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UNION BANK OF THE PHILIPPINES

(A BANKING CORPORATION ORGANIZED AND EXISTING UNDER PHILIPPINE LAWS)

UP TO ₱5,000,000,000

[•]% LONG TERM NEGOTIABLE CERTIFICATES OF DEPOSIT DUE 2019

OFFER PRICE 100.00 PER CENT OF FACE VALUE

Union Bank of the Philippines, ("UnionBank" or the "Bank") is offering up to ₱5.0 Billion worth of Long Term Negotiable Certificates of Deposit due 2019 (the "LTNCDs") pursuant to the authority granted by the Bangko Sentral ng Pilipinas ("BSP") to the Bank on August 15, 2013 and Section X233.9 of the Manual of Regulations ("MORB") for Banks, BSP Circular No. 304 and BSP Circular No. 428, and any other circulars and regulations as may be relevant for the transaction, as amended from time to time.

The LTNCDs will bear interest at the rate of []% per annum from and including [•] 2013 to but excluding [] and interest will be payable quarterly in arrears at the end of each Interest Period on [•], [•], [•], and [•], beginning on [] 2013.

Unless previously redeemed, the LTNCDs will be redeemed at their principal amount on Maturity Date which is on [] 2019. Subject to the satisfaction of certain regulatory approval requirements, the Bank may redeem the LTNCDs in whole and not only in part on the Early Redemption Option at the face value of the LTNCDs, plus accrued and unpaid interest as of but excluding the Early Redemption Option. *See Terms and Conditions of the LTNCDs – Early Redemption Option.*

The LTNCDs constitute direct, unconditional, unsecured (save for the mandatory insurance coverage under the rules of the Philippine Deposit Insurance Corporation, ("PDIC")), and unsubordinated peso-denominated obligations of the Bank, enforceable according to Terms and Conditions of the LTNCDs, and shall at all times rank pari passu and ratably without any preference or priority amongst themselves, and at least pari passu with all other present and future direct, unconditional, unsecured, and unsubordinated peso-denominated obligations of the Bank, except for any obligation enjoying a statutory preference or priority established under Philippine laws.

The LTNCDs will be issued in scripless form in denominations of ₱250,000.00 per Certificate, and increments of ₱50,000.00 beyond the minimum and will be registered and lodged with the Registrar through the LTNCD Registry in the name of the LTNCD holders. The LTNCDs will be represented by a Master Long Term Negotiable Certificate of Time Deposit deposited with the Registrar. The electronic registry book of the Registrar (the "LTNCD Registry") shall serve as the best evidence of ownership with respect to the LTNCDs up to the level of the beneficial LTNCD holders. However, a written advice will be issued by the Registrar to the LTNCD holders to confirm the registration of LTNCDs in their name in the LTNCD Registry including the amount and summary terms and conditions of the LTNCDs (the "Registry Confirmations"). The LTNCDs are and shall be, while outstanding, insured with the PDIC for up to the maximum insurance coverage set out in and subject to PDIC's applicable rules, regulations, terms and conditions, as may be amended from time to time. *See Terms and Conditions of the LTNCDs.*

The Bank has an Issuer/Debt Rating (long-term) of BB- from Fitch Ratings. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the rating agency concerned. The LTNCDs are not rated.

Sole Lead Arranger and Bookrunner

HSBC

Selling Agents

HSBC

MULTINATIONAL INVESTMENT BANCORPORATION

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The date of this Preliminary Offering Circular is [] 2013.

This Preliminary Offering Circular has been prepared solely for the information of persons to whom it is transmitted by The Hongkong and Shanghai Banking Corporation Limited ("HSBC") as Sole Lead Arranger and Selling Agent, together with Multinational Investment Bancorporation ("MIB") and Union Bank of the Philippines, in their capacity as Selling Agents, with respect to the LTNCDs to be issued by the Bank. This Preliminary Offering Circular shall not be reproduced in any form, in whole or in part, for any purpose whatsoever nor shall it be transmitted to any other person.

The Bank confirms that this Preliminary Offering Circular contains all information with respect to the Parent Bank and its subsidiaries and the LTNCDs which is material in the context of the issue and offering of the LTNCDs. The Bank also confirms that the information contained herein is true and accurate in all material respects and is not misleading, that the opinions and intentions expressed herein are honestly held and have been reached after considering all relevant circumstances and are based on reasonable assumptions, that there are no other facts, the omission of which would, in the context of the issue and offering of the LTNCDs, make this document as a whole or any such information or the expression of any such opinions or intentions misleading in any material respect, and that all reasonable enquiries have been made by the Bank to verify the accuracy of such information. The Bank accepts responsibility accordingly.

In making an investment decision, the prospective LTNCD Holders must rely on its own examination of the Bank and the terms of the offering of the LTNCDs, including the merits and risks involved. By receiving this Preliminary Offering Circular, the prospective LTNCD Holder acknowledges that (i) it has not relied on the Sole Lead Arranger or any of the Selling Agents or any person affiliated with them in connection with its investigation of the accuracy of any information in this Preliminary Offering Circular or its investment decision, and (ii) no person has been authorized to give any information or to make any representation concerning the Bank or the LTNCDs other than as contained in this Preliminary Offering Circular and, if given or made, any such other information or representation should not be relied upon as having been authorized by the Bank, the Sole Lead Arranger or the Selling Agents.

No representation or warranty, express or implied, is made by the Sole Lead Arranger and the Selling Agents as to the accuracy or completeness of the information contained in this Preliminary Offering Circular. The Sole Lead Arranger and the Selling Agents assume no responsibility for the accuracy of the information contained in this Preliminary Offering Circular. Neither the delivery of this Preliminary Offering Circular nor the offer of the LTNCDs shall, under any circumstances, constitute a representation or create any implication that there has been no change in the affairs of the Bank since the date of this Preliminary Offering Circular or that any information contained herein is correct as at any date subsequent to the date hereof. The Sole Lead Arranger and the Selling Agents expressly do not undertake to update the contents of this Preliminary Offering Circular.

None of the Bank, the Sole Lead Arranger or the Selling Agents or any of their respective affiliates or representatives is making any representation to any LTNCD Holder regarding the legality of an investment by such LTNCD Holder under applicable laws. In addition, the LTNCD Holder should not construe the contents of this Preliminary Offering Circular as legal, business or tax advice. The LTNCD Holder should be aware that it may be required to bear the financial risks of an investment in the LTNCDs for an indefinite period. The LTNCD Holder should consult with its own advisers as to the legal, tax, business, financial and related aspects of a purchase of the LTNCDs.

This Preliminary Offering Circular does not constitute an offer to sell, or an invitation by or on behalf of the Bank, the Sole Lead Arranger or Selling Agents or any of their respective affiliates or representatives to purchase any of the LTNCDs, and may not be used for the purpose of an offer to, or a solicitation by, anyone, in each case, in any jurisdiction or in any circumstances in which such offer or solicitation is not authorized or is unlawful. Recipients of this Preliminary Offering Circular are required to inform themselves about and observe any applicable restrictions.

Each LTNCD Holder must comply with all applicable laws and regulations in force in each jurisdiction in which it purchases, offers or sells such LTNCDs or possesses or distributes this Preliminary Offering Circular and must obtain any consent, approval or permission required by it for the purchase, offer or sale by it of such LTNCDs under the laws and regulations in force in any jurisdictions to which it is subject or in which it makes such purchases, offers or sales and the Bank, the Sole Lead Arranger or the Selling Agents shall have no responsibility thereof.

Conventions

In this Preliminary Offering Circular, unless otherwise specified or the context otherwise requires, all references to the "Philippines" are references to the Republic of the Philippines. All references herein to the "Government" are references to the Government of the Philippines. All references herein to "United States" or "U.S." are to the United States of America. Unless otherwise specified or the context otherwise requires, references herein to "U.S. dollars" and "US$" are to the lawful currency of the United States of America and references herein to "Pesos" and "₱" are to the lawful currency of the Republic of the Philippines. Certain monetary amounts and currency translations included in this document have been subject to rounding adjustments; accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures, which precede them. References in this document to ownership interests are, save as otherwise disclosed, as at the date of this document.

Forward-looking Statements

All statements contained in this Preliminary Offering Circular that are not statements of historical fact constitute "forward-looking statements". Some of these statements can be identified by forward-looking terms, such as "anticipate", "believe", "can", "could", "estimate", "expect", "intend", "may", "plan", "will" and "would" or similar words. However, these words are not the exclusive means of identifying forward-looking statements. All statements regarding the Bank's expected financial condition and results of operations, business, plans and prospects are forward-looking statements. These forward-looking statements include statements as to the Bank's business strategy, revenue and profitability, planned projects and other matters discussed in this Preliminary Offering Circular regarding matters that are not historical fact. These forward-looking statements and any other projections contained in this Preliminary Offering Circular (whether made by the Bank or any third party) involve known and unknown risks, uncertainties and other factors that may cause the Bank's actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements or other projections.

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GLOSSARY OF TERMS

In this Preliminary Offering Circular, unless the context otherwise requires, the following terms shall have the meanings set out below:

AAIIB	Al-Amanah Islamic Investment Bank of the Philippines
Aboitiz Group	Aboitiz Equity Ventures, Inc., its subsidiaries and affiliates, as a group
AMLC	Anti-Money Laundering Council
Anti-Money Laundering Act or AMLA	the Anti-Money Laundering Act 2001 of the Philippines
APDS	Automatic Payroll Deduction System
ATM	Automated Teller Machine
Banking Day	any day of the week, other than Saturday or Sunday, when banks are not required or authorized to close in Pasig City and Manila
BAP	Bankers Association of the Philippines
BIR	Philippine Bureau of Internal Revenue
BMBEs	Barangay Micro Business Enterprises
BoC	Bureau of Customs
BSP	Bangko Sentral ng Pilipinas, the Philippine Central Bank
Board, the Board of Directors, or BOD	the Board of Directors of the Bank
Center.	Retail Banking, Consumer Finance, Commercial Banking, Corporate Banking, Transaction Banking, Channel Management, Treasury and Trust
CitySavings.	City Savings Bank, Inc.
CPS	central processing services
Cross-Sells	practice of selling other bank products to an existing customer of the bank
DBP	Development Bank of the Philippines
DepEd	Department of Education

Director	a director of the Bank
DOSRI	loans granted to directors, officers, stockholders and related interests
FCDU..	foreign currency deposit unit
FCPA	Foreign Corrupt Practices Act of 1977
Financial Statements	the Bank's consolidated financial statements and related notes
General Banking Law	General Banking Law of 2000 (Republic Act No. 8791)
GDP	gross domestic product
Government.....................................	the government of the Republic of the Philippines
GRT	gross receipts tax
Guava	an integrated system that performs front, middle and back office functions, including deal entry, accounting, risk management and information reporting
GSIS..	Government Service Insurance System
HGC	Home Guaranty Corporation
HSBC	The Hongkong and Shanghai Banking Corporation Limited
IAS	International Accounting Standards
iBank	International Exchange Bank
IBCL	Interbank call loan
KYC	Know Your Customer
LBP	Land Bank of the Philippines
Metro Manila	the metropolitan area comprising the cities of Kalookan, Las Piñas, Makati, Malabon, Mandaluyong, Manila, Marikina, Muntinlupa, Navotas, Parañaque, Pasay, Pasig, Quezon, Valenzuela and Taguig and the municipality of San Juan, which together comprise the "National Capital Region" and are commonly referred to as "Metro Manila"
MIB	Multinational Investment Bancorporation
MOA	memorandum of agreement
Monetary Board	Monetary Board of the BSP

Moody's .... Moody's Investors Services, Inc.

MORB... the BSP Manual of Regulations for Banks

New Central Bank Act .... New Central Bank Act (Republic Act No. 7653)

NPAs .... non-performing assets

NPLs .... non-performing loans

OBUs .... offshore banking units

Open Source..................................... an approach to the design, development, and distribution of software, offering practical accessibility to a software's source code

P&A .... Punongbayan & Araullo, member firm within Grant Thornton International Ltd.

