Future salary rate increases

This is the expected long-term average rate of salary increase taking into account inflation, seniority, promotion and other market factors. Salary increases comprise of the general inflationary increases plus a further increase for individual productivity, merit and promotion. The future salary increase rates are set by reference over the period over which benefits are expected to be paid.

Demographic assumptions

Assumptions regarding future mortality and disability experience are based on published statistics generally used for local actuarial valuation purposes.

The defined benefit plan typically exposes the Bank to a number of risks such as investment risk, interest rate risk and salary risk. The most significant of which relate to investment and interest rate risk. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability. A decrease in government bond yields will increase the defined benefit obligation although this will also be partially offset by an increase in the value of the plan's fixed income holdings. Hence, the present value of defined benefit obligation is directly affected by the discount rate to be applied by the Bank. However, the Bank believes that due to the long-term nature of the pension liability and the strength of the Bank itself, the mix of debt and equity securities holdings of the plan is an appropriate element of the Bank's long term strategy to manage the plan efficiently.

The Bank ensures that the investment positions are managed within an asset-liability matching framework that has been developed to achieve long-term investments that are in line with the obligations under the plan. The Bank's main objective is to match assets to the defined benefit obligation by investing primarily in long-term debt securities with maturities that match the benefit payments as they fall due. The asset-liability matching is being monitored on a regular basis and potential change in investment mix is being discussed with the trustor, as necessary, to better ensure the appropriate asset-liability matching.

The average remaining service life of employees under the BPI unified retirement plan as at December 31, 2018 is 21 years (2017 - 23 years). The Bank contributes to the plan depending on the suggested funding contribution as calculated by an independent actuary. The expected contribution for the year ending December 31, 2019 for the Bank amounts to P0.6 million.

The weighted average duration of the defined benefit obligation as at December 31, 2018 is 12.3 years (2017 - 11.6 years).

The projected maturity analysis of retirement benefit payments as at December 31 is as follows:

	2018	2017
Between 1 to 5 years	1,056,732	1,902,941
Between 5 to 10 years	10,137,381	2,836,851
Between 10 to 15 years	6,293,538	12,232,401
Between 15 to 20 years	12,197,989	8,556,742
Over 20 years	38,838,543	22,352,863

The sensitivity of the defined benefit obligation to changes in the weighted principal assumptions follows:

		Impact on defined benefit obligation	
December 31, 2018	Change in assumption	Increase in assumption	Decrease in assumption
Discount rate	0.5%	Decrease by 5.9%	Increase by 6.4%
Salary growth rate	1.0%	Increase by 13.6%	Decrease by 11.8%

		Impact on defined benefit obligation	
December 31, 2017	Change in assumption	Increase in assumption	Decrease in assumption
Discount rate	0.5%	Decrease by 5.6%	Increase by 6.1%
Salary growth rate	1.0%	Increase by 11.6%	Decrease by 10.1%

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions, the same method (present value of the defined benefit obligation calculated with the projected unit credit method at the end of the reporting period) has been applied as when calculating the retirement liability recognized within the statement of condition.

Defined contribution retirement plan subject to the requirements of RA No. 7641

	2018	2017
Fair value of plan assets	1,694,050	1,317,686
Present value of defined benefit obligation under RA No. 7641	(18,279,619)	(4,775,597)
Deficit	(16,585,569)	(3,457,911)
Effect of asset ceiling	-	-
Pension liability recognized in the statement of condition	(16,585,569)	(3,457,911)

The movements in the present value of the defined benefit obligation follow:

	2018	2017
At January 1	4,775,597	335,257
Current service cost	19,858,115	3,431,874
Interest cost	296,565	18,875
Transfer to the Plan	-	3,184,969
Remeasurement gain		
Changes in financial assumptions	(7,855,201)	(587,815)
Experience adjustments	1,204,543	(1,607,563)
At December 31	18,279,619	4,775,597

The movements in the fair value of plan assets follow:

	2018	2017
At January 1	1,317,686	993,946
Asset return at net interest cost	85,943	59,202
Contributions	132,531	115,215
Remeasurement loss - return on plan assets	157,890	149,323
At December 31	1,694,050	1,317,686

Total retirement expense for the year ended December 31, 2018 under the defined contribution plan amounts to P20,068,737 (2017 - P3,391,547).

The principal assumptions used for the actuarial valuation of the defined contribution plan of the Bank are as follows:

	2018	2017
Discount rate	9.01%	6.21%
Salary increase rate	5.00%	5.00%

The major categories of plan assets as a percentage of the fair value of total plan assets at December 31 follow:

	2018		2017	
	Amount	%	Amount	%
Debt securities	423,512	25	329,422	25
Equity securities	1,236,657	73	909,203	69
Others	33,881	2	79,061	6
	1,694,050	100	1,317,686	100

The asset allocation of the plan is set and reviewed from time to time by the plan trustees taking into account the membership profile, the liquidity requirements of the plan and risk appetite of the plan sponsor.

Contributions are determined on the plan provisions. The expected contribution of the Bank for the year ending December 31, 2019 amounts to P10,137,181.

Note 19 - Related party transactions

In the ordinary course of business, the Bank has transactions with its directors, officers, stockholders and related interests (DOSRI) and with its Parent Bank such as cash deposit arrangements, purchase of investment securities and outsourcing of certain services, primarily loans operations, branch operations and human resource-related functions.

Significant related party transactions are summarized below:

As at and for the year ended December 31, 2018:

	Transactions for the year	Outstanding balance	Terms and conditions
Deposits to:			
Parent Bank	(98,576,672)	809,779,918	- These are demand, savings and time deposits bearing the following average interest rates: Savings - 0.66% to 1.11% Time - 1.68% to 2.83%
Fellow subsidiary	28,466,832	60,812,932	
	(70,109,840)	870,592,850	
Deposits from:			
Fellow subsidiary	(26,600,000)	1,700,000	- These are time deposits bearing average interest rates of 1.13% to 1.14%.
	(26,600,000)	1,700,000	
Accounts receivable:			
Parent Bank	(12,589)	-	- Unsecured, unguaranteed and non-interest bearing advances - Collectible at gross amount in cash and on demand but not later than 12 months from reporting period
	(12,589)	-	

	Transactions for the year	Outstanding balance	Terms and conditions
Accounts payable:			
Parent Bank	335,231,306	359,046,891	- Shared operating costs, occupancy and equipment related costs and office rental - Unsecured, unguaranteed and non-interest bearing - Payable at gross amount in cash and on demand but not later than 12 months from reporting period - Refer to Notes (a), (b) and (c) below
	335,231,306	359,046,891	

As at and for the year ended December 31, 2017:

	Transactions for the year	Outstanding balance	Terms and conditions
Deposits to:			
Parent Bank	(17,221,791)	908,356,590	- These are demand, savings and time deposits bearing the following average interest rates: Savings - 0.66% to 1.11% Time - 1.68% to 2.83%
Fellow subsidiary	6,503,342	32,346,100	
	(10,718,449)	940,702,690	
Deposits from:			
Fellow subsidiary	50,192,376	28,300,000	- These are time deposits bearing average interest rates of 1.13% to 1.14%.
	50,192,376	28,300,000	
Accounts receivable:			
Parent Bank	12,589	12,589	- Unsecured, unguaranteed and non-interest bearing advances - Collectible at gross amount in cash and on demand but not later than 12 months from reporting period
	12,589	12,589	

	Transactions for the year	Outstanding balance	Terms and conditions
Accounts payable:			
Parent Bank	23,642,392	23,752,245	- Shared operating costs, occupancy and equipment related costs and office rental - Unsecured, unguaranteed and non-interest bearing - Payable at gross amount in cash and on demand but not later than 12 months from reporting period - Refer to Notes (a), (b) and (c) below
	23,642,392	23,752,245	

The aggregate amounts included in the determination of income before income tax that resulted from transactions with each class of related parties are as follows:

	Notes	2018	2017
Interest income	2		
Parent Bank		2,598,898	2,468,493
Fellow subsidiaries		268,066	254,253
		2,866,964	2,722,746
Interest expense			
Fellow subsidiaries		439,437	453,040
Shared operating costs [Refer to Note (a) below]			
Parent Bank	16	212,788,850	40,470,590
Occupancy and equipment related costs [Refer to Note (b) below]			
Parent Bank		69,682,991	75,717,124
Office rental [Refer to Note (c) below]			
Parent Bank		5,556,411	6,190,025
Retirement benefits		1,238,784	295,989
Salaries, allowances and other short-term benefits			
Key management personnel		6,898,645	6,163,527
Directors' remuneration		1,460,000	858,000

(a) Shared operating costs

These pertain to the Parent Bank's outsourcing of services relating to anti-money laundering services, accounting and securities administration services, loan operations, treasury operations, human resource-related functions and information systems. Shared operating costs are billed based on rate and terms agreed by the parties. The agreement remains in force unless terminated by the parties.

(b) Occupancy and equipment related costs

These pertain to the Parent Bank's services relating to shared technology costs. It is billed based on rate and terms agreed by the parties. The agreement remains in force unless terminated by the parties.

(c) Office rental

In 2016, the Bank renewed its office lease agreement with the Parent Bank for the lease of the Bank's office premises in BPI Card Center Building. The lease period is for 3 years, commencing from June 1, 2016 to May 31, 2019 and is subject to extensions and renewals upon mutual agreement. The rent shall be increased by 5% on the second year of the lease period and 7% in the year thereafter. The related lease was terminated in 2017 and security deposit from such lease was refunded.

In 2017, the Bank transferred its office premise at BPI Greentop Condominium building, a property of the Parent Bank, for a lease period of 5 years from December 1, 2014 to November 30, 2019. The rent shall increase by 5% yearly starting on the second year and by 7% on the fourth year thereafter. The security deposit in relation to the lease is presented as part of Other resources, net in the statement of condition.

Details of DOSRI loans at December 31 are as follows:

	2018	2017
Outstanding to DOSRI loans	-	541,568
% to total outstanding loans and advances	-	0.0121%
% to total outstanding DOSRI loans		
Unsecured DOSRI loans	-	-
Past due DOSRI loans	-	-
Non-performing DOSRI loans	-	-

At December 31, 2018 and 2017, the Bank is in full compliance with the General Banking Act and the BSP regulations on DOSRI loans.

Note 20 - Basic quantitative indicators of financial performance

The Bank's key financial performance indicators (in %) at December 31 are summarized below:

	2018	2017
Return on average equity	11.63%	4.17%
Return on average assets	1.79%	0.56%
Net interest margin	12.28%	3.93%

Note 21 - Other commitments and contingent liabilities

As a result of the merger, the existing lease agreements by BanKo was assumed by the Bank effective December 29, 2016. The lease term of the Bank's main office space commenced on December 1, 2014 and will end on November 30, 2019. Likewise, the branch office spaces have various lease agreements that are renewable under certain terms and conditions. The rent is subject to 5% to 10% escalation rate. This agreement requires the Bank to pay security deposit which is presented at Other resources, net in the statement of condition.

As at December 31, the future minimum lease payments under this operating lease are as follows:

	2018	2017
Within one year	80,365,486	41,156,981
After one year but not more than five years	233,096,157	108,968,618
	313,461,643	150,125,599

The Bank has no outstanding contingent liabilities as at December 31, 2018 and 2017.

Note 22 - Critical accounting estimates and judgments

The Bank makes judgments, estimates and assumptions that affect the reported amounts of resources and liabilities. Judgments, estimates and assumptions 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. It is reasonably possible that the outcomes within the next financial year could differ from judgments, estimates and assumptions made at reporting date and could result in the adjustment to the carrying amount of affected assets and liabilities.

22.1 Critical accounting estimates

(i) Measurement of the expected credit loss (ECL) allowance (PFRS 9)

The measurement of the ECL for loans and advances is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behavior (e.g. the likelihood of customers defaulting and the resulting losses).

A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for significant increase in credit risk;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL.

Forward-looking scenarios

Three distinct macroeconomic scenarios (baseline, upside and downside) are considered in the Bank's estimation of ECL in Stage 1 and Stage 2. These scenarios are based on assumptions supported by economic theories and historical experience. The downside scenario reflects a negative macroeconomic event occurring within the first 12 months, with conditions deteriorating for up to two years, followed by a recovery for the remainder of the period. This scenario is grounded in historical experience and assumes a monetary policy response that returns the economy to a long-run, sustainable growth rate within the forecast period. The probability of each scenario is determined using expert judgment and recession probability tools provided by reputable external service providers. The baseline case incorporates the Bank's outlook for the domestic and global economy. The best and worst case scenarios take into account certain adjustments that will lead to a more positive or negative economic outcome.

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political changes is likewise considered, if material.

The most significant period-end assumptions used for the ECL estimate are set out below. The scenarios "base", "upside" and "downside" were used for all portfolios.

At December 31, 2018

	Base Scenario		Upside Scenario		Downside Scenario	
	Next 12 Months	2 to 5 years (Average)	Next 12 Months	2 to 5 years (Average)	Next 12 Months	2 to 5 years (Average)
Real GDP growth (%)	7.0	6.4	7.3	7.3	4.1	(1.2)
Inflation Rate (%)	4.1	3.2	3.5	2.7	6.1	8.8
PDST-R2 5Y (%)	7.0	6.7	6.7	6.4	8.1	10.7
US Treasury 5Y (%)	3.2	2.4	2.7	2.2	6.0	3.7
Exchange Rate	54.638	57.796	53.620	52.812	55.829	66.661

At January 1, 2018

	Base Scenario		Upside Scenario		Downside Scenario	
	Next 12 Months	2 to 5 years (Average)	Next 12 Months	2 to 5 years (Average)	Next 12 Months	2 to 5 years (Average)
Real GDP growth (%)	6.5	6.7	7.7	7.9	2.0	(6.4)
Inflation Rate (%)	2.8	2.6	2.1	2.0	9.6	23.6
PDST-R2 5Y (%)	5.0	6.7	4.9	6.2	18.5	36.2
US Treasury 5Y (%)	2.7	4.3	2.5	3.8	8.1	8.2
Exchange Rate	53.231	53.861	48.831	48.133	65.470	146.286

Sensitivity analysis

The loan portfolios have different sensitivities to movements in macroeconomic variables, so the above three scenarios have varying impact on the ECL of the Bank's portfolios. The allowance for impairment is calculated as the weighted average of ECL under the baseline, upside and downside scenarios. The impact of weighting these multiple scenarios was an increase in the allowance for impairment by P13 million from the baseline scenario as at December 31, 2018.

Transfers between stages

Transfers from Stage 1 and Stage 2 are based on the assessment of significant increase in credit risk ('SICR') from initial recognition. The impact of moving from 12 months ECL to lifetime ECL, or vice versa, varies by product and is dependent on the expected remaining life at the date of the transfer. Stage transfers may result in significant fluctuations in ECL. Assuming all Stage 2 accounts are considered as Stage 1, allowance for impairment would have decreased by P10.6 million as at December 31, 2018.

Impairment of loans and advances under PAS 39

Until December 31, 2017, the Bank reviews its loan portfolios to assess impairment at least on a monthly basis. In determining whether an impairment loss should be recorded in the statement of income, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for resources with credit risk characteristics and an objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. On the basis of existing knowledge, it is reasonably possible that outcomes within the next financial year, which are different from the assumptions used, may amount to a material difference compared to the recorded impairment loss.

It is, however, impracticable to estimate the impact of such difference in outcomes.

(ii) Fair value of financial instruments (Note 23)

The fair values of financial instruments that are not quoted in active markets are determined by using generally accepted valuation techniques. Where valuation techniques (for example, discounted cash flow models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. Inputs used in these models are from observable data and quoted market prices in respect of similar financial instruments.

All models are approved by the Board of Directors before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices. Changes in assumptions about these factors could affect reported fair value of financial instruments.

The Bank considers that it is impracticable to disclose with sufficient reliability the possible effects of sensitivities surrounding the fair value of financial instruments that are not quoted in active markets.

(iii) Pension liability on defined benefit plan (Note 18)

The Bank estimates its pension benefit obligation and expense for defined benefit pension plans based on the selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions are described in Note 18 and include, among others, the discount rate and future salary increases. The Bank determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the retirement obligations.

The present value of the defined benefit obligation of the Bank at December 31, 2018 and 2017 are determined using the market yields on Philippine government bonds with terms consistent with the expected payments of employee benefits. Plan assets are invested in either equity securities, debt securities or other forms of investments. Equity markets may experience volatility, which could affect the value of pension plan assets. This volatility may make it difficult to estimate the long-term rate of return on plan assets. Actual results that differ from the Bank's assumptions are reflected as remeasurements in other comprehensive income. The Bank's assumptions are based on actual historical experience and external data regarding compensation and discount rate trends.
The sensitivity analysis on key assumptions is disclosed in Note 18.

(iv) Valuation of assets held for sale

In determining the fair value of assets held for sale, the Bank analyzed the sales prices by applying appropriate units of comparison, adjusted by differences between the subject asset or property and related market data. Should there be a subsequent write-down of the asset to fair value less cost to sell, such write-down is recognized as impairment loss in the statement of income.

In 2018, the Bank has recognized provision of impairment loss on its foreclosed assets amounting to P757,526 as a result of the decline in fair market values of properties (2017 - provision for impairment loss of P183,724).

The Bank considers that it is impracticable to disclose with sufficient reliability the possible effects of sensitivities surrounding the fair value of assets held for sale.

(v) Useful lives of bank premises, furniture, fixtures and equipment (Note 8)

The Bank determines the estimated useful lives of its bank premises, furniture, fixtures and equipment based on the period over which the assets are expected to be available for use. The Bank annually reviews the estimated useful lives of bank premises, furniture, fixtures and equipment based on factors that include asset utilization, internal technical evaluation, technological changes, environmental and anticipated use of assets tempered by related industry benchmark information. It is possible that future results of operations could be materially affected by changes in these estimates brought about by changes in the factors mentioned.

The Bank considers that it is impracticable to disclose with sufficient reliability the possible effects of sensitivities surrounding the carrying values of bank premises, furniture, fixtures and equipment.

22.2 Critical accounting judgments

(i) Classification of investment securities (Note 5)

The Bank follows the guidance of PFRS 9 starting January 1, 2018 in classifying financial assets at initial recognition whether it will be subsequently measured at fair value through other comprehensive income, at amortized cost, or at fair value through profit or loss. The Bank determines the classification based on the contractual cash flow characteristics of the financial assets and on the business model it uses to manage these financial assets. The Bank determines whether the contractual cash flows associated with the financial asset are solely payments of principal and interest ('SPPI'). If the instrument fails the SPPI test, it will be measured at fair value through profit or loss.

Until December 31, 2017, the Bank followed the guidance of PAS 39 in classifying its financial assets. Key judgment was applied particularly in classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity at amortized cost. In making this judgment, the Bank has assessed its intention and ability to hold such investments to maturity.

The Bank has designated at FVOCI investments in a small portfolio of equity securities of listed private corporations. The Bank chose this presentation alternative because the investments were made for strategic purposes rather than with a view to profit on a subsequent sale, and there are no plans to dispose of these investments in the short or medium term.

(ii) Impairment of available-for-sale securities (Note 5)

Until December 31, 2017, the Bank follows the guidance of PAS 39 to determine when an available-for-sale security is impaired. This determination requires significant judgment. In making this judgment, the Bank evaluates, among other factors, the duration and extent to which the fair value of an investment is less than its cost; and the financial health and near-term business outlook of the issuer, including factors such as industry and sector performance, changes in technology and operational and financing cash flows.

(iii) Classification of assets held for sale

Management follows the principles in PFRS 5 in classifying certain foreclosed assets (consisting of real estate and auto or chattel) as assets held for sale when the carrying amount of the assets will be recovered principally through sale. Management is committed to a plan to sell these foreclosed assets and the assets are actively marketed for sale at a price that is reasonable in relation to their current fair value.

(iv) Realization of deferred income tax assets (Note 9)

Management reviews at each reporting date the carrying amounts of deferred tax assets. The carrying amount of deferred tax assets is reduced to the extent that the related tax assets cannot be utilized due to insufficient taxable profit against which the deferred tax losses will be applied. Management believes that sufficient taxable profit will be generated to allow all or part of the deferred income tax assets to be utilized.

Note 23 - Financial risk and capital management

Risk management in the Bank covers all perceived areas of risk exposure, even as it continuously endeavors to uncover hidden risks. Capital management is understood to be a facet of risk management. The Board of Directors is the Bank's principal risk and capital manager, and the Bank's only strategic risk taker. The Board of Directors provides written policies for overall risk management, as well as written procedures for the management of credit risk, foreign exchange risk, interest rate risk, equity risk, liquidity risk, and contingency risk, among others.

The primary objective of the Bank is the generation of recurring acceptable returns to shareholders' capital. To this end, the Bank's policies, business strategies, and business activities are directed towards the generation of cash flows that are in excess of its fiduciary and contractual obligations to its depositors, and to its various other funders and stakeholders.

To generate acceptable returns to its shareholders' capital, the Bank understands that it has to bear risk, that risk-taking is inherent in its business. Risk is understood by the Bank as the uncertainty in its future income - an uncertainty that emanates from the possibility of incurring losses that are due to unplanned and unexpected drops in revenues, increases in expenses, impairment of asset values, or increases in liabilities.

The possibility of incurring losses is, however, compensated by the possibility of earning more than expected income. Risk-taking is, therefore, not entirely a bad step to be avoided. Risk-taking presents opportunities if risks are accounted, deliberately taken, and are kept within rationalized limits.

The most important financial risks that the Bank manages are credit risk, liquidity risk and market risk.

23.1 Credit risk

The Bank takes on exposure to credit risk, which is the risk that may arise if a borrower or counterparty fails to meet its obligations in accordance with agreed terms. Credit risk is the single largest risk for the Bank's business; management therefore carefully manages its exposure to credit risk as governed by relevant regulatory requirements and international benchmarks.

Credit risk may also arise due to substantial exposures to a particular counterparty which the Bank manages by adopting proper risk controls and diversification strategies to prevent undue risk concentrations from excessive exposures to particular counterparties, industries, countries or regions.

The most evident source of credit risk is loans and advances; however, other sources of credit risk exist throughout the activities of the Bank, including in credit-related activities recorded in the banking, investment securities in the trading books and off-balance sheet transactions.

23.1.1 Credit risk management

The Credit Policy and Risk Management division of the Parent Bank supports the Credit Committees in coordination with various business lending and operations units in managing credit risk, and reports are regularly provided to the Bank's Senior Management and the Board of Directors. A rigorous control framework is applied in the determination of ECL models. The Parent Bank has policies and procedures that govern the calculation of ECL and such policies are consistently being observed by the Bank. All ECL models are regularly reviewed by the Risk Management Office to ensure that necessary controls are in place and the models are applied accordingly.

The review and validation are performed by groups that are independent of the team that prepares the calculations, e.g., Risk Models Validation and Internal Auditors. Expert judgements on measurement methodologies and assumptions are reviewed by a group of internal experts from various functions.

The Bank employs a range of policies and practices to mitigate credit risk. The Bank monitors its portfolio based on different segmentation to reflect the acceptable level of diversification and concentration. Credit concentration arises from substantial exposures to particular counterparties. Concentration risk in credit portfolios is inherent in banking and cannot be totally eliminated. However, said risk may be reduced by adopting proper risk control and diversification strategies to prevent undue risk concentrations from excessive exposures to particular counterparties, industries, countries or regions.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a regular basis and subjected to annual or more frequent review, when deemed necessary. Limits on large exposures and credit concentration are approved by the BOD through the RMC.

The exposure to any one borrower is further restricted by sub-limits covering on- and off-balance sheet exposures. Actual exposures against limits are monitored regularly.

Settlement risk arises in any situation where a payment in cash, securities, foreign exchange currencies, or equities is made in the expectation of a corresponding receipt in cash, securities, foreign exchange currencies, or equities. Daily settlement limits are established for each counterparty to cover the aggregate of all settlement risk arising from the Bank's market transactions on any single day. For certain securities, the introduction of the delivery versus payment facility in the local market has brought down settlement risk significantly.

The Bank employs a range of policies and practices to mitigate credit risk. Some of these specific control and risk mitigation measures include collateral or guarantees.

Collateral or guarantees

One of the most traditional and common practice in mitigating credit risk is requiring security particularly for loans and advances. The Bank implements guidelines on the acceptability of specific classes of collateral for credit risk mitigation. The Bank assesses the valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically. The common collateral types for loans and advances are:

- Mortgages over physical properties (e.g., real estate and personal) and
- Mortgages over financial assets (e.g., guarantees)

In order to minimize credit loss, the Bank seeks additional collateral from the counterparty when impairment indicators are observed for the relevant individual loans and advances.

The Bank's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collaterals held by the Bank since the prior period.

23.1.2 Credit risk rating

The Bank uses internal credit risk gradings that reflect its assessment of the probability of default of individual counterparties. The Bank uses internal rating models tailored to the various categories of counterparty. Borrower and loan specific information collected at the time of application (such as disposable income, and level of collateral for retail exposures; and turnover and industry type for wholesale exposures) is fed into this rating model. In addition, the models enable expert judgement from the Credit Review Officer to be fed into the final internal credit rating for each exposure. This allows for considerations which may not be captured as part of the other data inputs into the model.

The Bank has put in place a credit classification system to promptly identify deteriorating exposures and to determine the appropriate credit losses. Classification is being done on the basis of Bank's existing internal credit risk rating system, credit models or determined using reputable external rating agencies. The following are the considerations observed by the Bank in classifying its exposures:

- *Standard monitoring* refers to accounts which do not have a greater-than-normal risk and do not possess the characteristics of special monitoring and defaulted loans. The counterparty has the ability to satisfy the obligation in full and therefore minimal loss, if any, is anticipated.