PAS .... Philippine Accounting Standards

Parent Company............................... Union Bank of the Philippines only (excluding its subsidiaries)

PCD... Philippine Central Depository

PCD Nominee .... PCD Nominee Corporation, a corporation wholly-owned by the PDTC

PDIC .... Philippine Deposit Insurance Corporation

PDTC .... the Philippine Depository and Trust Corporation, the central securities depositary of, among others, securities listed and traded on the PSE

Pesos, Php , or ₱............................... the lawful currency of the Philippines

PFRS .... Philippine Financial Reporting Standards

SEC .... Securities and Exchange Commission

Philippines .... Republic of the Philippines

PSE.. Philippine Stock Exchange

RMs... relationship managers

ROPA.. real and other properties acquired

SCR……………………………… sales contract receivables

SBL .... single borrower limit

Shares	shares of common stock of the Bank, with a par value of ₱10.0 each
SMEs	small- to medium-sized enterprises
SSS	Social Security System
Subordinated Notes	unsecured subordinated amounting to ₱3.7 billion issued by the Bank in October 2009; and ₱1.3 billion issued by the former iBank in March 2006
Tax Code	National Internal Revenue Code
TISG	Trust and Investment Services
TPFM	Trading, Positioning and Funds Management
TMS	Technology Management Services
U.S.$ or U.S. dollar	the lawful currency of the United States of America
UnionBank, UnionBank Group or Bank	Union Bank of the Philippines and its subsidiaries
UITF	unit investment trust funds
VAT	value-added tax

OFFERING CIRCULAR SUMMARY

This summary highlights information contained elsewhere in this Preliminary Offering Circular. This summary is qualified by, and must be read in conjunction with, the more detailed information and financial statements appearing elsewhere in this Preliminary Offering Circular. Each prospective LTNCD Holder is recommended to read this entire Preliminary Offering Circular carefully, including the Financial Statements and "Investment Considerations".

Description of the Bank

Union Bank of the Philippines ("UnionBank" or the "Bank") is a publicly-listed universal bank. The Bank distinguishes itself through superior technology, unique branch sales and service culture, and centralized backroom operations. UnionBank's superior technology allows delivery of online, real time business solutions to meet the customers' changing and diverse needs through innovative and customized cash management products and service offerings. The Bank's unique branch sales and service culture ensures efficient and quality service as well as mitigates operational risk. Its distinct centralized backroom operations enables the Bank to provide responsive, scalable, and secure transaction processing.

Aligned with its thrust of being at the forefront of technology-based banking in the Philippines, the Bank endeavors to elevate its systems and processes to be at par with international standards and best practices. It obtained ISO 9001:2000 Quality Management System ("QMS") Certification for its Central Processing Services ("CPS") in 2008, making it then the FIRST and ONLY bank awarded for its entire centralized backroom operations. In 2010, the Bank received ISO 9001:2008 certification, an upgrade from the previous. Thereafter, UnionBank was certified for ISO 27001:2005 Information Security Management System, attesting to the Bank's unwavering commitment to become an acknowledged leader and benchmark for service quality, technological advancement, and operational excellence. The Bank also achieved ISO 9001:2008 certifications for its Customer Service Group in 2012 and Branch Operations Management in 2013, and has consistently been certified as having zero non-conformance every year from date of certification during quality audits, demonstrating the Bank's dedication to uphold quality in its business processes.

Notwithstanding volatility in trading-related earnings, the Bank has a proven track record for delivering consistent and strong performance from treasury businesses. Gains from the Bank's treasury businesses have historically accounted for a significant and consistent portion of the Bank's operating income.

UnionBank's clientele encompasses retail, middle-market and corporate customers, as well as major government institutions. The Bank believes that its use of technology, and marketing and operational structure has enabled it to capture and secure a loyal customer base, and to achieve high levels of efficiency and productivity.

The Bank's consolidated total assets amounted to ₱279.7 billion as of December 31, 2012 and reached ₱340.6 billion as of June 30, 2013. Net income was ₱7.6 billion for the year ended December 31, 2012 and ₱6.2 billion for the six months ended June 30, 2013. The Bank's Tier 1 and Total Capital Adequacy Ratios remained greater than the minimum ten percent (10.0%) regulatory requirement, ending the year 2012 at 18.0% and 20.7%, respectively. As of June 30, 2013, the Bank continued to exhibit above industry performance on key financial ratios, with return on shareholders' equity, return on assets and cost-to-income ratios at 26.7%, 4.0% and 44.9%, respectively. Based on consolidated quarterly reports filed with the Philippine Securites and Exchange Commission ("SEC"), the Bank's return on assets and return on shareholders' equity were the highest, and its cost-to-income ratio was the second most efficient, among private domestic commercial banks in the Philippines.

The authorized share capital of the Bank is 670,000,000 shares with a par value of ₱10.0 each. As of June 30, 2013, there were 641,422,420 issued and outstanding common shares, fully paid. Based on the closing price of its shares on the Philippine Stock Exchange ("PSE") on June 28, 2013, the Bank had a market capitalization of approximately ₱89.5 billion.

The Bank provides its relevant target customers' information and transaction needs through its consolidated network of 229 strategically located branches and 267 automated teller machines ("ATMs") nationwide as of June 30, 2013, supplemented by a call center under the Bank's ISO-certified Customer Service Group. To complement its brick and mortar presence and strengthen its digital footprint, UnionBank has a Web site, www.unionbankph.com.

Competitive Strengths

The Bank considers the following to be its principal competitive strengths:

- Superior technology,
- Unique branch sales and service culture,
- Centralized backroom operations; and
- Consistent and strong performance from Treasury businesses.

Business Strategy

The Bank's corporate vision is to become one of the top three (3) universal banks in the Philippines in respect to market capitalization, profits and customer coverage, grounded on its purpose of "Making the Diff" by connecting and enabling communities through Smart Banking in the spirit of UBUNTU, which means community building. To achieve this vision, UnionBank has adopted five (5) key strategic imperatives, referred to as "FOCUS", which is an acronym for the following:

- Financial Value: Enhance the financial value of the Bank's operations;
- Operational Excellence: Increase productivity while reducing costs;
- Customer Franchise: Increase customer base and reduce customer attrition;
- UnionBank Brand/Experience: Establish a unique brand image in strategic markets; and
- Superior Innovation: Continue to offer innovative products and services.

The Bank will continue to selectively consider opportunities for acquisitions as they arise in order to support its growth under its FOCUS strategy.

Bank Information

The Bank's registered office is located at UnionBank Plaza, Meralco Avenue corner Onyx & Sapphire Roads, Ortigas Center, Pasig City 1605, Philippines. The Bank's telephone number is +(632) 667-6388 and its corporate Web site is www.unionbankph.com. The information on the Bank's Web site is not incorporated by reference into, and does not constitute part of, this Preliminary Offering Circular.

SUMMARY OF THE OFFERING

HSBC in its capacity as Sole Lead Arranger has agreed with the Bank, subject to the satisfaction of certain conditions, to distribute and sell the LTNCDs at the Issue Price (defined below) in consideration for certain fees and expenses. The Sole Lead Arranger will offer the LTNCDs to selected prospective LTNCD Holders.

The distribution and sale of the LTNCDs to prospective LTNCD Holders shall be undertaken by the Sole Lead Arranger and the Selling Agents for the issue. Nothing herein shall limit the right of the Sole Lead Arranger to purchase the LTNCDs for its own account. The Sole Lead Arranger may, from time to time, engage in transactions with and perform services for the Bank or its shareholders or affiliates in the ordinary course of its business.

The following is a general summary of the terms of the LTNCDs. This summary is derived from and should be read in conjunction with the full text of the Terms and Conditions of the LTNCDs (the "Terms and Conditions"). The Terms and Conditions shall prevail in the event of any inconsistency with the terms set out in this section.

ISSUER	Union Bank of the Philippines
CDs OFFERED	*Fixed Rate Long Term Negotiable Certificates of Time Deposits*
DENOMINATION	Minimum of ₱250,000.00 per Certificate, and increments of ₱50,000.00 beyond the minimum.
ISSUE PRICE	100% of the face value of each Certificate.
INTEREST RATE	[●]% *per annum*, payable to the Holder for the period from and including the Issue Date up to, but excluding, the Maturity Date.
ISSUE DATE	[●] 2013
MATURITY DATE	The last day of the twenty-second (22nd) Interest Period, as specified in the Terms and Conditions.
MATURITY VALUE	The LTNCDs will be redeemed on Maturity Date at their face value plus unpaid accrued applicable Interest.
OFFER PERIOD	[●] to [●]
FORM	The LTNCDs will be issued scripless and will be maintained in electronic form with the Registrar, subject to the payment of fees to the Registrar and in compliance with the provisions of Republic Act No. 8792, otherwise known as the Electronic Commerce Act, particularly on the existence of an assurance on the integrity, reliability, and authenticity of the LTNCDs in electronic form. The LTNCDs shall be registered in the name of individuals or corporations, are negotiable and pre-numbered serially. A Registry Confirmation will be issued by the Registrar in favor of the Holders in accordance with the BSP Rules.
INTEREST ACCRUAL	The face value of the LTNCD multiplied by the Interest Rate calculated on the basis of a three hundred and sixty (360)-day year consisting of twelve (12) months of thirty (30) days each month.
INTEREST PERIODS	Consecutive three (3) calendar month period reckoned from the Issue Date up to the numerically same day of the third (3rd) month from Issue Date, and every succeeding three (3) calendar month periods beginning on the last day of the prior period up to the numerically same day of every third (3rd) month thereafter, until the Maturity Date.

INTEREST PAYMENT DATE	The last day of an Interest Period, subject to the Modified Business Day Convention, except for the last Interest Payment Date which shall fall on the Maturity Date.
PRINCIPAL REPAYMENT	Any payment of principal or interest under the LTNCDs shall be made to the Holders through the Paying Agent.
NON-PRETERMINABILITY	The LTNCDs shall not be redeemable or terminable at the instance of any Holder before Maturity Date. However, negotiation or transfer from one holder to another is allowed and shall not constitute pretermination of the Certificate.
STATUS AND PDIC INSURANCE	The LTNCDs constitute direct, unconditional, unsecured, and unsubordinated peso-denominated obligations of the Issuer, enforceable according to these Terms and Conditions. The LTNCDs shall be insured with the PDIC, subject to applicable rules and regulations.
TAXATION	The Market Makers and/or Registrar may, unless properly provided with satisfactory proof of the tax-exempt status of a Holder, assume that said Holder is taxable and proceed to apply the tax due on the LTNCDs. LTNCD Holders who are individual citizens, resident aliens and non-resident aliens engaged in trade and business in the Philippines who shall hold on to the LTNCDs for at least five (5) years shall be exempt from the twenty percent (20.0%) final withholding tax.
GOVERNING LAW	Laws of the Republic of the Philippines
GOVERNING REGULATIONS	Securities Regulation Code (Republic Act No. 8799), the Revised Implementing Rules and Regulations to the Securities Regulation Code, General Banking Law of 2000 (Republic Act No. 8791), the New Central Bank Act (Republic Act No. 7653), Manual of Regulations for Banks updated as of December 2011, BSP Circular No. 778, which govern the issuance of long term negotiable certificates of time deposit, and other related circulars and issuances, as these may be amended from time to time
INVESTMENT CONSIDERATIONS	These relate to considerations relating to the: Bank; Philippine Banking Industry; and the LTNCDs. (See discussion on Investment Considerations.)
SOLE LEAD ARRANGER	The Hongkong and Shanghai Banking Corporation Limited
SELLING AGENTS	Union Bank of the Philippines, The Hongkong and Shanghai Banking Corporation Limited, and Multinational Investment Bancorporation.
REGISTRAR AND PAYING AGENT	Deutsche Bank AG, Manila Branch - Direct Securities Services
MARKET MAKER	The Hongkong and Shanghai Banking Corporation Limited and Multinational Investment Bancorporation.
BANKING DAY	Any day in a week, other than Saturday or Sunday, when banks are not required or authorized to close in Pasig City and Manila.

SUMMARY CONSOLIDATED FINANCIAL INFORMATION

The following tables present selected consolidated financial information of the Bank and should be read in conjunction with the consolidated financial statements and the related notes included elsewhere in this Offering Circular. The selected financial information presented below as of and for the years ended December 31, 2010, 2011, and 2012 were derived from the consolidated financial statements prepared in accordance with financial reporting standards in the Philippines for banks which include Philippine Financial Reporting Standards ("PFRS"), as discussed in Note 2 to the Bank's financial statements, and audited by Punongbayan & Araullo ("P&A") in accordance with Philippine Standards on Auditing. The selected financial information as of and for the six months ended June 30, 2012 and 2013 were derived from the unaudited interim consolidated financial statements of the Bank, prepared in accordance with Philippine Accounting Standards ("PAS") PAS 34, Interim Financial Reporting and reviewed by P&A in accordance with Philippine Standard on Review Engagement 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" (PSRE 2410). The selected financial information set out below does not purport to project the consolidated results of operations or financial position of the Bank for any future period or date.

	Audited			Unaudited	
	For the year ended December 31			For the six months ended June 30	
	2010	2011	2012	2012	2013
			(₱ in millions)		
INTEREST INCOME ON					
Loans and other receivables	6,374.5	6,875.6	6,984.1	3,480.3	4,060.4
Trading and investments securities	4,362.2	4,011.1	3,745.2	2,081.4	1,811.6
Cash and cash equivalents	1,023.0	831.6	113.8	102.5	501.2
Interbank loans receivables	53.3	32.1	24.8	14.8	9.7
	11,813.1	**11,750.4**	**10,867.9**	**5,679.0**	**6,382.8**
INTEREST EXPENSE ON					
Deposit liabilities	4,289.7	4,349.4	3,182.9	1,838.3	1,973.4
Bills payable and other liabilities	449.1	417.8	373.3	171.5	346.1
	4,738.8	**4,767.3**	**3,556.2**	**2,009.8**	**2,319.5**
NET INTEREST INCOME	**7,074.2**	**6,983.2**	**7,311.6**	**3,669.2**	**4,063.3**
IMPAIRMENT LOSSES	**524.5**	**1,549.6**	**1,559.8**	**260.1**	**369.6**
NET INTEREST INCOME AFTER IMPAIRMENT LOSSES	**6,549.8**	**5,433.6**	**5,751.8**	**3,409.1**	**3,693.7**
OTHER INCOME					
Trading gain-net	2,851.9	5,401.5	6,472.8	3,289.0	5,613.2
Premium revenues	281.5	1,387.3	1,243.0	1,078.6	1,003.7
Service charges, fees and commissions	682.1	846.6	861.6	378.5	1,001.6
Miscellaneous	2,319.3	1,922.6	2,253.4	823.4	1,091.6
	6,134.8	**9,558.0**	**10,830.9**	**5,569.4**	**8,710.1**
OTHER EXPENSES					
Salaries and employee benefits	2,451.7	2,958.6	3,304.1	1,648.0	2,082.6
Trust fund due	262.3	1,304.1	1,168.9	1,014.3	942.9
Taxes and licenses	796.1	830.3	998.2	512.8	937.3
Occupancy	509.6	545.5	553.7	278.3	302.7
Depreciation and amortization	373.0	357.8	351.5	174.9	225.4
Miscellaneous	2,105.5	2,185.5	2,293.0	1,044.3	1,239.9
	6,498.2	**8,181.7**	**8,669.3**	**4,672.6**	**5,730.8**
PROFIT BEFORE TAXES	**6,186.5**	**6,809.9**	**7,913.4**	**4,305.9**	**6,673.0**
TAX EXPENSE	**833.2**	**214.5**	**328.0**	**238.6**	**481.2**
NET PROFIT	**5,353.3**	**6,595.4**	**7,585.4**	**4,067.3**	**6,191.8**

	Audited			Unaudited	
	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
			(₱ in millions)		
Cash and Other Cash Items	4,178.0	3,686.9	4,242.4	3,217.2	3,836.2
Due from Bangko Sentral ng Pilipinas	42,524.0	28,771.9	27,450.3	28,670.4	91,927.4
Due from Other Banks	1,760.1	3,213.7	2,999.3	3,765.8	2,919.3
Interbank Loans Receivable	7,470.5	12,989.1	5,503.5	2,792.4	13,062.7
Trading and Investment Securities	75,475.3	90,014.4	88,955.8	90,496.2	92,819.6
At fair value through profit or loss	5,997.3	270.9	397.5	811.8	321.0
Available-for-sale financial assets-net	33,812.8	89,743.5	88,558.3	89,684.4	92,498.6
Held-to-maturity investments-net	35,665.2	-	-	-	-
Loans and Other Receivables-net	95,031.7	105,011.2	119,716.6	87,502.7	99,751.3
Bank Premises, Furniture, Fixtures and Equipment-net	2,862.6	2,769.6	3,105.8	2,904.7	3,308.1
Assets Held for Sale	137.5	198.1	397.5	253.3	504.7
Investment Properties	12,382.2	12,167.0	11,555.1	11,293.7	12,047.3
Goodwill	7,886.9	7,886.9	7,886.9	7,886.9	11,258.3
Other Resources-net	4,074.7	5,920.1	7,931.9	3,692.7	9,205.5
TOTAL RESOURCES	**253,783.3**	**272,628.9**	**279,745.0**	**242,476.1**	**340,640.4**
Deposit Liabilities	193,319.5	206,653.3	189,841.4	168,813.5	259,546.1
Demand	109,468.2	114,752.3	62,811.7	72,728.7	87,824.4
Savings	25,208.4	22,521.9	23,868.7	17,817.4	25,418.6
Time	58,642.9	69,379.2	103,160.9	78,267.3	146,303.1
Bills Payable	7,396.3	5,619.2	18,541.3	13,254.8	15,208.0
Notes Payable	5,037.1	3,750.0	3,750.0	3,750.0	3,750.0
Other Liabilities	12,045.1	13,767.3	19,765.1	13,324.3	17,102.6
TOTAL LIABILITIES	**217,798.0**	**229,789.9**	**231,897.7**	**199,142.5**	**295,606.7**
TOTAL CAPITAL FUNDS	**35,985.4**	**42,839.0**	**47,847.2**	**43,333.5**	**45,033.7**
Common Stock	6,414.2	6,414.2	6,414.2	6,414.2	6,414.2
Additional Paid-in Capital	5,819.9	5,819.9	5,819.9	5,819.9	5,819.9
Surplus Free	23,033.4	28,011.3	33,656.9	30,152.5	37,602.2
Surplus Reserves	120.2	134.2	149.6	134.2	149.6
Net Unrealized Gains (Losses) on Available-for-sale Financial Assets	597.7	2,459.5	1,806.6	812.8	(4,964.7)
Non-controlling Interests	-	-	-	-	12.4
TOTAL LIABILITIES AND CAPITAL FUNDS	**253,783.3**	**272,628.9**	**279,745.0**	**242,476.1**	**340,640.5**

	Audited			Unaudited	
	For the year ended December 31			For the six months ended June 30	
	2010	2011	2012	2012	2013
Return on assets	2.2%	2.5%	3.0%	3.2%	4.0%
Return on shareholders' equity	15.5%	16.7%	17.0%	18.8%	26.7%
Net interest margin	3.5%	3.1%	3.5%	3.4%	3.4%
Cost-to-income ratio	49.2%	49.5%	47.8%	50.6%	44.9%
Net loans and other receivables-to-deposits	49.2%	50.8%	63.1%	51.8%	38.4%
Tier I capital adequacy ratio	13.3%	15.3%	18.0%	15.9%	16.7%
Total capital adequacy ratio	17.0%	18.2%	20.7%	18.6%	19.5%
Total equity-to-total assets	14.2%	15.7%	17.1%	17.9%	13.2%
Total non-performing loans-to-total loans – excluding interbank loans	5.3%	3.2%	3.5%	3.8%	(0.2%)
Total non-performing loans-to-total loans – including interbank loans	4.8%	2.8%	3.3%	3.7%	(0.2%)
Allowances for probable loan losses to total loans	11.4%	10.6%	11.7%	10.5%	10.5%
Allowances for probable loan losses-to-total non-performing loans	93.1%	100.6%	104.2%	97.2%	112.6%
Earnings per share (₱)	8.35	10.28	11.83	12.68	19.31

INVESTMENT CONSIDERATIONS

An investment in the LTNCDs involves a number of investment considerations. You should carefully consider all the information contained in this Preliminary Offering Circular including the investment considerations described below, before any decision is made to invest in the LTNCDs. The Bank's business, financial condition and results of operations could be materially and adversely affected by any of these investment considerations. The market price of the LTNCDs could decline due to any one of these risks, and all or part of an investment in the LTNCDs could be lost.

The following discussion is not intended to be a comprehensive description of the risks and other factors and is not in any way meant to be exhaustive. Prospective LTNCD Holders are encouraged to make their own independent legal, tax, financial, and business examination of the Bank, the LTNCDs, and the market. Neither the Bank nor the Sole Lead Arranger make any warranty or representation on the marketability or price on any investment in the LTNCDs.

Considerations Relating to the Bank

The Bank may not be successful in implementing its strategies.

UnionBank's long-term FOCUS strategy is principally about leveraging - leveraging its capital, branch network, corporate relationships, process and brand. The Bank intends to achieve retail-based asset build-up and a more cost-effective funding base, anchored on its thrust on broadening customer base and deepen relationships through innovative product and service offerings.

Growth strategy

The Bank's growth strategy contemplates, among other things, organic growth and growth through acquisitions. As part of its acquisition strategy, the Bank regularly evaluates potential acquisition targets, and may in the future seek to acquire other businesses to expand its operations.

UnionBank has undertaken two bank mergers with International Corporate Bank ("Interbank") in 1993 and International Exchange Bank ("iBank") in 2006, catapulting it to being one of the 10 largest universal banks in the Philippines based on asset size.

On January 8, 2013, UnionBank's Board of Directors ("BOD") approved the purchase of City Savings Bank, Inc. ("CitySavings"), a premier thrift bank specializing in granting teachers' loans under the Department of Education's ("DepEd") Automatic Payroll Deduction System ("APDS"). The acquisition is in accordance with the UnionBank's business plan and aligned with management's long-term strategy of building asset businesses based on consumers. It will complement UnionBank's business operations, financial condition and performance as this provides the following:

- Potential to be one of UnionBank's highest earning customer business segment;
- Potential to apply the current teachers' loan business model to other civil servant market segments;
- Opportunity for UnionBank and CitySavings to complement each other's management strengths, augment technological skills, leverage financial capabilities, and, ultimately, maximize value for all stakeholders; and
- Significant impact on industry standing.

As of June 30, 2013, the Bank had consolidated total assets of ₱340.6 billion, total deposits of ₱259.5 billion and loan portfolio of ₱104.1 billion, expanding by 21.8%, 36.7% and 14.3%, respectively, from December 31, 2012.

There can be no assurance that the Bank will not experience difficulties integrating acquired businesses, retaining and integrating key employees of acquired companies, or addressing new business risks not currently faced by the Bank. If general economic and regulatory conditions or market and competitive conditions change, or if operations do not generate sufficient funds or other unexpected events occur, the Bank may decide to delay, modify or forego some aspects of its growth strategies, and this could have an adverse effect on the Bank's financial condition and results of operations as well as its future growth prospects.

In addition, completing acquisitions could require use of a significant amount of the Bank's available cash. Acquisitions and investments may also have negative effects on the Bank's reported results of operations due to acquisition related charges, amortization of acquired technology and other intangibles, and/or actual or potential liabilities, known and unknown, associated with the acquired businesses or joint ventures. Any of these acquisition related risks or costs could adversely affect the Bank's business, financial condition and results of operations.

Business strategy

The Bank's business strategy includes expanding the range of its products and services to diversify its revenue sources and to solidify its strong foothold on its established franchises further widening its loyal customer base. For example, the Bank has targeted the retail and middle-market banking segments as key areas for growth. Expanding the Bank's business activities to increase the number of financial products and services that it offers exposes the Bank to a number of risks and challenges including, among others, the following:

- new and expanded business activities may require greater marketing and compliance costs than the Bank's traditional services;
- new and expanded business activities may have less growth or profit potential than the Bank anticipates and there can be no assurance that new business activities will become profitable at the level the Bank desires or at all;
- the Bank may fail to identify and offer attractive new services in a timely fashion, putting it at a disadvantage to competitors;
- the Bank's competitors may have substantially greater experience and resources for the new and expanded business activities and thus the Bank may not be able to attract customers from its competitors;
- the Bank may need to enhance the capability of its information technology systems to support a broader range of activities; and
- economic conditions, such as rising interest rates or inflation, could hinder the Bank's expansion, particularly in the consumer loan industry.

In addition, new business endeavors may require knowledge and expertise which differ from those used in the current business operations of the Bank, including different management skills, risk management procedures, guidelines and systems, credit appraisal, monitoring and recovery systems. The Bank may not be successful in developing such knowledge and expertise. Furthermore, managing such growth and expansion requires significant managerial and operational resources, which the Bank may not be able to procure on a timely basis or at all. The Bank's inability to implement its business strategy could have a material adverse effect on its business, financial condition and results of operations.

The business of lending carries the risk of default by borrowers and the Bank may face increasing levels of NPLs and provisions for impairment losses on loans.

Any lending activity is exposed to credit risk arising from the risk of default by borrowers. The Bank's results of operations may potentially be negatively affected by the level of its non-performing loans ("NPLs"). For the years ended December 31, 2010, 2011 and 2012, and for the six months ended June 30, 2012 and 2013, the Bank's provisions for impairment amounted to ₱524.5 million, ₱1.5 billion, ₱1.6 billion, ₱260.1 million and ₱369.6 million, respectively, representing approximately 7.4%, 22.2%, 21.3%, 7.1% and 9.1%, respectively, of net interest income for these periods. A number of factors affect the Bank's ability to control and reduce its NPLs, such as ongoing volatile economic conditions in the Philippines, which continue to adversely affect many of the Bank's customers, causing uncertainty regarding their ability to fulfill their loan obligations, thus significantly increasing the Bank's exposure to credit risk. These and other factors could result in an increased number of NPLs in the future and would require the Bank to book additional provisions for impairment on loans. While the Bank regularly monitors its NPL levels and has strict credit processes in place, there can be no assurance that the Bank will be successful in reducing its NPL levels or that the percentage of NPLs that the Bank will be able to recover will be similar to the Bank's historical recovery rates or that the overall quality of its loan portfolio will not deteriorate in the future. If the Bank is not able to control and reduce its NPLs or if there is a significant increase in its provisions for loan losses, the Bank's business, financial condition, results of operations and capital adequacy could be adversely affected.