- *Special monitoring* are accounts which need closer and frequent monitoring to prevent any further deterioration of the credit. The counterparty is assessed to be vulnerable to highly vulnerable and its capacity to meet its financial obligations is dependent upon favorable business, financial, and economic conditions.

- *Default* refers to accounts which exhibit probable to severe weaknesses wherein possibility of non-repayment of loan obligation is ranging from high to extremely high severity.

The mapping of internal credit risk ratings with the Bank's standard account classification is shown below:

(a) Loans and advances

The Bank's internal credit risk rating system comprises a 30-scale rating with eighteen (18) 'pass' rating levels for large corporate accounts; 14-scale rating system with ten (10) 'pass' rating grades for SME; and 26-scale rating system with thirteen (13) pass ratings for cross-border accounts mapped based on reputable external rating agency.

The Bank uses automated scoring models to assess the level of risk for retail accounts. Behavioral indicators are considered in conjunction with other forward-looking information (e.g., industry forecast) to assess the level of risk of a financial asset. After the date of initial recognition, the payment behavior of the borrower is monitored on a periodic basis to develop a behavioral score which is mapped to a PD.

Classifications	PL, Auto, Housing	SEME
Standard monitoring	Current to 30 dpd	Current to 7 dpd
Special monitoring	31-90 dpd	-
Default	>90, IL, Loss	8 dpd and up

(b) Treasury and debt securities

Investments in high grade securities and bills are viewed as a way to gain better credit quality mix and at the same time, maintain a readily available source to meet funding requirements. The level of credit risk for treasury and other investment debt securities and their associated probability of default (PD) are determined using reputable external ratings and/or available and reliable qualitative and quantitative information. In the absence of credit ratings, a comparable issuer or guarantor rating is used. Should there be a change in the credit rating of the chosen comparable, evaluation is made to ascertain whether the rating change is applicable to the security being assessed for impairment.

Classifications	Credit Risk Grade following S&P or its equivalent
Standard monitoring	Investment Grade (AAA to BBB-)
Special monitoring	Non-IG (BB+ to C)
Default	Default (D)

(b) Other financial assets

For other financial assets (accounts receivable and rental deposits), the Bank applies the simplified approach, as permitted by PFRS 9, in measuring ECL which uses a lifetime ECL methodology. These financial assets are grouped based on shared risk characteristics and aging profile. For some of these, impairment is assessed individually at a counterparty level.

23.1.3 Maximum exposure to credit risk

The following tables contain an analysis of the credit risk exposure of each financial instrument for which an ECL allowance is recognized. The gross carrying amount of financial assets below also represents the Bank's maximum exposure to credit risk on these assets.

Credit quality of loans and advances, net

	2018				2017
	ECL Staging				
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total	Total
Credit grade					
Standard monitoring	8,782,243,783	286,747,363	-	9,068,991,146	4,084,408,547
Special monitoring	14,559,458	201,489,316	-	216,048,774	158,173,187
Default	-	-	630,521,230	630,521,230	255,860,872
Gross carrying amount	8,796,803,241	488,236,679	630,521,230	9,915,561,150	4,498,442,606
Loss allowance	(328,566,682)	(22,433,268)	(319,366,513)	(670,366,463)	(202,242,606)
Carrying amount	8,468,236,559	465,803,411	311,154,717	9,245,194,687	4,296,200,000

Treasury and other investment securities

Credit risk exposures relating to treasury and other investment securities are as follows:

	2018	2017
Due from other banks	884,795,667	967,092,652
Interbank loans receivable	300,158,333	165,255,798
Due from BSP	3,853,846,029	8,793,748,200
Financial assets at FVOCI	100,065,545	-
AFS securities	-	102,960,515
	5,138,865,574	10,029,057,165

Credit quality of other financial assets

	2018				2017
	ECL Staging				
	Stage 1 12-month ECL	**Stage 2** Lifetime ECL	**Stage 3** Lifetime ECL	**Total**	**Total**
Credit grade					
Standard monitoring					
Due from other banks	884,795,667	-	-	884,795,667	967,092,652
Interbank loans receivable	300,158,333	-	-	300,158,333	165,255,798
Due from BSP	3,853,846,029	-	-	3,853,846,029	8,793,748,200
Financial assets at FVOCI	100,065,545	-	-	100,065,545	-
Available-for-sale securities	-	-	-	-	102,960,515
Default					
Available-for-sale securities	-	-	-	-	12,412
Gross carrying amount	5,138,865,574	-	-	5,138,865,574	10,029,069,577
Loss allowance	-	-	-	-	(12,412)
Carrying amount	5,138,865,574	-	-	5,138,865,574	10,029,057,165

The Bank's other financial assets generally arise from transactions with various unrated counterparties with good credit standing. The Bank applies the simplified approach, as permitted by PFRS 9, in measuring ECL which uses a lifetime expected loss methodology for other financial assets.

To measure the ECL, other financial assets have been grouped based on shared credit risk characteristics and the days past due. The expected loss rates are based on the payment profiles of receivables over a period of 36 months before January 1, 2018 or December 31, 2018, respectively, and corresponding historical credit losses experienced within these periods. The impact of forward-looking variables on macroeconomic factors is considered insignificant in calculating ECL provisions for other financial assets

23.1.4 Credit impaired loans and advances

The Bank closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Bank will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

	2018 (PFRS 9)			2017 (PAS 39)
	Gross exposure	Impairment allowance	Carrying amount	Gross exposure
Credit-impaired assets				
Corporate entities	50,000,000	50,000,000	-	50,000,000
Retail customers	580,521,230	163,040,718	417,480,512	486,816,695
Total credit-impaired assets	630,521,230	213,040,718	417,480,512	536,816,695
Fair value of collateral	292,118,361	-	233,694,689	613,504,794

As at December 31, 2018, the Bank acquired assets by taking possession of collaterals held as security for loans and advances with carrying amount of P15,046,077 (2017 - P30,692,202). The related foreclosed collaterals at December 31, 2018 have aggregate fair value of P22,798,200 (2017 - P49,489,537).

As at December 31, 2018, the allowance for impairment of foreclosed collateral amounts to P4,539,247 (2017 - P4,003,079). Foreclosed collaterals include real estate (land, building, and improvements) and chattel.

Repossessed properties are sold as soon as practicable and are classified as assets held for sale in the statement of condition.

23.1.5 Loss allowance

The loss allowance recognized in the period is affected by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments de-recognized in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period;
- Impact on the measurement of ECL due to changes made to models and assumptions;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognized during the period and write-offs of allowances related to assets that were written off during the period.

The following table summarizes the changes in the loss allowance for loans and advances between the beginning and the end of the annual period:

	Stage 1	Stage 2	Stage 3	
	12-month ECL	Lifetime ECL	Lifetime ECL	Total
Loss allowance, beginning	96,711,892	21,063,603	96,314,383	214,089,878
Movements with P&L impact				
Transfers:				
Transfer in (out of) Stage 1	(51,235,682)	12,576,285	150,840,253	112,180,856
Transfer in (out of) Stage 2	214,655	(9,232,055)	15,171,672	6,154,272
Transfer in (out of) Stage 3	5,087,301	1,283,450	(31,914,265)	(25,543,514)
New financial assets originated	341,471,969	-	-	341,471,969
Financial assets derecognized during the year	(30,604,120)	(3,694,852)	(29,281,961)	(63,580,933)
Changes in PDs/EADs/LGDs and models assumptions	(33,129,447)	(5,448,544)	68,946,807	30,368,816
Write-offs	-	-	(146,928,273)	(146,928,273)
Other movements	50,115	5,885,381	196,217,895	202,153,391
Loss allowance, ending	328,566,683	22,433,268	319,366,511	670,366,462

No movement analysis of allowance for impairment for other financial assets subject to impairment as the related loss allowance is deemed insignificant for financial reporting purposes.

Write-off policy

The Bank writes off financial assets when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) where the Bank's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full.

The Bank may write-off financial assets that are still subject to enforcement activity. The write-off of loans is approved by the BOD in compliance with the BSP requirements. Loans written-off in 2018 are fully covered with allowance.

23.1.6 Concentration of financial assets with credit exposure

The Bank's main credit exposures based on carrying amounts and categorized by industry sectors are summarized below:

	Financial Institutions	Manufacturing	Business Services and Real Estate	Private Households	Others	Less - Allowance	Total
At December 31, 2018							
Due from other banks	884,795,667	-	-	-	-	-	884,795,667
Interbank loans	-	-	-	-	300,158,333	-	300,158,333
Due from BSP	-	-	-	-	3,853,846,029	-	3,853,846,029
Investment securities at FVOCI	-	-	100,065,545	-	-	-	100,065,545
Loans and advances, net	35,239,112	1,872,022	373,049,925	8,373,895,855	1,131,504,236	(670,366,462)	9,245,194,688
Other resources, net	-	-	-	-	293,924,043	(2,459,317)	291,464,726
	920,034,779	1,872,022	473,115,470	8,373,895,855	5,579,432,641	(672,825,779)	14,675,524,988
At December 31, 2017							
Due from other banks	967,092,652	-	-	-	-	-	967,092,652
Interbank loans	-	-	-	-	165,255,798	-	165,255,798
Due from BSP	-	-	-	-	8,793,748,200	-	8,793,748,200
Available-for-sale	-	-	102,960,515	-	-	-	102,960,515
Held-to-maturity	-	-	-	-	-	-	-
Loans and advances, net	39,995,679	7,347,008	479,108,601	3,458,656,088	513,335,230	(202,242,606)	4,296,200,000
Other resources, net	-	-	-	-	95,460,290	(1,451,329)	94,008,961
	1,007,088,331	7,347,008	582,069,116	3,458,656,088	9,567,799,518	(203,693,935)	14,419,266,126

23.2 Market risk

The Bank is exposed to market risk - the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk is managed by the Risk Management Office (RMO) and confirmed by the Board of Directors.

Market risk management

Market risk management is incumbent on the Board of Directors through its Risk Management Committee (RMC). Market risk management in the Bank covers managing exposures to trading risk, foreign exchange risk, counterparty credit risk, interest rate risk of the banking book and liquidity risk. At the management level, the Bank's market risk exposure is managed RMO, headed by the Bank's Chief Risk Officer (CRO) who reports directly to the RMC. In addition, Internal Audit is responsible for the independent review of risk assessment measures and procedures and the control environment.

The Bank reviews and controls market risk exposures of both its trading and non-trading portfolios. Trading portfolios include those positions arising from the Bank's market-making transactions.

Non-trading portfolios primarily arise from the interest rate management of the Bank's retail and commercial banking assets and liabilities.

Value-at-Risk (VaR) measurement is an integral part of the Bank's market risk control system. This metric estimates, at 99% confidence level, the maximum loss that a trading portfolio may incur over a trading day. This metric indicates as well that there is 1% statistical probability that the trading portfolios' actual loss would be greater than the computed VaR. In order to ensure model soundness, the VaR is periodically subject to model validation and back testing. VaR is supplemented by other risk metrics and measurements that would provide preliminary signals to Treasury and to the management to assess the vulnerability of Bank's positions. To control the risk, the RMC sets risk limits for trading portfolios which are consistent with the Bank's goals, objectives, risk appetite, and strategy.

Stress tests indicate the potential losses that could arise in extreme conditions that would have detrimental effect to the Bank's positions. The Bank periodically performs stress testing (price risk and liquidity risk) to assess the Bank's condition on assumed stress scenarios. Contingency plans are frequently reviewed to ensure the Bank's preparedness in the event of real stress. Results of stress tests are reviewed by senior management and by the RMC.

The average daily VaR for the trading portfolios at December 31 follows:

	2018	2017
Local fixed-income	-	-
Foreign exchange	89	57

23.3 Interest rate risk

There are two types of interest rate risk - (i) fair value interest rate risk and (ii) cash flow interest rate risk. Fair value interest rate risk is the risk that the fair value of a financial instrument will fluctuate because of changes in market interest rates. Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may also result in losses in the event that unexpected movements arise.

The Board of Directors sets limits on the level of mismatch of interest rate repricing that may be undertaken, which is monitored daily by the RMO.

Interest rate risk in the banking book arises from the Bank's core banking activities. The main source of this type of interest rate risk is repricing risk, which reflects the fact that the Bank's assets and liabilities are of different maturities and are priced at different interest rates.

	Up to 1 year	Over 1 year and up to 3 years	Over 3 years	Non-repricing	Total
As at December 31, 2018					
Assets					
Cash and other cash items	-	-	-	86,383,976	86,383,976
Due from other banks	-	-	-	884,795,667	884,795,667
Interbank loans	-	-	-	300,158,333	300,158,333
Due from BSP	-	-	-	3,853,846,029	3,853,846,029
Financial assets at FVOCI	-	-	-	100,065,545	100,065,545
Loans and advances	5,448,712,642	3,577,582,194	121,284,774	97,615,078	9,245,194,688
Other resources	-	-	-	293,924,043	293,924,043
Total financial assets	5,448,712,642	3,577,582,194	121,284,774	5,616,788,671	14,764,368,281
Liabilities					
Deposit liabilities	12,560,640,302	-	-	-	12,560,640,302
Accrued interest	-	-	-	7,447,214	7,447,214
Accounts payable	-	-	-	531,245,917	531,245,917
Total financial liabilities	12,560,640,302	-	-	538,693,131	13,099,333,433
Total interest gap	(7,111,927,660)	3,577,582,194	121,284,774	5,078,095,540	1,665,034,848

	Up to 1 year	Over 1 year and up to 3 years	Over 3 years	Non-repricing	Total
As at December 31, 2017					
Assets					
Cash and other cash items	-	-	-	26,310,761	26,310,761
Due from other banks	-	-	-	967,092,652	967,092,652
Interbank loans	-	-	-	165,255,798	165,255,798
Due from BSP	-	-	-	8,793,748,200	8,793,748,200
Available-for-sale	-	-	-	102,960,515	102,960,515
Loans and advances	8,447,795	353,757,929	3,713,681,420	422,555,462	4,498,442,606
Other resources	-	-	-	95,460,290	95,460,290
Total financial assets	8,447,795	353,757,929	3,713,681,420	10,573,383,678	14,649,270,822
Liabilities					
Deposit liabilities	12,838,030,189	-	-	-	12,838,030,189
Accrued interest	-	-	-	6,375,482	6,375,482
Accounts payable	-	-	-	47,251,982	47,251,982
Total financial liabilities	12,838,030,189	-	-	53,627,464	12,891,657,653
Total interest gap	(12,829,582,394)	353,757,929	3,713,681,420	10,519,756,214	1,757,613,169

The Bank uses a simple version of the Balance Sheet VaR (BSVaR) whereby only the principal and interest payments due and relating to the banking book as at particular valuation dates are considered. The BSVaR assumes a static balance sheet, i.e., it is assumed that there will be no new transactions moving forward, and no portfolio rebalancing will be undertaken in response to future changes in market rates.

The BSVaR is founded on re-pricing gaps, or the difference between the amounts of rate sensitive assets and the amounts of rate sensitive liabilities. An asset or liability is considered to be rate-sensitive if the interest rate applied to the outstanding principal balance changes (either contractually or because of a change in a reference rate) during the interval.

The BSVaR estimates the "riskiness of the balance sheet" and compares the degree of risk taking activity in the banking books from one period to the next. In consideration of the static framework, and the fact that income from the positions is accrued rather than generated from marking-to-market, the probable loss (that may be exceeded 1% of the time) that is indicated by the BSVaR is not realized in accounting income.

The cumulative BSVaR for the banking or non-trading book in 2018 and 2017 amount to P114,190,000 and P171,000,000 , respectively.

23.4 Foreign exchange risk

Foreign exchange risk is the risk that the fair value or future cash flows of financial instrument will fluctuate because of changes in foreign exchange rates. It arises on financial instruments that are denominated in a foreign currency other than the functional currency which they are measured.

The Bank takes on exposure to the effects of fluctuations in the prevailing exchange rates on its foreign currency financial position and cash flows. The table below summarizes the Bank's exposure to foreign currency exchange rate risk relative to its financial assets and liabilities denominated in United States Dollar (US Dollar) at December 31.

	2018	2017
Financial assets		
Due from other banks	339,118,419	436,445,261
Other resources	186,210	154,030
	339,384,629	436,599,291
Financial liabilities		
Deposit liabilities	324,942,353	426,793,847
Accrued interest	50,887	31,882
	324,993,240	426,825,729
Net foreign exchange exposure	14,311,389	9,773,562

At December 31, 2018, if the Philippine Peso had weakened/strengthened by 12.46% (2017 - 21.17%) against the US Dollar based on historical information in the last five years with all other variables held constant, net income as at and for the year ended December 31, 2018 would have been P1,783,199 (2017 - P2,069,063) higher/lower, mainly as a result of foreign exchange gains/losses on translation of US Dollar-denominated deposits with other banks and deposit liabilities.

23.5 Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

The Bank's liquidity profile is observed and monitored through its metric, the Minimum Cumulative Liquidity Gap (MCLG). The MCLG is the smallest net cumulative cash inflow (if positive) or the largest net cumulative cash outflow (if negative) over the next three (3) months. The MCLG indicates the biggest funding requirement in the short term and the degree of liquidity risk present in the current cash flow profile of the Bank. The MCLG is computed monthly and reported in the RMC meetings. A red flag is immediately raised and reported to management and the RMC when the MCLG level projected over the next 3 months breaches the RMC prescribed MCLG limit.

23.5.1 Liquidity risk management process

The Bank's liquidity management process, as carried out within the Bank and monitored by the RMC and the Risk Management Office includes:

- day-to-day funding, which includes replenishment of funds as they mature or are borrowed by customers, managed by monitoring future cash flows to ensure that requirements can be met;
- maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- monitoring balance sheet liquidity ratios against internal and regulatory requirements;
- managing the concentration and profile of debt maturities; and
- performing periodic liquidity stress testing on the Bank's liquidity position by assuming a faster rate of withdrawals in its deposit base.

Monitoring and reporting take the form of cash flow measurement and projections for the next day, week and month as these are key periods for liquidity management. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

The Bank also monitors unmatched medium-term assets, the level and type of undrawn lending commitments, the usage of overdraft facilities and the impact of contingent liabilities (if any).

23.5.2 Funding approach

Sources of liquidity are regularly reviewed by the Bank to maintain a wide diversification by currency, geography, counterparty, product and term.

23.5.3 Non-derivative cash flows

The table below presents the maturity profile of non-derivative financial instruments based on undiscounted cash flows, including interest, which the Bank uses to manage the inherent liquidity risk. The analysis takes into account the maturity grouping based on the remaining period from the end of the reporting period to the contractual maturity date or, if earlier, the expected date the financial asset will be realized or the financial liability will be settled.

	Up to 1 year	Over 1 up to 3 years	Over 3 years	Total
As at December 31, 2018				
Financial assets				
Cash and other cash items	86,383,976	-	-	86,383,976
Due from other banks	884,795,667	-	-	884,795,667
Interbank loans	300,158,333	-	-	300,158,333
Due from BSP	3,853,846,029	-	-	3,853,846,029
Investment securities at FVOCI	106,756,752	-	-	106,756,752
Loans and advances	5,546,327,720	3,577,582,194	121,284,774	9,245,194,688
Other resources	293,924,043	-	-	293,924,043
Total financial assets	11,072,192,520	3,577,582,194	121,284,774	14,771,059,488
Financial liabilities				
Deposit liabilities	12,566,494,800	-	-	12,566,494,800
Accrued interest and other expense	7,447,214	-	-	7,447,214
Other liabilities	531,245,917	-	-	531,245,917
Total financial liabilities	13,105,187,931	-	-	13,105,187,931
Total maturity gap	(2,032,995,411)	3,577,582,194	121,284,774	1,665,871,557

	Up to 1 year	Over 1 up to 3 years	Over 3 years	Total
As at December 31, 2017				
Financial assets				
Cash and other cash items	26,310,761	-	-	26,310,761
Due from other banks	967,092,652	-	-	967,092,653
Interbank loans	165,255,798	-	-	165,255,798
Due from BSP	8,793,748,200	-	-	8,793,748,200
Available-for-sale securities	6,273,000	106,273,000	-	112,546,000
Loans and advances	1,159,256,485	1,198,233,168	2,049,309,183	4,406,798,836
Other resources	95,460,290	-	-	95,460,290
Total financial assets	11,213,397,187	1,304,506,168	2,049,309,183	14,567,212,538
Financial liabilities				
Deposit liabilities	14,585,560,299	-	-	14,585,560,299
Accrued interest and other expense	6,375,482	-	-	6,375,482
Other liabilities	47,251,982	-	-	47,251,982
Total financial liabilities	14,639,187,763	-	-	14,639,187,763
Total maturity gap	(3,425,790,576)	1,304,506,168	2,049,309,183	(71,975,225)

The maturity gap is being managed through the minimum cumulative liquidity gap.

23.6 Fair values of financial assets and liabilities

The table below summarizes the carrying amounts and fair values of those financial assets and liabilities at December 31 not presented in the statement of condition at fair value.

	Carrying Value		Fair Value	
	2018	2017	2018	2017
Financial assets				
Cash and other cash items	86,383,976	26,310,761	86,383,976	26,310,761
Due from other banks	884,795,667	967,092,652	884,795,667	967,092,652
Interbank loans receivable	300,158,333	165,255,798	300,158,333	165,255,798
Due from BSP	3,853,846,029	8,793,748,200	3,853,846,029	8,793,748,200
Loans and advances, net	9,245,194,688	4,296,200,000	9,245,194,688	4,909,942,857
Other resources, net	293,924,043	95,460,290	293,924,043	95,460,290
Financial liabilities				
Deposit liabilities	12,560,640,302	12,838,030,191	12,560,640,302	12,838,030,191
Accrued interest and other expenses	7,447,214	6,375,482	7,447,214	6,375,482
Other liabilities	531,245,917	47,251,982	531,245,917	47,251,982

Cash and other cash items, due from BSP and other banks and interbank loans receivable

The fair value of floating rate placements and overnight deposits approximates their carrying amounts. The estimated fair value of fixed interest-bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and remaining maturity. All of these financial assets have a maturity of one year, thus their fair values approximate their carrying amounts.

Loans and advances

The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted with the use of assumptions regarding appropriate credit spread for the loan, derived from other market instruments.

Financial liabilities

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand.

The estimated fair value of fixed interest-bearing deposits is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

Other resources and other liabilities

Carrying amounts of other resources and other liabilities which have no definite repayment dates are assumed to be their fair values.

23.6.1 Fair value hierarchy

The following table presents the fair value hierarchy of the Bank's financial assets and liabilities at December 31:

2018	Fair value Level 1	Level 2	Total
Recurring measurements			
Financial assets at FVOCI			
Debt security	-	99,640,000	99,640,000
Equity security	7,338	-	7,338
	7,338	99,640,000	99,647,338

Non-recurring measurements			
Assets held for sale, net	-	128,669,155	128,669,155

2018	Fair value Level 1	Level 2	Total
Financial assets			
Cash and other cash items	-	86,383,976	86,383,976
Due from other banks	-	884,795,667	884,795,667
Interbank loans receivable	-	300,158,333	300,158,333
Due from BSP	-	3,853,846,029	3,853,846,029
Loans and advances, net	-	9,245,194,688	9,245,194,688
Other resources, net	-	93,000,973	93,000,973
Financial liabilities	-		
Deposit liabilities	-	12,560,640,302	12,560,640,302
Accrued interest and other expenses	-	7,447,214	7,447,214
Other liabilities	-	531,245,917	531,245,917

2017	Fair value Level 1	Level 2	Total
Recurring measurements			
Available-for-sale financial assets			
Debt security	-	102,530,000	102,530,000
Equity security	24,720	-	24,720
	24,720	102,530,000	102,554,720

Non-recurring measurements			
Assets held for sale, net	-	140,928,679	140,928,679

2017	Fair value Level 1	Level 2	Total
Financial assets			
Cash and other cash items	-	26,310,761	26,310,761
Due from other banks	-	967,092,652	967,092,652
Interbank loans receivable	-	165,255,798	165,255,798
Due from BSP	-	8,793,784,200	8,793,784,200
Loans and advances, net	-	4,909,942,857	4,909,942,857
Other resources, net	-	95,460,290	95,460,290
Financial liabilities	-		
Deposit liabilities	-	12,838,030,189	12,838,030,189
Accrued interest and other expenses	-	6,375,482	6,375,482
Other liabilities	-	47,251,982	47,251,982

There are no transfers between the fair value hierarchy above for the years ended December 31, 2018 and 2017.

23.7 Capital management

Capital management is understood to be a facet of risk management. The primary objective of the Bank is the generation of recurring acceptable returns to shareholders' capital. To this end, the Bank's policies, business strategies and activities are directed towards the generation of cash flows that are in excess of its fiduciary and contractual obligations to its depositors, and to its various funders and stakeholders.

Cognizant of its exposure to risks, the Bank understands that it must maintain sufficient capital to absorb unexpected losses, to stay in business for the long haul, and to satisfy regulatory requirements. The Bank further understands that its performance, as well as the performance of its various units, should be measured in terms of returns generated vis-à-vis allocated capital and the amount of risk borne in the conduct of business.

Effective January 1, 2014, the BSP, through its Circular 781, requires each bank and its financial affiliated subsidiaries to adopt new capital requirements in accordance with the provisions of Basel III. The new guidelines are meant to strengthen the composition of a bank's capital by increasing the level of core capital and regulatory capital. The Circular sets out minimum Common Equity Tier 1 (CET1) ratio and Tier 1 Capital ratios of 6% and 7.5%, respectively. A capital conservation buffer of 2.5%, comprised of CET1 capital, was likewise imposed. The minimum required capital adequacy ratio remains at 10% which includes the capital conservation buffer.