The Bank's provisioning policies in respect of classified loans require significant subjective determinations which may increase the variation of application of such policies and affect the Bank's results of operations. Such policies may also be less stringent than those in other countries.

Regulations of the BSP require that Philippine banks classify loans that have a greater-than-normal risk into four (4) different categories corresponding to various levels of credit risk as follows: loans especially mentioned, substandard, doubtful and loss. Generally, the classification of loans depends on a combination of a number of qualitative and quantitative factors, such as the number of months that payment is in arrears, the type of loan, the terms of the loan and the level of collateral coverage. These requirements have in the past been changed by the BSP. Periodic examination by the BSP of these classifications in the future may also result in changes being made by the Bank to such classifications and to the factors relevant thereto. As part of its move to compliance with PFRS/PAS, in 2005, the Bank re-evaluated its NPLs and its collateral by the present value of the expected future cash flows realizable from its loans in estimating allowance for impairment.

In addition, the BSP requirements in certain circumstances may be less stringent than those applicable to banks in other countries and may result in particular loans being classified as non-performing later than would be required in such countries or being classified in a category reflecting a lower degree of risk. As a result, the amount of the Bank's NPLs as well as reserves may be lower than what would be required if the Bank were located in such countries. Further, if the Bank changes its provisioning policies to become more in line with international standards or practices or otherwise, the Bank's results of operations may be adversely affected.

Increased exposure to consumer debt could result in increased delinquencies in the Bank's loan portfolios.

The Bank has expanded and plans to continue to expand its consumer loan operations. Such expansions increase the Bank's exposure to consumer debt and changes in general economic conditions affecting Philippine consumers. Accordingly, economic difficulties in the Philippines that have a significant adverse effect on Philippine consumers could result in reduced growth and deterioration in the credit quality of the Bank's consumer loan portfolios. For example, a rise in unemployment or an increase in interest rates could have an adverse impact on the ability of borrowers to make payments and increase the likelihood of potential defaults, while reducing demand for consumer loans. In addition, the number of loan accounts may be negatively affected by declines in household income, public concerns about unemployment or other negative macroeconomic factors.

The Bank may be unable to recover the assessed value of its collateral when its borrowers default on their obligations, which may expose the Bank to significant losses.

The recorded values of the Bank's collateral may not accurately reflect its liquidation value, which is the maximum amount the Bank is likely to recover from a sale of collateral, less expenses of such sale. There can be no assurance that the realized value of the collateral would be adequate to cover the Bank's loans. An economic downturn, in particular, a downturn in the real estate market, could result in a fall in relevant collateral values for the Bank. Some of the valuations in respect of the Bank's collateral may also be out of date or may not accurately reflect the value of the collateral. In certain instances, where there are no purchasers for a particular type of collateral, there may be significant difficulties in disposing of such collateral at a reasonable price. Any decline in the value of the collateral securing the Bank's loans, including with respect to any future collateral taken by the Bank, would mean that its loan loss provisions may be inadequate and the Bank may need to increase such provisions. There can be no assurance that the collateral securing any particular loan will protect the Bank from suffering a partial or complete loss if the loan becomes non-performing. Any increase in the Bank's loan loss provisions would adversely affect its business, its financial condition, results of operations and capital adequacy ratio.

In addition, the Bank may not be able to recover in full the value of any collateral or enforce any guarantee due, in part, to difficulties and delays involved in enforcing such obligations through the Philippine legal system. To foreclose on collateral or enforce a guarantee, banks in the Philippines are required to follow certain procedures specified by Philippine law. These procedures are subject to administrative and bankruptcy law requirements which may be more burdensome than in certain other jurisdictions. The resulting delays can last several years and lead to the deterioration in the physical condition and market value of the collateral, particularly where the collateral is in the form of inventory or receivables. In addition, such collateral may not be insured. These factors have exposed, and may continue to expose, the Bank to legal liability while in possession of the collateral. These factors may also significantly reduce the Bank's ability to realize the value of its collateral and therefore the effectiveness of taking security for the loans it grants. Furthermore, the Bank may incur expenses to maintain such properties and prevent their deterioration. In realizing cash value for such properties, the Bank may incur further expenses such as legal fees and taxes associated with such realization.

The Bank has significant credit exposure to certain borrowers and industries. In particular, the Bank has a high exposure to the Philippine property market through its ROPA portfolio and its lending to customers in the real estate industry. A deterioration in the performance of any of these industry sectors or if a substantial portion of these loans were to become non-performing, may adversely impact the asset quality of the Bank's loan portfolio and business.

The Bank's three (3) largest industry exposures were to real estate, renting and business services; other community, social & personal services; agricultural, hunting & forestry (shown as part of Others in loans by economic activity under the section on Assets and Liabilities – Loan Portfolio), representing 24.1%, 18.4% and 14.6%, respectively, of the Bank's total loan portfolio as of June 30, 2013. The global and domestic trends in these industries may have a bearing on the Bank's financial position. Any significant deterioration in the performance of a particular sector, driven by events outside the Bank's control, such as regulatory action or policy announcements by the Government or the general condition of the domestic and global economies, would adversely impact the ability of borrowers in that industry to service their debt obligations to the Bank. In addition, if the loans to these borrowers or sectors were to become non-performing, this could adversely affect the Bank's business and results of operations.

The Bank has significant exposure to the Philippine property market due to the level of its holdings in real and other properties acquired ("ROPA"). The Bank acquires ROPA when it forecloses on the collateral provided by a borrower. Accordingly, the level of the Bank's ROPA varies according to the level of its NPLs. As of June 30, 2013, ROPA amounted to approximately ₱10.3 billion, representing 3.0% of the Bank's total assets. The Bank periodically disposes of its ROPA in public auctions and through negotiated sales at prevailing market prices, which are largely determined by purchasers. The Philippine property market has in the past been cyclical and property values have been affected by supply of and demand for comparable properties, the rate of economic growth in the Philippines and political and social developments.

To the extent that property values decline in the future, there can be no assurance that the Bank will be able to sell and recover the value of the ROPA stated in the financial statements or that the ability of the Bank's customers in the real estate industry to make timely payment on their loans will not deteriorate.

The Bank's funding is primarily short-term and if depositors do not roll over deposited funds upon maturity, the Bank's business could be adversely affected.

A significant portion of the Bank's funding needs is satisfied from short-term sources, primarily in the form of demand, savings and time deposits. Accordingly, the maturity profile of the Bank's assets and liabilities may from time to time show a negative gap in the short term when the Bank's liabilities which are composed of short-term funding sources (primarily in the form of deposits), subordinated notes and other liabilities are of shorter average maturity than its loans and investments, thereby creating a potential for funding mismatches. Although these deposits have historically been a stable source of funding for the Bank, no assurance can be given that this will continue to be the case. In the event the Bank is unable to attract or retain sufficient deposits or if a substantial number of the Bank's depositors do not roll over deposited funds upon maturity, its liquidity position could be adversely affected and the Bank may be unable to fund its loan portfolio and may be required to seek alternative sources of funding such as swaps, sale of its securities portfolio or entering into repurchase agreements. The Bank can provide no assurance as to the availability or terms of such funding. To the extent the Bank is unable to obtain sufficient funding on acceptable terms or at all, the Bank's financial condition and results of operations may be adversely affected.

The Bank may not be able to maintain its technological advantage over its competitors or its brand image of being a "high-tech" service bank.

The Bank is heavily reliant on technology in certain business operations and uses technology to differentiate its products and services from those of its competitors. The Bank believes that the products and services it offers are more technologically advanced than its competitors and that these products and services have shaped its image of being a "high-tech" service bank.

The Bank has a dedicated team that endeavors to research and develop new technology enablers to support the Bank's High Tech, High Touch strategy. As a metric for evaluating its success in continuously offering innovative products and services, the Bank has defined and adopted an innovation index which targets at least 25.0% of net customer revenues to come from products not more than three (3) years old. Acknowledging its reliance on technology, as part of the Bank's business continuity plan, the Bank undertook a Mirroring project in 2007. It is a major Information Technology initiative which mirrors the two sites of the Bank for its failover scheme to achieve disaster readiness. It is a resilient and dynamic technology on data replication, offering flexibility in choosing between the Bank's data centers in capturing real time transactions. This is a first in the Philippine banking industry, attesting to the Bank's commitment to remain at the forefront of technology.

While the Bank aims to remain at the forefront of technology banking in the Philippines, there are no significant barriers that prevent its competitors from adopting a similar technology for their products and services. Accordingly, there can be no assurance that the Bank will be able to maintain its technological advantage over its competitors or its brand image of being a "high-tech" service bank. Furthermore, the Bank may need to incur a significant amount of research and development and/or capital expenditures to maintain its technological advantage. For the year ended December 31, 2012, the amount spent by the Bank on research and development activities amounted to ₱461.3 million representing 2.5% of 2012 revenues while for the six months ended June 30, 2013, the Bank spent ₱265.5 million which represents 2.1% of the revenues for the same period. Failure to maintain its technological advantage or its brand image may have a material adverse impact on its fee-based revenue and its ability to attract new deposits from affluent retail and corporate customers, which in turn may lead to an increase in costs of funding and a loss of business, and result in a material adverse effect on the Bank's business, financial condition or its results of operations.

The Bank's failure to manage risks associated with its information and technology systems could adversely affect its business.

The Bank is subject to risks relating to its information and technology systems and processes. The hardware and software used by the Bank in its information technology is vulnerable to damage or interruption by human error, misconduct, malfunction, natural disasters, power loss, sabotage, computer viruses or the interruption or loss of support services from third parties such as internet service providers, ATM operators and telephone companies. Any disruption, outage, delay or other difficulties experienced by any of these information and technology systems could result in delays, disruptions, losses or errors that may result in loss of income and decreased consumer confidence in the Bank. These may, in turn, adversely affect the Bank's business, financial condition and results of operations.

The Bank has invested heavily in protecting its computer systems and network infrastructure from systems breakdowns in order to minimize any down time which may be experienced by end users. The Bank has also been working on minimizing electronic break-ins as well as security breaches and other disruptive problems caused by the Bank's increased use of the internet. Computer break-ins and security breaches could affect the security of information stored in and transmitted through these computer systems and network infrastructure. Cognizant that security is an on-going and continuous endeavor to improve the electronic defenses, UnionBank has a five (5)-year strategic plan to address the security requirements based on the audit of both foreign and local consultants who are experts in the field of information security. The Bank employs security systems, including firewalls, intrusion prevention systems and password encryption, designed to minimise the risk of security breaches and maintains operational procedures to prevent break-ins, damage and failures. The potential for fraud and securities problems is likely to persist and there can be no assurance that these security measures will be adequate or successful. The costs of maintaining such security measures may also increase substantially. Failure in security measures could have a material adverse effect on the Bank's business, financial condition and results of operations.

The Bank is subject to foreign currency risk and interest rate risk.

As a financial organization, the Bank is exposed to exchange rate risk. Movements in foreign exchange rates could adversely affect the Bank's business and results of operations. The foreign exchange transactions of Philippine banks are subject to stringent BSP regulation. Under BSP guidelines, the Bank is required to provide a hundred percent (100.0%) foreign asset cover for all foreign currency liabilities in its foreign currency deposit unit ("FCDU") books. The decline in the value of the peso against foreign currencies, in particular, the U.S. dollar may affect the ability of the Bank's customers or the Government to service debt obligations denominated in foreign currencies and, consequently, increase NPLs. Conversely, increases in the value of the peso can depress the export market which can negatively affect the ability of the Bank's customers to repay their debt obligations or may reduce credit quality or demand. There can be no assurance that the peso will not fluctuate further against other currencies and that such fluctuations will not ultimately have an adverse effect on the Bank.

The Bank realizes income from the margin between interest-bearing assets, such as investments and loans, and on interest-bearing liabilities, such as deposits and borrowings. The business of the Bank is subject to fluctuations in market interest rates as a result of mismatches in the re-pricing of assets and liabilities. These interest rate fluctuations are neither predictable nor controllable and may have a material adverse impact on the operations and financial condition of the Bank. In a rising interest rate environment, if the Bank is not able to pass along higher interest costs to its customers, it may negatively affect the Bank's profitability. If such increased costs are passed along to customers, such increased rates may make loans less attractive to potential customers and result in a reduction in customer volume and hence operating revenues. In a decreasing interest rate environment, potential competitors may find it easier to enter the markets in which the Bank operates and to benefit from wider spreads. As a result, fluctuations in interest rates could have an adverse effect on the Bank's margins and volumes and in turn adversely affect the Bank's business, financial condition and results of operations.