The table below summarizes the CAR under the Basel III framework for the years ended December 31:

	2018	2017
Tier 1 capital	2,368,682,739	2,047,202,631
Tier 2 capital	93,316,281	39,560,975
Gross qualifying capital	2,461,999,020	2,086,763,606
Less: Required deductions	264,091,514	307,424,076
Total qualifying capital	2,197,907,506	1,779,339,530
Risk weighted assets	10,528,451,664	5,249,351,544
CET1	19.99%	33.14%
CAR (%)	20.88%	33.90%

The Bank has fully complied with the CAR requirement of the BSP.

Note 24 - Summary of significant accounting policies

The principal accounting policies applied in the preparation of the Bank's financial statements are set out below. These policies have been consistently applied to both years presented, unless otherwise stated.

24.1 Basis of preparation

The financial statements of the Bank have been prepared in accordance with Philippine Financial Reporting Standards (PFRSs). The term PFRSs in general includes all applicable PFRSs, Philippine Accounting Standards (PAS), and interpretations of the Philippine Interpretations Committee (PIC), Standing Interpretations Committee (SIC) and International Financial Reporting Interpretations Committee (IFRIC) which have been approved by the Financial Reporting Standards Council (FRSC) and adopted by the SEC.

The financial statements comprise the statement of condition, statement of income and statement of comprehensive income shown as two statements, statement of changes in capital funds, the statement of cash flows and the notes.

These financial statements of the Bank have been prepared under the historical cost convention, as modified by the revaluation of investment securities at FVOCI (AFS securities in 2017), and plan assets of the Bank's retirement plans.

The preparation of these financial statements in conformity with PFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Bank's accounting policies. Changes in assumptions may have a significant impact on the financial statements in the period the assumptions changed. Management believes that the underlying assumptions are appropriate and that the financial statements therefore fairly present the financial position and results of the Bank. The areas involving higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 22.

24.1.1 Changes in accounting policy and disclosures

(a) New and amended standards adopted by the Bank

The Bank has adopted the following standards effective January 1, 2018:

- *PFRS 15, 'Revenue from contracts with customers'* replaces PAS 18, *'Revenue'* which covers contracts for goods and services and PAS 11, *'Construction contracts'* which covers construction contracts. The new standard is based on the principle that revenue is recognized when control of a good or service transfers to a customer - so the notion of control replaces the existing notion of risks and rewards.

  A new five-step process must be applied before revenue can be recognized: (1) identify contracts with customers, (2) identify the separate performance obligation, (3) determine the transaction price of the contract, (4) allocate the transaction price to each of the separate performance obligations, and (5) recognize the revenue as each performance obligation is satisfied.

  The adoption of PFRS 15 did not have a material impact on the Bank's financial statements.

- *PFRS 9, 'Financial instruments'* replaces the provisions of PAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting.

  The adoption of PFRS 9 resulted in changes in accounting policies and adjustments to the amounts previously recognized in the financial statements. The Bank did not early adopt any provisions of PFRS 9 in previous periods.

  As permitted by the transitional provisions of PFRS 9, the Bank elected not to restate comparative figures. Resulting adjustments to the carrying amounts of financial assets and liabilities at the date of transition were recognized in the opening balance of Surplus as at January 1, 2018.

  The adoption of PFRS 9 has resulted in changes mainly in the Bank's accounting policies for recognition, classification and measurement and impairment of financial assets. There were no changes in the classification of financial liabilities. PFRS 9 also significantly amends other standards dealing with financial instruments such as PFRS 7, Financial Instruments: Disclosures.

The table below presents the classification and measurement of the Bank's financial assets as at December 31, 2017 and January 1, 2018:

	PAS 39		PFRS 9	
	December 31, 2017		January 1, 2018	
Financial assets	Measurement category	Carrying amount	Measurement category	Carrying amount
Cash and other cash items	Amortized cost	26,310,761	Amortized cost	26,310,761
Due from other banks	Amortized cost	967,092,652	Amortized cost	967,092,652
Interbank loans receivable	Amortized cost	165,255,798	Amortized cost	165,255,798
Due from BSP	Amortized cost	8,793,748,200	Amortized cost	8,793,748,200
Investment securities				
Equity	FVOCI (AFS)	24,720	FVOCI	24,720
Debt	FVOCI (AFS)	102,935,795	FVOCI	102,935,795
Loans and advances, net	Amortized cost	4,296,200,000	Amortized cost	4,284,347,311
Other financial assets	Amortized cost	95,460,290	Amortized cost	95,460,290

The Bank shifted from the incurred loss model under PAS 39 to the ECL model in the determination of impairment provisions for financial assets not carried at fair value through profit or loss upon adoption of PFRS 9. As a result, the Bank booked transitional adjustment to the opening balance of Surplus as at January 1, 2018 amounting to P12 million for the additional allowance determined under PFRS 9.

Reconciliation of statement of condition balances from PAS 39 to PFRS 9

On January 1, 2018, the Bank performed a detailed analysis of its business models for managing financial assets including their cash flow characteristics. Please refer to Note 24.5 for more detailed information regarding the new classification requirements of PFRS 9.

The financial assets affected by the adoption of the new standard are shown below. The reconciliation of the carrying amounts of these financial assets from their previous measurement category in accordance with PAS 39 to their new measurement categories upon transition to PFRS 9 on January 1, 2018 follow:

	Investment securities at FVOCI	**Loans and advances, net**
Closing balance, December 31, 2017 - PAS 39	**102,960,515**	**4,296,200,000**
Reclassifications	-	
ECL provision	-	(11,852,689)
	-	(11,852,689)
Opening balance, January 1, 2018 - PFRS 9	**102,960,515**	**4,284,347,311**

(b) New standards, amendments and interpretations not yet effective and not yet adopted by the Bank

A number of new standards, amendments and interpretations are effective for annual periods beginning after January 1, 2018, and have not been applied in preparing these financial statements. None of these standards are relevant to the financial statements of the Bank, except the following as set out below:

- *PFRS 16, Leases (effective for annual periods beginning on or after January 1, 2019)*

  PFRS 16 will replace the current guidance in PAS 17, '*Leases*'. PFRS 16 which will become effective on January 1, 2019 will affect primarily the accounting by lessees and will result in the recognition of almost all leases on balance sheet. PFRS 16 removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts. Under PFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. An optional exemption exists for short-term and low-value leases.

  The adoption of PFRS 16 will likely affect the accounting for long-term operating lease agreements of the Bank. The financial impact is currently being finalized by the Bank's management.

- *Philippine Interpretation IFRIC-23, Uncertainty over Income Tax Treatments (effective for annual periods beginning on or after January 1, 2019)*

  It has been clarified previously that PAS 12, '*Income taxes*', not PAS 37, '*Provisions, Contingent Liabilities and Contingent Assets*', applies to accounting for uncertain income tax treatments. IFRIC 23 explains how to recognize and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.

  An uncertain tax treatment is any tax treatment applied by an entity where there is uncertainty over whether that treatment will be accepted by the tax authority. For example, a decision to claim a deduction for a specific expense or not to include a specific item of income in a tax return is an uncertain tax treatment if its acceptability is uncertain under tax law. IFRIC 23 applies to all aspects of income tax accounting where there is an uncertainty regarding the treatment of an item, including taxable profit or loss, the tax bases of assets and liabilities, tax losses and credits and tax rates.

  The adoption of the above interpretation will not have a material impact on the Bank's financial statements.

There are no other standards, amendments or interpretations that are effective after January 1, 2018 that are expected to have a material impact on the Bank's financial statements.

24.2 Business combination between entities under common control

Business combinations under common control are accounted for using the predecessor cost method following the guidance under the PIC Q&A No. 2011-02 and PIC Q&A 2012-01. Under this method, the Bank does not restate the acquired businesses or assets and liabilities to their fair values. The net assets of the combining entities or businesses are combined using the carrying amounts of assets and liabilities of the acquired entity. No amount is recognized in consideration for goodwill or the excess of acquirer's interest in the net fair value of acquired identifiable assets, liabilities and contingent liabilities over their cost at the time of the common control combination.

The financial statements incorporated the net assets and results of operations of the combining entities or businesses at the date of acquisition. The difference between the consideration given and the aggregate book value of the assets and liabilities acquired as of the date of the transaction are included in "Other reserves" under the equity account.

24.3 Cash and cash equivalents

Cash and cash equivalents consist of cash and other cash items, due from BSP and other banks and interbank loans receivable with maturities of less than three months from the date of acquisition and that are subject to insignificant risk of changes in value.

24.4 Reverse repurchase agreements

Securities sold subject to repurchase agreements are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral; the counterparty liability is included in deposits from banks or deposits from customers, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Securities purchased under agreements to resell are recorded as loans and advances to other banks and customers and included in the statement of condition under "Interbank loans receivable." Securities lent to counterparties are also retained in the financial statements.

24.5 Financial assets

Policies applicable beginning January 1, 2018 (PFRS 9)

24.5.1 Classification and subsequent measurement (PFRS 9)

From January 1, 2018, the Bank has applied PFRS 9 and classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value through profit or loss (FVTPL);
- those to be measured subsequently at FVOCI; and
- those to be measured at amortized cost.

The classification depends on the Bank's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether Bank has made an irrevocable election at the time of initial recognition to account for the equity investment at FVOCI.

The Bank reclassifies debt investments when and only when its business model for managing those assets changes.

In the determination of the business model, the Bank considers its past experience on how the cash flows for these assets were collected, how the assets' performance are evaluated and how risks are assessed and managed.

24.5.2 Recognition and derecognition

Regular way purchases and sales of financial assets are recognized on trade date, the date on which the Bank commits to purchase or sell the asset. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or have been transferred and the Bank has transferred substantially all the risks and rewards of ownership.

24.5.3 Measurement

The classification requirements for debt and equity instruments are described below:

At initial recognition, the Bank measures a financial asset at its fair value plus, in the case of a financial asset not at FVTPL, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVTPL are expensed in profit or loss.

Based on these factors, the Bank classifies its debt instruments into one of the following three measurement categories:

Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds and trade receivables purchased from clients in factoring arrangements without recourse. Subsequent measurement of debt instruments depends on the Bank's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Bank classifies its debt instruments:

- *Amortized cost*
  Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI'), and that are not designated at fair value through profit or loss, are measured at amortized cost. The carrying amount of these assets is adjusted by any ECL allowance recognized and measured. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

  Amortized cost financial assets as at January 1, 2018 and December 31, 2018 include cash and other cash items, due from BSP, due from other banks, interbank loans receivables, loans and advances, and other financial assets.

- *FVOCI*
  Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVTPL, are measured at fair value through other comprehensive income (FVOCI). Movements in the carrying amount are taken through other comprehensive income, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortized cost which are recognized in the statements of income. When the financial asset is derecognized, the cumulative gain or loss previously recognized in other comprehensive income is reclassified from equity to profit or loss. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

  The Bank's financial assets at FVOCI as at January 1, 2018 to December 31, 2018 consist of corporate bonds.

- *FVTPL*
  Assets that do not meet the criteria for amortized cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognized in profit or loss and presented in the statements of income within Trading gain on securities in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately.

  The Bank does not hold financial assets at FVTPL as at January 1, 2018 and December 31, 2018.

Business model: The business model reflects how the Bank manages the assets in order to generate cash flows. That is, whether the Bank's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable, then the financial assets are classified as part of 'other' business model and measured at fair value through profit or loss. Factors considered by the Bank in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Bank assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

The Bank reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and none occurred during the period.

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets.

The Bank subsequently measures equity investments at FVTPL, except where the Bank's management has elected, at initial recognition, to irrevocably designate an equity investment at fair value through other comprehensive income. The Bank's policy is to designate equity investments as FVOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognized in other comprehensive income and are not subsequently reclassified to profit or loss, even on disposal. Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value. Dividends, when representing a return on such investments, continue to be recognized in profit or loss as other income when the Bank's right to receive payments is established. Gains and losses on equity investments at fair value through profit or loss are included in the Trading gain on securities in the statement of income.

24.5.4 Impairment of financial assets at FVOCI and at amortized costs

The Bank assesses impairment as follows:

- individually for loans that exceed specified thresholds - where there is an objective evidence of impairment, individually assessed provisions will be recognized; and
- collectively for loans below the specified thresholds noted above or if there is no objective evidence of impairment. These loans are included in a group of loans with similar risk characteristics and collectively assessed for impairment. If there is objective evidence that the group of loans is collectively impaired, collectively assessed provisions will be recognised.