The Bank relies on certain key personnel and the loss of any such key personnel or the inability to attract and retain them may negatively affect its business.

The Bank's continued success depends upon, among other factors, the retention of its key management executives and upon its ability to attract and retain other highly capable individuals. The Bank has leadership development and retention programs, one of which is called the Leadership Assessment Development Deployment and Retention or LADDER that ensures structures are in place to increase retention among key management executives, attract talent from external sources and develop talent from within to increase the leadership bench strength in order to address the business needs now and in the future. Having such programs in place potentially reduces the impact of key personnel movements that could materially affect the Bank's business, financial condition and results of operations. The Bank has a succession plan in place. This ensures that business continuity is achieved even if a key personnel is separated from employment with the Bank. These programs are regularly reviewed with the Center Heads and at Board Committee level under the Compensation and Remuneration Committee.

The Bank's business, reputation and prospects may be adversely affected if the Bank is not able to detect and prevent fraud or other misconduct committed by the Bank's employees or outsiders on a timely basis.

The Bank is exposed to the risk that fraud and other misconduct committed by employees or outsiders could occur. Such incidences may adversely affect banks and financial institutions more significantly than companies in other industries due to the large amounts of cash that flow through their systems. Any occurrence of such fraudulent events may damage the reputation of the Bank and may adversely affect its business, financial condition, results of operations and prospects. In addition, failure on the part of the Bank to prevent such fraudulent actions may result in administrative or other regulatory sanctions by the BSP or other Government agencies, which may be in the form of suspension or other limitations placed on the Bank's banking and other business activities. Thus, the Bank has various structures in place that are set-up to detect and prevent fraud and other misconduct committed by the Bank's employees or outsiders on a timely basis such as:

- Money laundering detection and reporting processes;
- Debit and credit card fraud detection and mitigation processes;
- Intrusion prevention system and other security tools;
- An Anti-Fraud Unit that identifies and investigates suspicious transactions;
- A fraud unit within the Internal Audit Division that continuously conducts assessments of potential risk areas;
- Separation of sales and marketing and operations function in branches provides the necessary check and balances to ensure compliance and prevent fraud;
- Strong coordination between Operational Units and Operations Risk Management Unit in the conduct of risk assessment on critical processes and services of the Bank;
- A policy and process set up under the Code of Conduct of the Bank that allows for any employee to make a report on misconduct that violates the code; and

- Continuous and mandatory training for employees in the areas of risk and fraud under the UnionBank University's Risk Academy and Operations Academy.

The Bank is involved in litigation, which could result in financial losses or harm its business.

The Bank is and may in the future be, implicated in lawsuits on an ongoing basis. Litigation could result in substantial costs to, and a diversion of effort by, the Bank and/or subject the Bank to significant liabilities to third parties. There can be no assurance that the results of such legal proceedings will not materially harm the Bank's business, reputation or standing in the marketplace or that the Bank will be able to recover any losses incurred from third parties, regardless of whether the Bank is at fault. However, there can be no assurance that (i) losses relating to litigation will not be incurred beyond the limits, or outside the coverage, of such insurance, or that any such losses would not have a material adverse effect on the results of the Bank's business, financial condition or results of operation, or (ii) provisions made for litigation related losses will be sufficient to cover the Bank's ultimate loss or expenditure.

Considerations Relating to the Philippine Banking Industry

The Philippine banking industry is highly competitive and the bank may have to be more aggressive in the implementation of its growth strategy.

The Bank is subject to significant levels of competition in all areas of its business from many other Philippine banks and branches of foreign banks, including competitors which, in some instances, have greater financial and other capital resources, a greater market share, and greater name recognition in certain areas than the Bank. The banking industry in the Philippines has, in recent years, been subject to consolidation and liberalization, including liberalization of foreign ownership restrictions. According to data from the BSP Web site, as of June 30, 2013, there were 36 domestic and foreign universal and commercial banks operating in the Philippines. (See "Philippine Banking Industry".)

In the future, the Bank may face increased competition from other financial institutions offering a wider range of commercial banking services and products and which have larger lending limits, greater financial resources and stronger balance sheets than the Bank. Increased competition may arise from:

- other large Philippine banking and financial institutions with significant presence in Metro Manila and large country-wide branch networks;

- foreign banks, due to relaxed standards permitting large foreign banks to expand their branch network through the acquisition of domestic banks among other things;

- domestic banks entering into strategic alliances with foreign banks with significant financial and management resources; and

- continued consolidation in the banking sector involving domestic and foreign banks, driven in part by the gradual removal of foreign ownership restrictions.

There can be no assurance that the Bank will be able to compete effectively in the face of such increased competition. In addition, the Bank faces intense competition in areas it has identified for growth such as the retail and middle-markets. Increased competition may make it difficult for the Bank to increase the size of its loan portfolio and deposit base, as well as cause increased pricing competition, which could have a material adverse effect on its margins, business, results of operations and financial condition and inhibit the Bank's ability to implement its growth strategy.

Banking is a heavily regulated industry and material changes in banking regulations may increase the costs associated with complying with such regulations.

The Bank is regulated principally by, and has reporting obligations to, the BSP. The Bank is also subject to banking, corporate and other laws in effect in the Philippines from time to time.

In recent years, existing rules and regulations have been modified, new rules and regulations have been enacted and reforms have been implemented which are intended to provide tighter control and more transparency in the Philippine banking sector. These rules include new guidelines on the monitoring and reporting of suspected money laundering activities as well as regulations governing the capital adequacy of banks in the Philippines. The Philippines will be adopting the new capital adequacy requirements under Basel III, which places emphasis on higher quality capital, starting January 2014 and the Bank, for its part, has started embarking on its initiatives in order to meet the more stringent requirements.

The Bank may also have to comply with stricter regulations and guidelines issued by other regulatory authorities in the Philippines, such as the Bureau of Internal Revenue ("BIR") and international bodies, such as the Financial Action Task Force. If additional rules or regulations are introduced, the Bank may incur substantial compliance and monitoring costs.

Philippine banks are generally exposed to higher credit risks and greater market volatility than banks in more developed countries.

Philippine banks are subject to the credit risk that Philippine borrowers may not make timely payment of principal and interest on loans and, in particular that, upon such failure to pay, Philippine banks may not be able to enforce the security interest they may have. The credit risk from Philippine borrowers is, in many instances, higher than that from borrowers in developed countries due to:

- the greater uncertainty associated with the Philippine regulatory, political, legal and economic environment;
- the dependence of the Philippine economy in general on exports for economic growth, however, in recent years, growth has largely been fuelled by personal consumption spending that accounted for 70.0% of gross domestic product ("GDP");
- the large foreign debt of the Government and private sector, relative to the GDP of the Philippines; and
- the greater volatility of interest rates and peso/U.S. dollar exchange rates.

Higher credit risk has an adverse effect on the quality of loan portfolios and exposes Philippine banks, including the Bank, to greater potential losses and higher risks than banks in more developed countries. In addition, higher credit risk generally increases the cost of capital for Philippine banks compared to their international counterparts. Such losses and higher capital costs arising from this higher credit risk may have a material adverse effect on the Bank's business, financial condition and results of operations.

According to data published by the BSP, non-performing loan ratios (including interbank loans) of the Philippine banking system were 3.6%, 2.9% and 2.5% as of December 31, 2010, 2011 and 2012, respectively.

The Bank's ability to assess, monitor and manage risks inherent in its business differs from the standards of its counterparts in more developed countries.

The Bank is exposed to a variety of risks, including credit risk, market risk, portfolio risk, foreign exchange risk and operational risk. The effectiveness of the Bank's risk management is limited by the quality and timeliness of available data in the Philippines in relation to factors such as the credit history of proposed borrowers and the loan exposure borrowers have with other financial institutions. Presently, the Bank has access to loan information of corporate and individual borrowers thru the BAP-Credit Bureau. The BAP-Credit Bureau was organized by the Bankers Association of the Philippines ("BAP") and its membership includes all universal and commercial banks operating in the Philippines. For its credit cards and other consumer loans, the Bank has access to both positive and negative information on credit cards issued in the Philippines thru its membership with the Credit Card Association of the Philippines. The Bank is also an active member of the Credit Management Association of the Philippines and gains access to court cases filed with the Philippine judiciary system. Republic Act No. 9510 or also known as Credit Information System Act was signed into law in 2008. It is the intent of this law to organize a National Credit Bureau in the Philippines. Until such time that the National Credit Bureau is in place, the Bank shall continue to rely on its own network to assist in its risk management functions.

The sovereign credit ratings of the Philippines may adversely affect the Bank's business.

In March 2013, Fitch Ratings raised its foreign currency sovereign rating for the Philippines from "BB+" to "BBB-" with a stable outlook. Likewise, in May 2013, Standard & Poor's Rating Services, a division of The McGraw-Hill companies, raised the long-term foreign currency sovereign rating of the Philippines to investment grade from "BB+" to "BBB-" with a stable outlook.

Any downgrades of the credit ratings of the Philippines or any deterioration in economic conditions in the Philippines as a result of these or other factors, including a significant depreciation of the peso or increase in interest rates, could materially adversely affect the Bank's borrowers and contractual counterparties and their ability to service their obligations to the Bank. This, in turn, could materially and adversely affect the Bank's business, financial condition and results of operations, including the Bank's ability to grow its asset portfolio, the quality of its assets and its ability to implement its business strategy.

Moody's change in methodology for downgrading sub-debt Issuers among Asian and regional banks may not have an adverse effect on subordinated debt markets.

In recent weeks, Moody's Investors Services, Inc. ("Moody's) has released a statement indicating a future review to look into the downgrading of sub-debt ratings among Asian regional banks in the region. This action was brought about by an increasingly held view that with less acute effects of the sub-prime and European financial crisis, there is less possibility of bank bailouts and political action during periods of economic stress. Despite this development, the Bank's consistent increases in capital stock will enable it to soften the blow that a sub-debt downgrading may have on borrowers.

The potential payout of holding subordinated debt justifies the risk of holding one because banks are now more capable of protecting their investors.

Considerations Relating to the LTNCDs

Limited right to accelerate

The LTNCDs constitute direct, unconditional, unsecured and unsubordinated obligations of the Issuer, enforceable according to the Terms and Conditions, and shall at all times rank *paripassu* and without any preference or priority among themselves and at least paripassu with all other present and future direct, unconditional, unsecured, and unsubordinated obligations of the Issuer, except for any obligation enjoying a statutory preference or priority established under Philippine laws.

The rights of the LTNCD Holders are limited in certain respects. If any one or more of the Non-Acceleration Events of Default (as defined in the Terms and Conditions) shall have occurred and be continuing, after any applicable cure period shall have lapsed, then only Holders representing at least a majority of the then aggregate outstanding principal amount of the LTNCDs may, declare the principal and all accrued interest (including default interest, as specified in the Terms and Conditions) on the LTNCDs and other charges thereon (including any incremental tax that may be due on the interest income already earned under the LTNCDs), if any, to be immediately due and payable, but the Holders representing at least a majority of the then aggregate outstanding principal amount may rescind and annul such declaration or waive any past default of the Issuer. (See "Terms and Conditions of the LTNCDs" for further details.)

PDIC Coverage

The LTNCDs will be insured with the PDIC, subject to PDIC's applicable rules and regulations, among others, on maximum insurance coverage per depositor, currently at ₱500,000.00. In determining the insured deposit, the investment in LTNCDs shall be added together with all deposits in the Bank maintained in the same right and capacity for the depositor's benefit either in his own name or in the name of others.

Transfers only through the Market Makers

All transfers of the LTNCDs must be made through a Market Maker. Consequently, the parties to a transfer may be subject to the guidelines of the Market Maker and the payment to the relevant Market Maker and the Registry of any reasonable fees and applicable taxes.

Issuance and Transfer Restrictions

The LTNCDs may not be issued or transferred to (i) the Bank; (ii) the subsidiaries or affiliates of the Bank; or (iii) wholly or majority-owned or -controlled entities of such subsidiaries and affiliates of the Bank. The Registry is authorized to refuse any transfer or transaction in the Registry Book that may be in violation of these restrictions.