24.5.5 Expected credit losses

The Bank assesses on a forward-looking basis the ECL associated with its debt instrument assets carried at amortized cost and FVOCI and with the exposure arising from loan commitments. The Bank recognizes a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

PFRS 9 outlines a 'three-stage' model for impairment based on changes in credit quality since initial recognition as summarized below:

- A financial instrument that is not credit-impaired on initial recognition is classified in "Stage 1" and has its credit risk continuously monitored by the Bank.
- If a significant increase in credit risk since initial recognition is identified, the financial instrument is moved to "Stage 2" but is not yet deemed to be credit-impaired. The Bank determines SICR based on prescribed benchmarks approved by the Board of the Directors.
- If the financial instrument is credit-impaired, the financial instrument is then moved to "Stage 3".

- Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on ECL on a lifetime basis.
- A pervasive concept in measuring ECL in accordance with PFRS 9 is that it should consider forward-looking information.

The Bank assesses on a forward-looking basis the ECL associated with its debt instrument assets carried at amortized cost and FVOCI. The Bank recognizes a loss allowance for such losses at each reporting date.

The following diagram summarizes the impairment requirements under PFRS 9 (other than purchased originated credit-impaired financial assets):

Change in credit quality since initial recognition

Stage 1	Stage 2	Stage 3
(Initial recognition)	(Significant increase in credit risk since initial recognition)	(Credit-impaired assets)
12-month expected credit losses	Lifetime expected credit losses	Lifetime expected credit losses

For ECL provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous.

Determination of significant increase in credit risk (SICR)

The Bank compares the probabilities of default occurring over its expected life as at the reporting date with the probability of default occurring over its expected life on the date of initial recognition to determine significant increase in credit risk. Since comparison is made between forward-looking information at reporting date against initial recognition, the deterioration in credit risk may be triggered by the following factors:

- substantial deterioration in credit quality as measured by the applicable internal or external ratings, credit score or shift from investment grade category to non-investment grade category;
- adverse changes in business, financial and/or economic conditions of the borrower;
- early warning signs of worsening credit where the ability of the counterparty to honor his obligation is dependent upon favorable business or economic condition;
- the account has become past due beyond 30 days where an account is classified under special monitoring category; and
- expert judgment for the other quantitative and qualitative factors which may result to SICR as defined by the Bank.

Measuring ECL - Inputs, assumptions and estimation techniques

The ECL is measured on either a 12-month or lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. ECLs are the discounted product of the PD, EAD and LGD, defined as follows:

- The PD represents the likelihood that the borrower will default (as per "Definition of default and credit-impaired" above), either over the next 12 months (12M PD), or over the remaining life (lifetime PD) of the asset.

- EAD is based on the amounts the Bank expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining life (lifetime EAD). For example, for a revolving commitment, the Bank includes the current drawn balance plus any further amount that is expected to be drawn up to the current contractual limit by the time of default, should it occur.

  The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type.

  - For amortizing products and bullet repayment loans, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis.
  - For committed credit lines, the exposure at default is predicted by taking current drawn balance and adding a "credit conversion factor" which allows for the expected drawdown of the remaining limit by the time of default.

- LGD represents the Bank's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default.

  The LGDs are determined based on the factors which impact the recoveries made post-default.

  - For secured products, this is primarily based on collateral type and projected collateral values, historical discounts to market/book values due to forced sales, time to repossession and recovery costs observed.
  - For unsecured products, LGDs are typically set at product level due to the limited differentiation in recoveries achieved across different borrowers. These LGDs are influenced by collection strategies and historical recoveries.

The ECL is determined by multiplying the PD, LGD and EAD together for each individual exposure or collective segment. This effectively calculates an ECL for each future year, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

The lifetime PD is developed by applying a maturity profile to the current 12M PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the life of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and credit grade band.

Forward-looking economic information is also included in determining the 12-month and lifetime PD. These assumptions vary by product type.

The assumptions underlying the ECL calculation - such as how the maturity profile of the PDs and how collateral values change - are monitored and reviewed regularly.

There have been no significant changes in estimation techniques or significant assumptions made during the reporting period from the time of the adoption of PFRS 9 on January 1, 2018 to the reporting date.

Forward-looking information incorporated in the ECL models

The Bank incorporates historical and current information, and forecasts forward-looking events and key economic variables that are assessed to impact credit risk and ECL for each portfolio. Macroeconomic variables that affect a specific portfolio's non-performing loan rate(s) are determined through statistical modelling and the application of expert judgement. The Bank's economics team establishes possible global and domestic economic scenarios. With the use of economic theories and conventions, expert judgement and external forecasts, the economics team develops assumptions to be used in forecasting variables in the next five (5) years, subsequently reverting to long run-averages. The probability-weighted ECL is calculated by running each scenario through the relevant ECL models and multiplying it by the appropriate scenario weighting.

The estimation and application of forward-looking information requires significant judgment. As with any economic forecasts, the projections and likelihood of occurrences are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The scenarios and their attributes are reassessed at each reporting date. Information regarding the forward-looking economic variables and the relevant sensitivity analysis is disclosed in Note 22.

Financial assets with low credit risk

Loss allowance for financial assets at amortized cost and FVOCI that have low credit risk is limited to 12-month ECLs. Management considers "low credit risk" for listed government bonds to be an investment grade credit rating with at least one major rating agency. Other debt instruments are considered to be low credit risk when they have a low risk of default and the issuer has a strong capacity to meet its contractual cash flow obligations in the near term.

Definition of default and credit-impaired assets

The Bank considers a financial instrument in default or credit-impaired, when it meets one or more of the following criteria:

Quantitative criteria

The borrower is more than 90 days past due on its contractual payments (with the exception of micro-finance loans where a borrower is required to be over 7 days past due to be considered in default).

Qualitative criteria

The counterparty is experiencing significant financial difficulty which may lead to non-payment of loan as may be indicated by any or combination of the following events:

- The counterparty is in long-term forbearance;
- The counterparty is insolvent;
- The counterparty is in breach of major financial covenant(s) which lead(s) to event of default;
- An active market for the security has disappeared;
- Granting of concession that would not be otherwise considered due to economic or contractual reasons relating to the counterparty's financial difficulty;
- It is becoming probable that the counterparty will enter bankruptcy or other financial reorganization; and
- Financial assets are purchased or originated at a deep discount that reflects the incurred credit losses.

The criteria above have been applied to all financial instruments held by the Bank and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the probability of default, EAD, and LGD throughout the Bank's ECL calculations.

The Bank's definition of default is substantially consistent with non-performing loan definition of the BSP. For treasury and debt securities, these are classified as defaulted based on combination of BSP and external credit rating agency definitions.

24.5.6 Modification of loans

The Bank sometimes renegotiates or otherwise modifies the contractual cash flows of loans to customers. When this happens, the Bank assesses whether or not the new terms are substantially different to the original terms. The Bank does this by considering, among others, the following factors:

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- Significant extension of the loan term when the borrower is not in financial difficulty.
- Significant change in the interest rate.
- Change in the currency the loan is denominated in.
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Bank derecognizes the original financial asset and recognizes a 'new' asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Bank also assesses whether the new financial asset recognized is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognized in the statement of income as a gain or loss on derecognition.

24.5.7 Derecognition other than on a modification

Financial assets, or a portion thereof, are derecognized when the contractual rights to receive the cash flows from the assets have ceased, or when they have been transferred and either (i) the Bank transfers substantially all the risks and rewards of ownership, or (ii) the Bank neither transfers nor retains substantially all the risks and rewards of ownership and the Bank has not retained control.

The Bank derecognizes financial assets if the principal terms and conditions have been modified in accordance with a new (restructured) agreement setting forth a new plan of payment or a schedule of payment on a periodic basis. Derecognition of loan is necessary in cases where the deterioration in the financial position of the borrower is such that the borrower can no longer service his debt, whether principal and/or interest, according to existing terms and conditions. This would have been brought about by major operating losses and/or serious and sustained impairment in cash flow, in turn caused by factors such as adverse economic and industry trends, contraction of markets or revenue sources, heavy debt burden, poor business/financial management, labor unrest, and product obsolescence which contributed to business financial difficulty.

The Bank enters into transactions where it retains the contractual rights to receive cash flows from assets but assumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards. These transactions are accounted for as 'pass through' transfers that result in derecognition if the Bank:

(i) Has no obligation to make payments unless it collects equivalent amounts from the assets;
(ii) Is prohibited from selling or pledging the assets; and
(iii) Has an obligation to remit any cash it collects from the assets without material delay.

Collateral (shares and bonds) furnished by the Bank under standard repurchase agreements and securities lending and borrowing transactions are not derecognized because the Bank retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met. This also applies to certain securitization transactions in which the Bank retains a subordinated residual interest.

24.5.7 Write-off policy

The Bank writes off financial assets when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) where the Bank's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full. Eligible loans, other credit accommodations or advances for write-off are proposed in full outstanding principal amounts.

The Bank may write-off financial assets that are still subject to enforcement activity. The outstanding contractual amounts of such assets written off during the year ended December 31, 2018 was P147 million. The write-off of loans is being approved by the BOD in compliance with the BSP requirements.

Policies applicable until December 31, 2017 (PAS 39)

24.5.8 Classification

The Bank classifies its financial assets in the following categories: (i) FVTPL, (ii) loans and receivables, (iii) held-to-maturity securities and (iv) available-for-sale securities. The classification depends on the purpose for which the financial assets are acquired. Management determines the classification of its financial assets at initial recognition.

As at December 31, 2017, the Bank has no financial assets classified at FVTPL and held-to-maturity securities.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments: (i) that are not quoted in an active market, (ii) with no intention of being traded, and (iii) that are not designated as available-for sale securities. Significant accounts falling under this category are cash and other cash items, due from BSP and other banks, interbank loans and receivable, loans and advances and accrued interest receivable and accounts receivable under Other resources, net.

AFS securities

Available-for-sale securities are non-derivative financial aseets that are either designated in this category or not classified in any of the other categories. AFS securities are classified as such in the statement of condition.

24.5.9 Recognition and measurement

Initial recognition and measurement

Regular-way purchases and sales of financial assets at fair value through profit or loss, held-to-maturity security and available-for-sale securities are recognized on trade date, the date on which the Bank commits to purchase or sell the asset. Loans and receivables are recognized upon origination when cash is advanced to the borrowers or when the right to receive payment is established. Financial assets such as available for sale securities and loans and advances are initially recognized at fair value plus transaction costs. Financial assets carried at fair value through profit or loss are initially recognized at fair value; and transaction costs are recognized in profit or loss.

Subsequent measurement

Available-for-sale securities are subsequently carried at fair value. Loans and receivables are subsequently carried at amortized cost using the effective interest method. Changes in the fair value of available-for-sale securities are recognized directly in other comprehensive income, until the financial asset is derecognized or impaired at which time the cumulative fair value adjustments previously recognized in other comprehensive income is recognized in profit or loss. However, interest is calculated on these securities using the effective interest method and foreign currency gains or losses on monetary assets classified as available-for-sale securities are recognized in profit or loss. Dividends on equity instruments are recognized in profit or loss when the Bank's right to receive payment is established.

24.5.10 Reclassification

The Bank may choose to reclassify financial assets that would meet the definition of loans and receivables or held-to-maturity securities out of the available-for-sale category if the Bank has the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification.

Reclassifications are made at fair value as at reclassification date. Fair value becomes the new cost or amortized cost as applicable, and no reversals of fair value gains or losses recorded before reclassification date are subsequently made. Effective interest rates for financial assets reclassified to loans and receivables and held-to-maturity categories are determined at reclassification date. Further increases in estimates of cash flows adjust effective interest rates prospectively.

24.5.11 Impairment of financial assets

(a) Assets carried at amortized cost

The Bank assesses at each reporting date whether there is an objective evidence that a financial asset or a group of financial asset is impaired. A financial asset or a group of financial asset is impaired and impairment losses are incurred only if there is an objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Bank uses to determine that there is an objective evidence of impairment include:
- delinquency in contractual payments of principal or interest;
- cash flow difficulties experienced by the borrower;
- breach of loan covenants or conditions;
- initiation of bankruptcy proceedings;
- deterioration of the borrower's competitive position; and
- deterioration in the value of collateral.

The Bank first assesses whether an objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an 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 them for impairment. Financial assets that are individually assessed for impairment and for which an impairment loss is or continues t6 be recognized are not included in a collective assessment of impairment.

The amount of impairment loss is measured as the difference between the financial asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate (recoverable amount). The calculation of recoverable amount of a collateralized financial asset reflects the cash flows that may result from foreclosure less cost of obtaining and selling the collateral, whether or not foreclosure is probable. Impairment loss is recognized in the statement of income and the carrying amount of the asset is reduced through the use of an allowance.

For purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e., on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Bank and historical loss experience for assets with credit risk characteristics similar to those in the Bank. 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 currently exist. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the statement of income as a reduction of impairment losses for the year.

(b) Assets classified as available-for-sale

The Bank assesses at each reporting date whether there is an objective evidence that a security classified as available-for-sale is impaired. For debt securities, the Bank uses the criteria disclosed under loans and advances. For an equity security classified as available-for-sale, a significant or prolonged decline in the fair value below cost is considered in determining whether the securities are impaired.

Generally, the Bank treats 20% or more as 'significant' and greater than twelve months as 'prolonged'. The cumulative loss (difference between the acquisition cost and the current fair value less any impairment loss on that financial asset previously recognized in profit or loss) is removed from other comprehensive income and recognized in profit or loss when the asset is determined to be impaired. If in a subsequent period, the fair value of a debt instrument previously impaired increases and the increase can be objectively related to an event occurring after the impairment loss was recognized, the impairment loss is reversed through profit or loss. Reversal of impairment losses recognized previously on equity instruments is made directly to other comprehensive income.

(c) *Renegotiated loans*

Loans that are either subject to individual or collective impairment assessment and those with terms which have been renegotiated are no longer considered to be past due but are treated as new loans.

24.5.12 Derecognition

A financial asset is derecognized when the contractual right to receive the cash flows from the asset has ceased to exist or the asset has been transferred and substantially all the risks and rewards of ownership of the asset are also transferred (that is, if substantially all the risks and rewards have not been transferred, the Bank tests control to ensure that continuing involvement on the basis of any retained powers of control does not prevent derecognition).

Policies applicable for both years

24.6 Financial liabilities

24.6.1 Classification

The Bank classifies its financial liabilities in the following categories: financial liabilities at fair value through profit or loss, and financial liabilities at amortized cost.

(a) *Financial liabilities at fair value through profit or loss*

This category comprises two sub-categories: financial liabilities classified as held for trading, and financial liabilities designated by the Bank as at fair value through profit or loss upon initial recognition.

A financial liability is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorized as held for trading unless they are designated and effective as hedging instruments.

As at December 31, 2018 and 2017, the Bank has no financial liabilities that are designated at fair value through profit loss.

(b) *Other liabilities measured at amortized cost*

Financial liabilities that are not classified as at fair value through profit or loss fall into this category and are measured at amortized cost.

Financial liabilities measured at amortized cost include deposit liabilities, accrued interest and other expenses, and other liabilities (except tax-related/statutory payables).

24.6.2 Recognition and measurement

Initial recognition and measurement

Financial liabilities at amortized cost are initially recognized at fair value plus transaction costs.

Subsequent measurement

Financial liabilities at amortized cost are subsequently measured at amortized cost using the effective interest method.

24.6.3 Derecognition

Financial liabilities are derecognized when they have been redeemed or otherwise extinguished (i.e. when the obligation is discharged or is cancelled or has expired). Collateral (shares and bonds) furnished by the Bank under standard repurchase agreements and securities lending and borrowing transactions, if any, is not derecognized because the Bank retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met.

24.7 Fair value measurement

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 measurement date.

The fair value of financial and non-financial liabilities takes into account non-performance risk, which is the risk that the entity will not fulfill an obligation.

Financial instruments

The Bank classifies its fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges (for example, Philippine Stock Exchange, Inc., Philippine Dealing and Exchange Corp. (PDEX), etc.).

- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes the majority of the over-the-counter ("OTC") derivative contracts. The primary source of input parameters like LIBOR yield curve or counterparty credit risk is Bloomberg.

- Level 3 - Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components. This hierarchy requires the use of observable market data when available. The Bank considers relevant and observable market prices in its valuations where possible. The Bank has no assets or liabilities classified under Level 3 as at December 31, 2018 and 2017.

The appropriate level is determined on the basis of the lowest level input that is significant to the fair value measurement.

For financial instruments traded in active markets, the determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations. This includes listed equity securities and quoted debt instruments on major exchanges and broker quotes mainly from PDEX and Bloomberg.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indications that a market is inactive are when there is a wide bid-offer spread or significant increase in the bid-offer spread or there are few recent transactions.

For all other financial instruments, fair value is determined using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques, using inputs (for example, LIBOR yield curve, FX rates, volatilities and counterparty spreads) existing at reporting dates. The Bank uses widely recognized valuation models for determining fair values of non-standardized financial instruments of lower complexity. For these financial instruments, inputs into models are generally market observable.

In cases when the fair value of unlisted equity instruments cannot be determined reliably, the instruments are carried at cost less impairment.

The fair value for loans and advances as well as liabilities to banks and customers are determined using a present value model on the basis of contractually agreed cash flows, taking into account credit quality, liquidity and costs. The fair values of contingent liabilities and irrevocable loan commitments correspond to their carrying amounts.

Non-financial assets or liabilities

The Bank uses valuation techniques that are appropriate in the circumstances and applies the technique consistently. Commonly used valuation techniques are as follows:

- Market approach - A valuation technique that uses observable inputs, such as prices, broker quotes and other relevant information generated by market transactions involving identical or comparable assets or group of assets.

- Income approach - A valuation technique that converts future amounts (e.g., cash flows or income and expenses) to a single current (i.e., discounted) amount. The fair value measurement is determined on the basis of the value indicated by current market expectations about those future amounts.

- Cost approach - A valuation technique that reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost).

The fair values were determined in reference to observable market inputs reflecting orderly transactions, i.e. market listings, published broker quotes and transacted deals from similar and comparable assets, adjusted to determine the point within the range that is most representative of the fair value under current market conditions.

The fair values of the Bank's foreclosed assets (shown as Assets held for sale) fall under level 2 of the fair value hierarchy using market approach. The Bank has no non-financial assets or liabilities classified under Level 3 as at December 31, 2018 and 2017.

24.8 Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of condition when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously. As at December 31, 2018 and 2017, there are no financial assets and liabilities that have been offset.

24.9 Bank premises, furniture, fixtures and equipment

Bank premises, furniture, fixtures and equipment are stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of an asset which comprises its purchase price, import duties and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Subsequent costs are included in the asset's carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to profit or loss during the financial year in which they are incurred.

Depreciation on assets is calculated using the straight-line method to allocate cost of each asset less its residual value over its estimated useful life as follows:

	Estimated useful life
Leasehold rights and improvements	Based on lease term or life of the leased item whichever is shorter
Furniture, fixtures, and equipment	36 months
Computer equipment	36 months

Leasehold rights and improvements in progress are stated at cost. Costs are accumulated in the accounts until these projects are completed upon which these are classified to the appropriate property accounts and accordingly depreciated.

Major renovations are depreciated over the remaining useful life of the related asset. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell or value-in-use.

An item of Bank premises, furniture, fixtures and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. 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 item) is included in profit or loss in the period the item is derecognized.

24.10 Computer software

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specified software. These costs are amortized on a straight-line basis over the expected useful lives of three to five years. Computer software is included in Other resources, net.

24.11 Impairment of non-financial assets

Asset that have indefinite useful lives - for example, goodwill or intangible assets not ready for use, are not subject to amortization and depreciation and are tested annually for impairment. Assets that have definite useful life are subject to amortization and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For purposes of assessing impairment, assets are grouped at the lowest levels for which there is a separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

24.12 Foreclosed asset

Assets foreclosed shown as Assets held for sale in the statement of condition are accounted for at the lower of cost and fair value less cost to sell, similar to the principles of PFRS 5. The cost of assets foreclosed includes the carrying amount of the related loan less allowance for impairment at the time of foreclosure. Impairment loss is recognized for any subsequent write-down of the asset to fair value less cost to sell.

These foreclosed assets are classified as assets held for sale since it is the intention of the Bank's management to principally recover the carrying amount through sale transactions and the sale is considered highly probable. The sale is expected to be completed within one year from the date of classification. In case events or circumstances may extend the period to complete the sale beyond one year, the extension of the period to complete the sale does not preclude the asset from being classified as held-for-sale if the delay is caused by events or circumstances beyond the Bank's control and the Bank remains committed to its plan to sell the asset.

24.13 Accrued expenses and other liabilities

Accrued expenses and other liabilities are recognized in the period in which the related money, goods or services are received or when a legally enforceable claim against the Bank is established.

Accrued expenses and other liabilities are derecognized upon settlement, or when discharged, cancelled or expired.

24.14 Provisions for legal or contractual obligations

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item is included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects the current market assessments of the time value of money and the risk specific to the obligation. The increase in the provision due to the passage of time is recognized as interest expense.

24.15 Interest income and expense

Interest income and expense are recognized in the statement of income for all interest-bearing financial instruments using the effective interest method.

When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognized using the rate of interest used to discount future cash flows for the purpose of measuring impairment loss.

24.16 Service fee income

Fees and commissions, mainly representing service fees, are recognized on an accrual basis when the service has been provided. Fees and commission arising from loans, deposits and other banking transactions are recognized as income based on agreed terms and conditions.

24.17 Foreign currency translation

Functional and presentation currency

Items in the financial statements of the Bank are measured using the currency of the primary economic environment in which it operates (the functional currency). The financial statements are presented in Philippine Peso, which is the Bank's functional currency.

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuations where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of income.

24.18 Income taxes

Current income tax

The tax expense for the period comprises current and deferred income tax. Tax is recognized in profit or loss, except to the extent that that it relates to items recognized in other comprehensive income or directly in equity. In this case, the tax is also recognized in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the reporting date in the country where the Bank operates and generates taxable income.

Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax

Deferred income tax is recognized on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted at the reporting date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized for all deductible temporary differences, carry-forward of unused tax losses (net operating loss carryover or NOLCO) and unused tax credits (excess minimum corporate income tax or MCIT) to the extent that it is probable that future taxable profit will be available against which the temporary differences, unused tax losses and unused tax credits can be utilized.

Deferred income tax liabilities are recognized in full for all taxable temporary differences in full for all taxable temporary differences. Deferred income tax liabilities are provided on taxable temporary differences except for deferred income tax liability where the timing of the reversal of the temporary difference is controlled by the Bank and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

24.19 Employee benefits

(a) Short-term benefits

The Bank recognizes a liability, net of amount already paid and an expense for services rendered by employees during the accounting period. Short-term benefits given to its employees include salaries and wages, social security contributions, short-term compensated absences and bonuses, and non-monetary benefits.

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

(b) Defined benefit retirement plan

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation.

The liability recognized in the statement of condition in respect of defined benefit pension plan is the present value of the defined benefit obligation at the reporting date less the fair value of plan assets. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

Past-service costs are recognized immediately in profit or loss.

For individual financial reporting purposes, the unified plan assets are allocated among the Bank entities based on the level of the defined benefit obligation attributable to each entity to arrive at the net liability or asset that should be recognized in the individual financial statements.

(c) Defined contribution retirement plan

The Bank also maintains a defined contribution plan that covers certain full-time employees. Under its defined contribution plan, the Bank pays fixed contributions based on the employees' monthly salaries. The Bank, however, is covered under RA No. 7641, otherwise known as The Philippine Retirement Pay Law, which provides for its qualified employees a defined benefit minimum guarantee. The defined benefit minimum guarantee is equivalent to a certain percentage of the monthly salary payable to an employee at normal retirement age with the required credited years of service based on the provisions of RA No. 7641. Accordingly, the Bank accounts for its retirement obligation under the higher of the defined benefit obligation relating to the minimum guarantee and the obligation arising from the defined contribution plan.

For the defined benefit minimum guarantee plan, the liability is determined based on the present value of the excess of the projected defined benefit obligation over the projected defined contribution obligation at the end of the reporting period. The defined benefit obligation is calculated annually by a qualified independent actuary using the projected unit credit method. The Banks determine the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability (asset) then, taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to the defined benefit plan are recognized in the statement of income.

The defined contribution liability is measured at the fair value of the defined contribution assets upon which the defined contribution benefits depend, with an adjustment for margin on asset returns, if any, where this is reflected in the defined contribution benefits.

Actuarial gains and losses arising from the remeasurements of the net defined contribution liability are recognized immediately in other comprehensive income.

(d) Profit sharing and bonus plans

The Bank recognizes a liability and an expense for bonuses and profit-sharing, based on a formula that takes into consideration the profit attributable to the Bank's shareholder after certain adjustments. The Bank recognizes a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

24.20 Share capital

Share capital represents common shares.

Incremental costs directly attributable to the issue of new shares are shown in capital funds as a deduction from the proceeds, net of tax.

24.21 Dividends on common shares

Dividends are recognized as a liability in the Bank's financial statements in the year in which they are approved by the Board of Directors.

24.22 Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by another party, the lessor, are classified as operating leases. Payments, including prepayments, made under operating leases (net of any incentives received from the lessor) are charged to "Occupancy and equipment-related expenses" in the statement of income on a straight-line basis over the period of the lease. When the lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognized as an expense in the period in which the termination takes place.

Lease income from operating sub-leases where the Bank is the intermediate party is recognized in income on a straight-line basis over the lease term.

24.23 Related party relationships and transactions

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

24.24 Subsequent events (or Events after the reporting date)

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

Note 25 - Supplementary information required by the Bureau of Internal Revenue (BIR)

Below is the additional information required by Revenue Regulations No. 15-2010 that is relevant to the Bank. This is information is presented for purposes of filing with the BIR and is not a required part of the basic financial statements.