Taxation of the LTNCDs

If, because of new or changes in the interpretations or conventions regarding current taxes, such that any payments of principal and/or interest under the Certificates shall be subject to deductions or withholdings for or on account of any present taxes, duties, assessments, or governmental charges of whatever nature imposed, levied, collected, withheld, or assessed by or within the Philippines or any authority therein or thereof having the power to tax, then such Taxes shall be for the account of the Holder concerned, and if the Issuer shall be required by law or regulation to deduct or withhold such Taxes, then the Issuer shall make the necessary withholding or deduction for the account of the Holder concerned; provided, however, that all sums payable by the Issuer to tax-exempt persons shall be paid in full without deductions for Taxes or government charges, subject to the submission by the relevant Holder claiming the exemption of reasonable and acceptable evidence of such exemption to the Registrar. In the event that (a) due to a change in tax status of the Certificates because of changes in tax laws (and not merely a change in the interpretation of current tax laws and regulations) , any payments of principal and/or interest under the Certificates shall be subject to deductions or withholdings for or on account of any taxes, duties, assessments, or governmental charges of whatever nature imposed, levied, collected, withheld, or assessed by or within the Philippines or any authority therein or thereof having the power to tax, including but not limited to stamp, issue, registration, documentary, value-added or similar tax, or other taxes, duties, assessments, or government charges, including interest, surcharges, and penalties thereon (the New Taxes), and (b) the Issuer does not redeem the Certificates prior to stated maturity pursuant to this Master Certificate and the Regulations, then all payments of principal and interest in respect of the Certificates shall be made free and clear of, and without withholding or deduction for, any such New Taxes. In that event, the Issuer shall pay to the Holders concerned such additional amount as will result in the receipt by the Holders of such amounts as would have been received by them had no such withholding or deduction for New Taxes been required. (See section on “Philippine Taxation” for a discussion on the taxation of the LTNCDs.)

TERMS AND CONDITIONS OF THE LTNCD

The statements of the terms and conditions of the LTNCDs set out in these Terms and Conditions do not purport to be complete listing of all the rights, obligations and privileges of the LTNCDs. The rights, obligations and privileges of the LTNCDs are set out in the Master Certificate, which provisions prevail in case of conflict with the terms and conditions of this Preliminary Offering Circular.

1. Prohibited Holders

The Issuer including its Subsidiaries and Affiliates and wholly or majority-owned or -controlled entities of such Subsidiaries and Affiliates cannot be a Holder of the LTNCDs of the Issuer.

For purposes hereof, an "Affiliate" refers to an entity, of which at least twenty percent (20.0%) but not exceeding fifty percent (50.0%) of the outstanding voting stock is owned by the Issuer.

For purposes hereof, "Subsidiaries" shall mean, in relation to the Issuer, any corporation, partnership or other entity of which at least a majority of the securities or other ownership interests having by the terms thereof ordinary voting power to elect a majority of the board of directors or other persons performing similar functions of such corporation, partnership or other entity is at the time directly or indirectly owned or controlled by (a) the Issuer or one (1) or more Subsidiaries of the Issuer or (b) by the Issuer and one (1) or more Subsidiaries of the Issuer.

2. Form and Denomination

Form. The LTNCDs will be issued scripless and will be maintained in electronic form with the Registrar, subject to the payment of fees to the Registrar and in compliance with the provisions of Republic Act No. 8792, otherwise known as the Electronic Commerce Act, particularly on the existence of an assurance on the integrity, reliability, and authenticity of the LTNCDs in electronic form. The LTNCDs shall be registered in the name of individuals or corporations, and are negotiable. A Registry Confirmation will be issued by the Registrar in favor of the Holders in accordance with the BSP Rules.

Denomination. Minimum of ₱250,000.00 per Certificate, and increments of ₱50,000.00 beyond the minimum.

3. Payment

Any payment of principal or interest under the LTNCDs shall be made to the Holders through the Paying Agent based solely on the records of the Registrar.

4. Interest

The face value of the Certificate multiplied by the Interest Rate calculated on the basis of a three hundred and sixty (360)-day year consisting of twelve (12) months of thirty (30) days each month.

5. Redemption at Maturity

Unless previously preterminated and cancelled in accordance with these terms and conditions, the LTNCDs shall not be redeemable or terminable at the instance of any Holder before Maturity Date. However, negotiation or transfer from one Holder to another is allowed and shall not constitute pretermination of the Certificate.

6. Early Redemption Option

(i) *Early Redemption Option for Taxation Reasons*. If any payment of principal or interest due under the LTNCDs becomes subject to additional or increased taxes other than the taxes and rates of such taxes prevailing as of the Issue Date as a result of changes in tax laws (and not merely a change in the interpretation of current tax laws and regulations) and such additional or increased rate of such tax cannot be avoided by the use of reasonable measures available to the Issuer, the Issuer, subject to the Regulations, shall have the option (but not the obligation) to preterminate and redeem all and not part of the LTNCDs on any Interest Payment Date before Maturity Date at the Early Redemption Amount.

(ii) *Early Redemption Option for Increased Reserves*. If the LTNCDs become subject to additional or increased reserves required by the BSP other than the statutory regular reserves required in the Regulations prevailing as of the Issue Date, and such additional or increased amount of reserves required cannot be avoided by use of reasonable measures available to the Issuer, the Issuer, subject to the Regulations, shall have the option (but not the obligation) to preterminate and redeem all and not part of the LTNCDs on any Interest Payment Date before Maturity Date at the Early Redemption Amount.

(iii) *Early Redemption Option for Other Reasons*. Subject to the Regulations, the Issuer has the option (but not the obligation) to pre-terminate and redeem all and not part of the LTNCDs on any Interest Payment Date before Maturity Date at the Early Redemption Amount on any other ground as may be approved by the BSP.

(iv) *Manner of Exercising the Early Redemption Option*. In exercising the Early Redemption Option, the Issuer shall give the Holders and the appropriate supervision and examination department of the BSP not more than sixty (60) days nor less than thirty (30) days' prior notice, stating therein the ground relied upon for the exercise of the Early Redemption Option, which grounds must be one of the grounds specified in (i) to (iii) above. The notice referred to in this section shall be published in at least two (2) newspapers of general circulation in the Philippines in accordance with SEC Memorandum Circular No. 1 (2008) for two (2) consecutive days at any time prior. Once issued, said notice shall be irrevocable, and shall be binding on the Issuer and each Holder.

(v) *Payments; Taxes; Reserves*. After the issuance of the notice under this section, the Issuer shall be obliged to repay all of the LTNCDs at the Early Redemption Amount on the Early Redemption Date. On the Early Redemption Date and following payment of the Early Redemption Amount, the Registrar shall transfer all of the interests of the Holders in the Certificate to the Issuer. All such LTNCDs preterminated pursuant to this Section shall then be deemed fully redeemed and cancelled.

As a consequence of the exercise of the Early Redemption Option, any incremental tax that may be due on the interest income already earned under the LTNCDs prior to or as a result of the exercise by the Issuer of the Early Redemption Option shall be for the account of the Issuer. In addition, the Issuer shall recompute its reserve positions retroactively based on the applicable reserve rate(s) for regular time deposits during the period between the Issue Date and the Early Redemption Date.

(vi) *Early Redemption Amount; Early Redemption Date; Early Redemption Option*. The Early Redemption Amount shall be equal to the Issue Price, plus accrued and unpaid interest up to, but excluding, the Early Redemption Date. The Early Redemption Date means the date (which must be an Interest Payment Date) when the Early Redemption Option is exercised by the Issuer pursuant to this section and subject to the Regulations. The Early Redemption Option means any option of the Issuer set out in (i) to (iii) above to pre-terminate and redeem the LTNCDs in whole, but not in part, before the Maturity Date at the Early Redemption Amount on any Early Redemption Date; subject to the Regulations.

7. No Pre-termination

Unless previously preterminated and cancelled in accordance with these terms and conditions, the LTNCDs shall not be redeemable or terminable at the instance of any Holder before Maturity Date. However, negotiation or transfer from one Holder to another is allowed and shall not constitute pretermination of the Certificate.

Negotiations or transfers of the LTNCDs to any one other than the Issuer prior to Maturity Date shall not constitute pre-termination.

8. Taxation

The Market Makers and/or Registrar may, unless properly provided with satisfactory proof of the tax-exempt status of a Holder, assume that said Holder is taxable and proceed to apply the tax due on the LTNCDs. The Market Makers may request the Holder claiming a preferential tax treatment to provide proof satisfactory to it of such preferential status.

If any payments of principal and/or interest under the LTNCDs shall be subject to deductions or withholdings for or on account of any present taxes, duties, assessments, or governmental charges of whatever nature imposed, levied, collected, withheld, or assessed by or within the Philippines or any authority therein or thereof having the power to tax, including but not limited to stamp, issue, registration, documentary, value-added or similar tax, or other taxes, duties, assessments, or government charges, including interest, surcharges, and penalties thereon (the *Taxes*), then such Taxes shall be for the account of the Holder concerned, and if the Issuer shall be required by law or regulation to deduct or withhold such Taxes, then the Issuer shall make the necessary withholding or deduction for the account of the Holder concerned; provided, however, that all sums payable by the Issuer to tax-exempt persons shall be paid in full without deductions for Taxes or government charges, subject to the submission by the relevant Holder claiming the exemption of reasonable and acceptable evidence of such exemption to the Registrar; and provided, further, that documentary stamp tax for the primary issue of the LTNCDs and the documentation, if any, shall be for the Issuer's account.

If, because of new or changes in the interpretations or conventions regarding current taxes, such that any payments of principal and/or interest under the LTNCDs shall be subject to deductions or withholdings for or on account of any present taxes, duties, assessments, or governmental charges of whatever nature imposed, levied, collected, withheld, or assessed by or within the Philippines or any authority therein or thereof having the power to tax, then such Taxes shall be for the account of the Holder concerned, and if the Issuer shall be required by law or regulation to deduct or withhold such Taxes, then the Issuer shall make the necessary withholding or deduction for the account of the Holder concerned; provided, however, that all sums payable by the Issuer to tax-exempt persons shall be paid in full without deductions for Taxes or government charges, subject to the submission by the relevant Holder claiming the exemption of reasonable and acceptable evidence of such exemption to the Registrar.

In the event that (a) due to a change in tax status of the LTNCDs because of changes in tax laws (and not merely a change in the interpretation of current tax laws and regulations), any payments of principal and/or interest under the LTNCDs shall be subject to deductions or withholdings for or on account of any taxes, duties, assessments, or governmental charges of whatever nature imposed, levied, collected, withheld, or assessed by or within the Philippines or any authority therein or thereof having the power to tax, including but not limited to stamp, issue, registration, documentary, value-added or similar tax, or other taxes, duties, assessments, or government charges, including interest, surcharges, and penalties thereon (the *New Taxes*), and (b) the Issuer does not redeem the LTNCDs prior to stated maturity pursuant to this Master Certificate and the Regulations, then all payments of principal and interest in respect of the LTNCDs shall be made free and clear of, and without withholding or deduction for, any such New Taxes. In that event, the Issuer shall pay to the Holders concerned such additional amount as will result in the receipt by the Holders of such amounts as would have been received by them had no such withholding or deduction for New Taxes been required.

9. Status

The LTNCDs constitute direct, unconditional, unsecured (save for the mandatory insurance coverage under the rules of the Philippine Deposit Insurance Corporation, “PDIC”), and unsubordinated peso-denominated obligations of the Issuer, enforceable according to these Terms and Conditions, and shall at all times rank pari-passu with all other present and future direct, unconditional, unsecured, and unsubordinated obligations of the Issuer, except for any obligation enjoying a statutory preference or priority established under Philippine laws.

The LTNCDs shall be insured with the PDIC, subject to applicable rules and regulations, among others, on maximum insurance coverage, in accordance with the following:

(i) Deposits are insured by the PDIC up to the maximum amount insurable by the PDIC which currently stands at Five Hundred Thousand Pesos (₱500,000.00) per depositor.

(ii) PDIC shall presume that the name/s appearing on the records of the Registrar & Paying Agent is/are the actual/beneficial owner/s of the deposit, except as provided in PDIC Regulatory Issuance No. 2002-03, as the same may be amended from time.

(iii) In case of (a) deposits in the name of, or transfers or break-up of deposits in favor of entities, either singly or jointly with individuals, and (b) transfers or break-up of deposits in favor of non-qualified relatives, whenever such transfer/break up will result in increased deposit insurance coverage, PDIC shall recognize beneficial ownership of the entity or transferee; provided, that the records of the Registrar & Paying Agent show the following:

   (a) details or information establishing the right and capacity or the relationship of the entity with the individual/s, or

   (b) details or information establishing the validity or effectivity of the deposit transfer, or

(c) copy of a Board Resolution, order of competent government body/agency, contract or similar document, as required/provided by applicable laws.

In the absence of any of the foregoing, PDIC shall deem the outstanding deposit as maintained for the benefit of the transferor-Holder although in the name of the transferee, subject to consolidation with the other deposits of the transferor-Holder.

(iv) PDIC may require additional documents from the depositor to ascertain the details of the deposit transfer or the right and capacity of the transferee or his relationship to the transferor-Holder.

The LTNCDs shall not be used as collateral for any loan made by the Issuer or any of its Subsidiaries or Affiliates

10. Title and Transfer

(a) *Registration.*

The LTNCDs shall be registered in the name of individuals or corporations, and are negotiable. A Registry Confirmation will be issued by the Registrar in favor of the Holders in accordance with the BSP Rules.

In case any Registry Confirmation shall be mutilated, destroyed, lost, or stolen, the Registrar shall deliver to the relevant Holder a new Registry Confirmation under the name of such relevant Holder with the same information for such relevant Holder, and of like denomination in exchange for, and upon cancellation of, the mutilated Registry Confirmation or in lieu of the Registry Confirmation so destroyed, lost or stolen only in the absence of any notice in writing to the Registrar that such Registry Confirmation has been acquired by a *bona fide* purchaser and upon presentation of the following:

(a) the original Registry Confirmation (only in cases of mutilation);

(b) a sworn affidavit of the Holder attesting to the destruction, loss, or theft of any such Registry Confirmation, the serial number of such Registry Confirmation and the amount of the deposit covered and undertaking to keep the Issuer and the Registrar and Paying Agent fully indemnified and free from and harmless against any loss, liability, cost, claim, damage or expense caused by or connected with the substitution of such Registry Confirmation;

(c) in the case of corporate Holders, a certificate from the Corporate Secretary of such Holder on the resolution of the Board of Directors of such Holder stating such fact of mutilation, destruction, loss, or theft, authorizing the application for a replacement of the Registry Confirmation and designating the authorized signatories for that purpose;

(d) the Purchase Advice issued by the Selling Agent or Market Makers to the Holder requesting a replacement Registry Confirmation; and

(e) such other reasonable requirements or conditions as the Registrar and Paying Agent may deem appropriate to impose.

(b) *Transfers.*

All negotiations/transfers of the LTNCDs shall be coursed through a Market Maker by coordinating and coursing such transfers through the Selling Agents and subsequently the Registrar, subject to the payment by the Holder of fees to the Market Maker. The Market Maker concerned through the Selling Agents may request for additional information and documents from the transferor-Holder and transferee-Holder, as may be required under the Regulations, AMLA, and jurisdiction/s (other than the Philippines) under which the Market Makers are organized and existing.

The transfer of LTNCDs among Holders who are classified under the same tax status (taxable or tax-exempt) can be effected at any point in time during which the LTNCDs are outstanding except during the Closed Period. The transfer of LTNCDs between taxable Holders and tax-exempt Holders can be effected only on the Interest Payment Date except during the Closed Period. Once the system of the Registrar can process the transfer of a Certificate that will result in a change in the taxability or non-taxability of the interest income due thereon in between Interest Payment Dates, then such transfers can be done at any time.

In the case of a transfer by a taxable or non-tax exempt Holder in favor of a transferee (whether taxable or tax-exempt), the final withholding tax on the interest income earned or deemed to be earned by the transferor-Holder on the LTNCDs during the Interest Period in which the transfer is made, based on the period that such LTNCDs were actually held by the transferor-Holder, shall be deducted from the purchase price due to it.

The Market Makers concerned or the fixed income exchange, as applicable, shall issue to such Holder (with a copy to the Registrar) a Purchase Advice to evidence the transfer or assignment of such LTNCDs. As a condition precedent for any transfer or assignment of the LTNCDs, the Registry Confirmation, the Purchase Advice, and such transfer instructions required by the Registrar must be surrendered by the transferor-Holder to the authorized Market Makers.

(c) *Closed Periods*.

No person may require the transfer of any Certificate to be registered by the Registrar in the Registry during the period of ten (10) Banking Days preceding any Interest Payment Date (the "Closed Period"). The Registrar will prevent any transfer of the LTNCDs to be recorded in the Registry during any Closed Period. The Registrar shall recognize and treat only those Holders registered as such in the Registry immediately prior to the start of the Closed Period as the owners of the corresponding LTNCDs for any relevant or allocation purpose.

(d) *Qualification Determination.*

Each Selling Agent (in the case of initial issuance of the LTNCDs) and Market Maker (in the case of negotiations/transfers of the LTNCDs) shall verify the identity and other relevant details of each investor and ascertain that the proposed Holder or transferee of a Certificate is not a Prohibited Holder. In the event that the LTNCDs are listed on any fixed income exchange, the obligation to verify the identity and other relevant details of each investor and ascertain that the proposed Holder or transferee of a Certificate is not a Prohibited Holder shall be performed by the trading participants of such fixed income exchange.

The Holder shall submit any and all information reasonably required by the Selling Agents and/or Market Makers with respect to the Know Your Customer ("KYC") Requirements and qualification of the proposed Holder or transferee in order to determine that such Holder or transferee is not a Prohibited Holder.

"KYC Requirements" shall mean the documentary requirements, as these may be amended from time to time, required under the AMLA and when applicable, the jurisdiction/s (other than the Philippines) under which the Selling Agents are subject and the Selling Agents' and Market Makers' own internal policies regarding "knowing your customer" and anti-money laundering.

11. Representations and Warranties

1. The Issuer represents, warrants, and agrees that:

   a. *Incorporation.* (a) The Issuer is duly incorporated and is validly existing as a commercial banking corporation in good standing under the laws of the Republic of the Philippines, has its principal office in the address indicated in this Agreement, is qualified to do business in the Philippines, with power and authority (corporate and otherwise) to own its assets and properties now owned by it as well as those to be hereafter acquired by it for the purpose of business and conduct its business as a bank as described in the Offering Circular, (b) The Issuer's Major Affiliates and Subsidiaries are duly incorporated and are validly existing as corporations in good standing under the laws of the Republic of the Philippines, with power and authority (corporate and otherwise) to own its assets and conduct its business as described in the Offering Circular.

   b. *Corporate Power.* The Issuer has the corporate power under the laws of its incorporation and its articles of incorporation and by-laws to issue and offer the LTNCDs and enter into and execute the Contracts and carry out the Issuer's obligations under the Contracts. All necessary actions and things required to be obtained, taken, fulfilled, or done, licenses, consents, approvals, authorizations, waivers, filings or registrations with or qualifications or orders of all courts, government agencies or regulatory authorities required:

      i. for or in connection with the issue and offering of the LTNCDs;

      ii. for or in connection with the entering into and execution by the Issuer of the Contracts for purposes of issuance of the LTNCDs and the carrying out of the Issuer's obligations under the Contracts.

   have been obtained, taken, fulfilled, or done, and such obtainment, taking, fulfillment, or doing are subsisting and unconditional, and are or will by the Issue Date be in full force and effect.

   c. *Capacity.* The issue and sale of the LTNCDs has been, or will prior to the issue date, be duly authorized by the Issuer and the LTNCDs, when duly executed, authenticated, issued and delivered as provided in accordance with the Registry and Paying Agency Agreement will constitute valid, enforceable and legally binding obligations of the Issuer subject to applicable bankruptcy, insolvency or similar laws affecting creditors' rights generally and general principles of equity; and the LTNCDs, when issued and delivered, will conform to the descriptions thereof contained in the Offering Circular.

d. *Validity of Contracts.* The Contracts have been duly authorized, executed, and delivered by the Issuer and the Sole Arranger and Selling Agents, and constitute valid and binding agreements between such parties. Such Contracts shall constitute, legal, valid and binding obligations of the Issuer enforceable in accordance with its terms, subject in each case in the event of enforcement to the laws of bankruptcy and other laws affecting the rights of creditors generally.

e. *Validity of the LTNCDs.* The LTNCDs have been duly authorized by the Issuer and, when duly executed, authenticated, issued and delivered in accordance with the Registry and Paying Agency Agreement, will constitute its valid and legally binding obligations.

f. *Consents.* All necessary actions and things all necessary actions and things required to be taken, fulfilled or done(including without limitation the obtaining of any consent, authorisation, order or license or the making of any filing or registration) for the issue of the LTNCDs, the carrying out of the other transactions contemplated by the LTNCDs and the Contracts or the compliance by the Bank with the terms of the LTNCDs and the Contracts, as the case may be, have been taken, fulfilled or done.

g. *Compliance.*

(a) The execution and delivery of the Contracts, the issuance of the LTNCDs, the carrying out of the other transactions contemplated by the and these Terms and Conditions, and compliance with their terms do not and will not (i) conflict with or result in a breach of any of the terms or provisions of, or constitute a default or violation under, the documents constituting the Issuer, or any contract, indenture, trust deed, mortgage, or other agreement or instrument to which the Issuer or any of its subsidiaries is a party or by which it or any of its properties is bound; or (ii) violate or infringe any existing applicable law, rule, regulation, judgment, order, or decree of any government, governmental body or court, domestic or foreign, having jurisdiction over the it, any such subsidiary or any of their properties.

(b) Each of the Issuer and any member of the UnionBank Group is not, or with the giving of notice or lapse of time or both, will not be, in any material respect, in violation of, or in default under its charter or by-laws, or any indenture, mortgage, deed of trust, loan agreement, or other agreement or instrument to which it may be a party or by which any of its property assets may be bound or may be subject (collectively and respectively, "Agreements" and "Instruments"). The execution, delivery and performance by the Issuer of each of the Contracts and the carrying out of the transactions contemplated in the Contracts will not conflict with or result in a breach of any of the terms or provisions of, or constitute a default under, or result in the creation or imposition of any lien, charge or encumbrance upon any property or assets of the Issuer or any member of the UnionBank Group pursuant to, the Contracts, and neither will any such action result in any violation of the provisions of the charter or by-laws of the Issuer or any member of the UnionBank Group applicable law or statute or any order, rule, or regulation of any court or governmental agency or body having jurisdiction over the Issuer or any member of the UnionBank Group or any of their respective assets. Any consent, approval, authorization, order, registration, or qualification of or with any such court or governmental agency or body which is required for the offer and sale of the LTNCDs or the carrying out by the Issuer of the transactions contemplated by the Contracts has been obtained.

h. *Status of LTNCDs*. The LTNCDs constitute direct, unconditional, unsecured (save for the mandatory insurance coverage under the rules of the PDIC), and unsubordinated peso-denominated obligations of the Issuer, enforceable according to these Terms and Conditions, and shall at all times rank pari-passu with all other present and future direct, unconditional, unsecured, and unsubordinated obligations of the Issuer, except for any obligation enjoying a statutory preference or priority established under Philippine laws.

i. *Litigation.* (a) Except as specifically and expressly disclosed in the Offering Circular, there are no legal or governmental proceedings in the Philippines or in any other jurisdiction pending or, to the best knowledge of the Issuer, after reasonable inquiries, threatened to be filed, to which the Issuer or any member of the UnionBank Group is or may be a party or to which any of its assets is or may be the subject which, if determined adversely against the Issuer or any member of the UnionBank Group, could individually or in the aggregate reasonably be expected to have a Material Adverse Effect. To the best of the Issuer's knowledge after reasonable inquiries, no such proceedings are threatened or contemplated by governmental authorities or threatened by others. (b) Except as specifically described in the Offering Circular, there are no pending actions, suits or proceedings against or affecting the Issuer, its subsidiaries, or affiliates or any of their properties which, if determined adversely, would, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect, and to the best of the Issuer’s knowledge such actions, suits, or proceedings are threatened or contemplated.

j. *Financial Statements*. The audited financial statements (including the summaries and schedules) and their related notes included in the Offering Circular are accurate in all respects and present fairly the financial position of the Issuer in its entirety as of the dates indicated and the results of operations and changes in financial position of the Issuer and the UnionBank Group for the periods, in respect of which they have been prepared. The information supplied and contained in said financial statements are true and correct. Said financial statements (i) have been prepared in conformity with Financial Reporting Standards in the Philippines for banks applied on a consistent basis, and interim financial statements as of and for the six months ended June 30, 2013 and 2012; (ii) make adequate provision for bad and doubtful debts (if any); and (iii) make appropriate provision (or contain a note in accordance with good accounting practice) for all deferred, contingent, or other liabilities as of the dates indicated. There has been no material change in the financial condition or results of operations of the Issuer sufficient to impair its ability to perform its obligations under the LTNCDs.

k. *Title to Property.* Except as disclosed in the Offering Circular or in its audited financial statements as of and for the period ended December 31, 2012, the Issuer and each member of the UnionBank Group has good and marketable title to all its properties, free and clear of liens, encumbrances, restrictions, pledges, mortgages, security interest, or charges, except for the following: (i) any liens, encumbrances, restrictions, pledges or mortgages over its properties existing prior to the date of the Offering Circular or disclosed in its audited financial statements as of and for the period ended December 31, 2012; (ii) any lien over those properties which are acquired by the Issuer through any legal action or proceedings or which are conveyed to the Issuer via dacion en pago or other similar arrangement in the course of the ordinary business of the Issuer; (iii) liens arising in the ordinary course of its business, or imposed or arising solely by operation of law (other than any statutory preference or priority under Article 2244(14) of the Civil Code of the Philippines), such as carrier's, warehousemen's and mechanic's liens and other similar liens arising in the ordinary course of business; (iv) liens for taxes, assessments or governmental charges on properties or assets of the Issuer if the same shall not at the time be delinquent or thereafter can be paid without penalty, (v) liens arising from workmen's compensation laws, pensions and social security legislations; (vi) any lien which secures foreign currency and interest rate swap and derivative transactions undertaken by the Issuer in the ordinary course of its business; (vii) the Registrar and Paying Agent's lien or security right on the funds of the Issuer in relation to all fees, charges, and expenses, and any credit facility or accommodation granted to the Issuer by the Registrar, as contemplated by Section 12 of the Registry and Paying Agency Agreement; and (viii) any extension, renewal or replenishment in whole or in part of the foregoing liens.

l. *Offering Circular.*

(i) The preliminary and, when issued, the final Offering Circular, presents a fair, complete, and accurate description of the Issuer, the LTNCDs, and the considerations that any potential investor in the LTNCDs needs to know before making an informed decision to invest in the LTNCDs.