Documentary stamp tax

Documentary stamp taxes (DST) paid through the Electronic Documentary Stamp Tax System for the year ended December 31, 2018 consist of DST on deposit documents amounting to P34,453,710 and DST on contract of lease amounting to P382,098.

Withholding taxes

Withholding taxes paid/accrued and/or withheld for the year ended December 31, 2018 consist of:

	Paid	Accrued	Total
Final income taxes withheld on interest on deposits and yield on deposit substitutes	13,826,754	2,768,899	16,595,653
Income taxes withheld on compensation	6,582,347	693,233	7,275,580
Creditable income taxes withheld (expanded)	14,966,410	4,149,174	19,115,584
	35,375,511	7,611,306	42,986,817

Withholding tax payable is presented as part of Accrued taxes, interest and other expenses in the statement of condition.

All other local and national taxes

All other local and national taxes paid/accrued for the year ended December 31, 2018 consist of:

	Paid	Accrued	Total
Gross receipts tax	76,277,684	34,438,841	110,716,525
Fringe benefits tax	90,732	24,167	114,899
Municipal taxes / Mayor's permit	2,242,533	-	2,242,533
Real property tax	372,487	-	372,487
Others	842,294	-	842,294
	79,825,730	34,463,008	114,288,738

Local and national taxes are presented as part of taxes and licenses under Other operating expenses in the statement of income.

Tax cases and assessments

As at reporting date, the Bank has pending cases filed in court and with the tax authorities contesting tax assessments. Management is of the opinion that the ultimate outcome of the said case will not have a material impact on the financial statements of the Bank.

BPI Direct BanKo, Inc., A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)
BanKo Center Building,
Ortigas Avenue, North Greenhills,
San Juan, Metro Manila

Reconciliation of Retained Earnings Available for Dividend Declaration
As at December 31, 2018
(All amounts in Philippine Peso)

Unappropriated Retained Earnings, beginning		1,969,611,156
Add: Net income actually earned/realized during the period		
Net income during the period closed to retained earnings	268,990,385	
Less: Non-actual/unrealized income net of tax		
Equity in net income of associate/joint venture	-	
Unrealized foreign exchange gain - net (except those attributable to Cash and Cash Equivalents)	-	
Fair value adjustment (market-to-market gains)	-	
Fair value adjustment of Investment Property resulting to gain	-	
Adjustment due to deviation from PFRS/GAAP – gain	-	
Other unrealized gains or adjustments to the retained earnings as a result of certain transactions accounted for under the PFRS	-	
Subtotal	-	
Add: Non-actual losses		
Depreciation on revaluation increment (after tax)	-	
Adjustment due to deviation from PFRS/GAAP - loss	-	
Loss on fair value adjustment of investment property (after tax)	-	
Subtotal	-	
Net income actually earned during the period		268,990,385
Add (Less):		
Dividend declarations during the period	-	
Appropriations of retained earnings during the period	-	
Reversal of appropriation	-	
Effects of prior period adjustments	(11,840,278)	
Treasury shares	-	
Subtotal	(11,840,278)	(11,840,278)
Total Retained Earnings available for dividends, ending		2,226,761,263

BPI Direct BanKo, Inc. A Savings Bank
(Formerly BPI Direct Savings Bank, Inc.)

Schedule of Philippine Financial Reporting Standards Effective as at December 31, 2018

The following table summarizes the effective standards, amendments and interpretations as at December 31, 2018:

		Adopted	Not Adopted	Not Applicable
Framework for the Preparation and Presentation of Financial Statements Conceptual Framework Phase A: Objectives and qualitative characteristics		✓		
PFRSs Practice Statement Management Commentary				✓
Philippine Financial Reporting Standards				
PFRS 1 (Revised)	First-time Adoption of Philippine Financial Reporting Standards	✓		
	Amendments to PFRS 1 and PAS 27: Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate			✓
	Amendment to PFRS 1: Limited Exemption from Comparative PFRS 7 Disclosures for First-time Adopters			✓
	Amendments to PFRS 1: Severe Hyperinflation and Removal of Fixed Date for First-time Adopters			✓
	Amendments to PFRS 1: Government Loans			✓
PFRS 2	Share-based Payment			✓
	Amendments to PFRS 2: Vesting Conditions and Cancellations			✓
	Amendments to PFRS 2: Group Cash-settled Share-based Payment Transactions			✓
	Amendments to PFRS 2: Classification and Measurement of Share-based Payment Transactions			✓
PFRS 3 (Revised)	Business Combinations			✓
	Amendments to PFRS 3: Definition of a business*		✓	
PFRS 4	Insurance Contracts			✓

		Adopted	Not Adopted	Not Applicable
	Amendments to PAS 39 and PFRS 4: Financial Guarantee Contracts			✓
	Amendments to PFRS 4: Applying PFRS 9, Financial Instruments with PFRS 4, Insurance Contracts			✓
PFRS 5	Non-current Assets Held for Sale and Discontinued Operations	✓		
PFRS 6	Exploration for and Evaluation of Mineral Resources			✓
PFRS 7	Financial Instruments: Disclosures	✓		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets			✓
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets - Effective Date and Transition			✓
	Amendments to PFRS 7: Improving Disclosures about Financial Instruments	✓		
	Amendments to PFRS 7: Disclosures - Transfers of Financial Assets			✓
	Amendments to PFRS 7: Disclosures - Offsetting Financial Assets and Financial Liabilities	✓		
	Amendments to PFRS 9, PFRS 7 and PAS 39: Hedge Accounting			✓
	Amendments to PFRS 9 and PFRS 7: Mandatory Effective Date and Transition Disclosures	✓		
PFRS 8	Operating Segments			✓
PFRS 9	Financial Instruments	✓		
	Amendments to PFRS 9, PFRS 7 and PAS 39: Hedge Accounting			✓
	Amendments to PFRS 9 and PFRS 7: Mandatory Effective Date and Transition Disclosures	✓		
	Amendments to PFRS 9: Prepayment Features with Negative Compensation*		✓	
PFRS 10	Consolidated Financial Statements			✓
	Amendments to PFRS 10, PFRS 12 and PAS 28: Application of the Consolidation Exception for Investment Entities			✓

		Adopted	Not Adopted	Not Applicable
	Amendments to PFRS 10 and PAS 28: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*		✓	
PFRS 11	Joint Arrangements			✓
	Amendments to PFRS 11: Acquisition of an Interest in a Joint Operation			✓
PFRS 12	Disclosure of Interests in Other Entities			✓
	Amendments to PFRS 10, PFRS 12 and PAS 28: Application of the Consolidation Exception for Investment Entities			✓
PFRS 13	Fair Value Measurement	✓		
PFRS 14	Regulatory Deferral Accounts			✓
PFRS 15	Revenue from Contracts with Customers	✓		
	Amendments to PFRS 15: Clarifications to PFRS 15	✓		
PFRS 16	Leases*		✓	
PFRS 17	Insurance contracts*			✓
Philippine Accounting Standards				
PAS 1 (Revised)	Presentation of Financial Statements	✓		
	Amendment to PAS 1: Capital Disclosures	✓		
	Amendments to PAS 32 and PAS 1: Puttable Financial Instruments and Obligations Arising on Liquidation			✓
	Amendments to PAS 1: Presentation of Items of Other Comprehensive Income	✓		
	Amendments to PAS 1: Disclosure Initiative	✓		
	Amendments to PAS 1 and PAS 8: Definition of material*		✓	
PAS 2	Inventories			✓
PAS 7	Statement of Cash Flows	✓		
	Amendments to PAS 7: Disclosure Initiative	✓		
PAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	✓		

		Adopted	Not Adopted	Not Applicable
	Amendments to PAS 1 and PAS 8: Definition of material*		✓	
PAS 10	Events after the Reporting Period	✓		
PAS 12	Income Taxes	✓		
	Amendment to PAS 16 - Deferred Tax: Recovery of Underlying Assets	✓		
	Amendments to PAS 12: Recognition of Deferred Tax Assets for Unrealized Losses			✓
PAS 16	Property, Plant and Equipment	✓		
	Amendments to PAS 16 and PAS 38: Acceptable Methods of Depreciation and Amortization	✓		
	Amendments to PAS 16 and PAS 41: Bearer Plants			✓
PAS 17	Leases	✓		
PAS 19 (Revised)	Employee Benefits	✓		
	Amendments to PAS 19: Contributions from Employees or Third Parties	✓		
	Amendments to PAS 19: Plan Settlement, Curtailment or Settlement*		✓	
PAS 20	Accounting for Government Grants and Disclosure of Government Assistance			✓
PAS 21	The Effects of Changes in Foreign Exchange Rates	✓		
	Amendment to PAS 21: Net Investment in a Foreign Operation			✓
PAS 23 (Revised)	Borrowing Costs	✓		
PAS 24 (Revised)	Related Party Disclosures	✓		
PAS 26	Accounting and Reporting by Retirement Benefit Plans			✓
PAS 27 (Revised)	Separate Financial Statements			✓
	Amendments to PAS 27: Use of Equity Method in Separate Financial Statements			✓
PAS 28	Investments in Associates and Joint Ventures			✓

		Adopted	Not Adopted	Not Applicable
(Revised)	Amendments of PFRS 10, PFRS 12 and PAS 28: Application of the Consolidation Exception for Investment Entities			✓
	Amendments to PFRS 10 and PAS 28: Sale or Contributions of Assets between an Investor and its Associate or Joint Venture			✓
	Amendment to PAS 28: Measuring an associate or joint venture at fair value			✓
	Amendments to PAS 28: Long-term Interests in Associates and Joint Ventures*		✓	
PAS 29	Financial Reporting in Hyperinflationary Economies			✓
PAS 32	Financial Instruments: Presentation	✓		
	Amendments to PAS 32 and PAS 1: Puttable Financial Instruments and Obligations Arising on Liquidation			✓
	Amendment to PAS 32: Classification of Rights Issues			✓
	Amendments to PAS 32: Offsetting Financial Assets and Financial Liabilities	✓		
PAS 33	Earnings per Share			✓
PAS 34	Interim Financial Reporting			✓
PAS 36	Impairment of Assets	✓		
	Amendment to PAS 36: Recoverable Amount Disclosures	✓		
PAS 37	Provisions, Contingent Liabilities and Contingent Assets	✓		
PAS 38	Intangible Assets	✓		
	Amendments to PAS 16 and PAS 38: Acceptable Methods of Depreciation and Amortization	✓		
PAS 40	Investment Property			✓
	Amendment to PAS 40: Transfers of Investment Property			✓
PAS 41	Agriculture			✓
	Amendments to PAS 16 and PAS 41: Bearer Plants			✓

		Adopted	Not Adopted	Not Applicable
Philippine Interpretations				
IFRIC 1	Changes in Existing Decommissioning, Restoration and Similar Liabilities			✓
IFRIC 2	Members' Share in Co-operative Entities and Similar Instruments			✓
IFRIC 4	Determining Whether an Arrangement Contains a Lease	✓		
IFRIC 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds			✓
IFRIC 6	Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment			✓
IFRIC 7	Applying the Restatement Approach under PAS 29 Financial Reporting in Hyperinflationary Economies			✓
IFRIC 10	Interim Financial Reporting and Impairment			✓
IFRIC 12	Service Concession Arrangements			✓
IFRIC 14	The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction			✓
	Amendments to IFRIC 14: Prepayments of a Minimum Funding Requirement			✓
IFRIC 15	Agreements for the Construction of Real Estate			✓
IFRIC 16	Hedges of a Net Investment in a Foreign Operation			✓
IFRIC 17	Distributions of Non-cash Assets to Owners			✓
IFRIC 18	Transfers of Assets from Customers			✓
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments			✓
IFRIC 20	Stripping Costs in the Production Phase of a Surface Mine			✓
IFRIC 21	Levies	✓		
IFRIC 22	Foreign Currency Transactions and Advance Consideration			✓
IFRIC 23	Uncertainty over Income Tax Treatments*		✓	
SIC-7	Introduction of the Euro			✓

		Adopted	Not Adopted	Not Applicable
SIC-10	Government Assistance - No Specific Relation to Operating Activities			✓
SIC-15	Operating Leases - Incentives	✓		
SIC-25	Income Taxes - Changes in the Tax Status of an Entity or its Shareholders			✓
SIC-27	Evaluating the Substance of Transactions Involving the Legal Form of a Lease	✓		
SIC-29	Service Concession Arrangements: Disclosures			✓
SIC-32	Intangible Assets - Web Site Costs			✓

The standards, amendments and interpretations marked with an asterisk (*) have been issued but are not yet effective for the December 31, 2018 financial statements. Unless otherwise stated, these standards, amendments and interpretations have not been early adopted.

The standards, amendments and interpretations that are labeled as "Not Applicable" are either already effective or not yet effective as at December 31, 2018 but will never be relevant/applicable to the Company or are currently not relevant to the Company because it has currently no related transactions.