(ii) No order preventing, limiting or suspending the use of the Offering Circular has been issued by the BSP or the SEC. The Offering Circular (i) is compliant and will remain compliant in all material respects with Regulations; (ii) contains all information with respect to the UnionBank Group and to the LTNCDs which is material in the context of the issue and offering of the LTNCDs (including, without limitation, all information required by the applicable laws and regulations of the Philippines and the information which, according to the particular nature of the Issuer and of the LTNCDs, is necessary to enable potential Holders and their investment advisers to make an informed assessment of the assets and liabilities, financial position, profits and losses, and prospects of the Issuer , the UnionBank Group, and of the rights attaching to the LTNCDs) and the statements contained in the Offering Circular as at the date thereof with respect to the UnionBank Group and the LTNCDs are true and accurate and not misleading; (iii) does not contain any untrue statement or omit to state a material fact required to be stated or necessary to make the statements, in light_of the circumstances under which they were made, not misleading; (iv) does not omit other facts in relation to the

UnionBank Group or the LTNCDs the omission of which would, in the context of the issue and offering of the LTNCDs, make any statement in the Offering Circular as at the date thereof misleading; (v) contains opinions and intentions expressed in the Offering Circular with regard to the Issuer and the UnionBank Group that are honestly held, have been reached after considering all relevant circumstances and are based on reasonable assumptions; and (vi) has been prepared after all reasonable inquiries have been made by the Issuer to ascertain such facts and to verify the accuracy of all such information and statements.

(iii) The statements, forecasts, estimates and expressions of opinion and intentions contained in the Offering Circular at the date thereof with regard to the Issuer and the UnionBank Group have been made after due and proper consideration of all relevant circumstances, are based on reasonable assumptions, and represent reasonable and fair expectations honestly held based on facts known to the Issuer.

(iv) Save as disclosed in the Offering Circular, all material transaction by the Issuer with its directors, officers, management, shareholders, or any other person, including persons formerly holding such positions, are on terms that are available from other parties on an arm's length basis.

(v) There are no material contracts or other documents of a character required to be filed as an exhibit or annex to, or required to be described in, the Offering Circular which are not so filed or described.

(vi) The Offering Circular accurately describes: (i) accounting policies which the Issuer believes to be the most important in the portrayal of the UnionBank Group's financial condition and results of operations; (ii) material judgments and uncertainties affecting the application of the said accounting policies; and (iii) an explanation of the likelihood that materially different amounts would be reported under different conditions or using different assumptions, and the Board of Directors and audit committee of the Issuer have reviewed and agreed with the selection and disclosure of the said accounting policies in the Offering Circular and have consulted with their independent accountants with regards to such disclosure.

(vii) The Offering Circular contains all information with respect to the Issuer and to the LTNCDs which is material in the context of the issue and offering of the LTNCDs (including, without limitation, all information required by the applicable laws and regulations of the Philippines and the information which, according to the particular nature of the Issuer and of the LTNCDs, is necessary to enable depositors and their advisers to make an informed assessment of the assets and liabilities, financial position, profits and losses, and prospects of the Issuer and of the rights attaching to the LTNCDs); (ii) the statements contained in the Offering Circular relating to the Issuer, its subsidiaries, and affiliates are in every material respect correct, true, accurate, and not misleading, (iii) the statements, forecasts, estimates, and expressions of opinion and intentions expressed in the Offering Circular with regard to them are honestly held, have been reached after considering all relevant circumstances, and are based on reasonable assumptions, and represent reasonable and fair expectations honestly held based on facts known to the issuer (iv) there are no other facts or information in relation to the Issuer, its subsidiaries, and affiliates, or the LTNCDs the omission of which would, in the context of the issue and offering of the LTNCDs, make any statement in the Offering Circular misleading, and (v) all reasonable enquiries have been made by the Issuer to ascertain such facts and to verify the accuracy of all such information and statements.

(viii) The Offering Circular accurately and fully describes (i) all material trends, demands, commitments, events, uncertainties and risks, and the potential effects thereof, that the Issuer believes would materially affect liquidity and are reasonably likely to occur; and (ii) all material off-balance sheet transactions, arrangements, and obligations; and neither the Issuer nor any other member of the UnionBank Group has any material relationships with unconsolidated entities that are contractually limited to narrow activities that facilitate the transfer of or access to assets by the Issuer or any other member of the UnionBank Group, such as structured finance entities and special purpose entities that are reasonably likely to have a material effect on the liquidity of the Issuer or any other member of the UnionBank Group or the availability thereof or the requirements of the Issuer or any other member of the UnionBank Group for capital resources.

m. *Accounting Controls*. The Issuer maintains systems of internal accounting controls sufficient to provide reasonable assurance that (i) transactions are executed in accordance with management’s general or specific authorizations; (ii) transactions are recorded as necessary to permit preparation of financial statements in conformity with Financial Reporting Standards in the Philippines for banks and to maintain asset accountability; (iii) access to assets is permitted only in accordance with management’s general or specific authorization; (iv) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences; and (v) each of its subsidiaries, and affiliates has made and kept books, records and accounts which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of assets of such entity and provide a sufficient basis for the preparation of the Issuer’s consolidated financial statements in accordance with Financial Reporting Standards in the Philippines for banks; and (vi) its current management information and accounting control system has been in operation for at least twelve (12) months during which none of the Issuer, its subsidiaries, and affiliates has experienced any material difficulties with regard to (i) through (v) above.

n. *Contingent Liabilities.* The Issuer has no outstanding guarantees or contingent payment obligations of the Issuer in respect of indebtedness of third parties except those issued in the ordinary course of business or as described in the Offering Circular; the Issuer is in compliance with all of its obligations under any outstanding guarantees or contingent payment obligations as described in the Offering Circular.

o. *Intellectual Property.* It has legal title to all its all patents, licenses, inventions, copyrights, know-how, trademarks, service marks, trade names or other intellectual property (collectively, “Intellectual Property”) necessary to carry on the business now operated by it, in each case free and clear of all liens, encumbrances and defects; and any real property and buildings held under lease by it are held by its under valid, subsisting, and enforceable leases. For its Intellectual Property, it has not received any notice or is otherwise aware of any infringement of or conflict with asserted rights of others with respect to any Intellectual Property or of any facts or circumstances which would render any Intellectual Property invalid or inadequate to protect its interests therein, and which infringement or conflict (if the subject of any unfavorable decision, ruling or finding) or invalidity or inadequacy, singly or in the aggregate, would reasonably be expected to result in a Material Adverse Effect.

p. *Licenses, Permits and Conduct of Business.* It (a) has all licenses, franchises, permits, authorizations, approvals, registrations and orders and other concessions that are necessary to own or lease its other properties and conduct its businesses as described in the Offering Circular; (ii) is conducting its business and operations in compliance with all applicable laws and regulations in each of the jurisdictions in which it conducts business and operations, including, without limitation, the Regulations (iii) has complied with, corrected and is effectively implemented, to the satisfaction of the BSP, all findings and recommendations of the BSP resulting from all past audits and examinations conducted by the BSP on the Bank; and (iv) is otherwise in compliance with all agreements and other instruments to which it is a party, except where any failure to be in compliance with any of which would not, individually or in the aggregate, have a Material Adverse Effect.

q. *Default.* No event has occurred or circumstance arisen and is continuing which, had the LTNCDs already been issued, would (whether or not with the lapse of time and/or other condition) constitute a Termination Event.

r. *Anti-Money Laundering.* The Issuer, its Subsidiaries and Affiliates and wholly or majority-owned or -controlled entities of such Subsidiaries and Affiliates and the other members of the UnionBank Group are in compliance with the AMLA in all material respects.

s. *Solvency.* The Issuer is Solvent. As used in this paragraph, the term "Solvent" means, with respect to a particular date, that on such date: (i) the present fair market value (or present fair saleable value) of the assets of the Issuer is not less than the total amount required to pay the liabilities of the Issuer on its total existing debts and liabilities (including contingent liabilities) as they become absolute and matured; (ii) the Issuer is able to realize upon its assets and pay its debts and other liabilities, contingent obligations and commitments as they mature and become due in the normal course of business; (iii) the Issuer is not incurring debts or liabilities beyond its ability to pay as such debts and liabilities mature; (iv) the Issuer is not engaged in any business or transaction, and does not propose to engage in any business or transaction, for which its property would constitute unreasonably small capital after giving due consideration to the prevailing practice in the industry in which the Issuer is engaged; (v) the Issuer will be able to meet its obligations under all its outstanding indebtedness as they fall due; and (vi) the Issuer is not a defendant in any civil action that would result in a judgment that the Issuer is or would become unable to satisfy.

t. *Auditors.* (i) All information provided by the Issuer to its Auditors required for the purposes of their comfort letters in connection with the offering and sale of the LTNCDs has been supplied, or as the case may be, will be supplied, in good faith and after due and careful enquiry; such information was when supplied and remains (to the extent not subsequently updated by further information supplied to such persons prior to the date hereof), or as the case may be, will be when supplied, true and accurate in all material respects and no further information has been withheld the absence of which might reasonably have affected the contents of any of such letters in any material respect; (ii) The Auditors are independent public accountants, as required by the Philippine Institute of Certified Public Accountants and the applicable rules and regulations thereof.

u. *OFAC.* (a) Neither the Issuer nor any of its Subsidiaries nor, to the best of the knowledge of the Issuer after due and careful enquiry, any director, officer, agent, employee or Affiliate of the Issuer and its Subsidiaries: (i) is an individual or entity (a "Person") currently the subject of any U.S. sanctions administered or enforced by the United States Government including, without limitation, the Office of Foreign Assets Control of the U.S. Department of the Treasury ("OFAC") or any sanctions or measures imposed by the United Nations Security Council, the European Union or Her Majesty's Treasury ("HMT") or any sanction or requirements imposed by, or based upon the obligations or authorisations set forth in, the U.S. Trading With the Enemy Act, the U.S. International Emergency Economic Powers Act, the U.S. United Nations Participation Act or the U.S. Syria Accountability and Lebanese Sovereignty Act, all as amended, or any foreign assets control regulations of the U.S. Department of the Treasury (including but not limited to 31 CFR, Subtitle B, Chapter V, as amended) or any enabling legislation or executive order relating thereto (collectively, the "Sanctions"); (ii) is located, organised or resident in a country or territory that is the subject of Sanctions (including without limitation, Cuba, Iran, North Korea, Sudan and Syria); (iii) has engaged in, and is now engaged in any dealings, transactions or connections with any government, person, entity or project targeted by, or located in any country or territory, that at the time of the dealing or transaction is or was the subject of Sanctions; and (iv) is or has been in violation of or subject to any claim, action, suit, proceeding or investigation relating to any Sanctions; (b) Neither the Issuer nor any of its Subsidiaries is controlled (within the meaning of the regulations promulgating such Sanctions or the laws authorising such promulgation) by any Person currently the subject of any Sanctions or in any country or territory that is the subject of Sanctions or in any other manner that would result in a violation by any Person (including any Person participating in the offering, whether as underwriter, adviser, investor or otherwise) of Sanctions; (c) None of the issue and sales of the LTNCDs, the execution, delivery and performance of the Contracts, the consummation of any other transactions contemplated hereby, or the provision of services contemplated by the Contracts will result in a violation of any Sanctions; (d) The funds raised under the offering will not directly or indirectly be lent, contributed, or otherwise made available to any subsidiary, joint venture partner, or any other person or entity, for the purpose of financing the activities of any person currently subject to any Sanctions.

v. *Anti-Bribery.* Neither the Issuer nor any of its Subsidiaries nor, to the best of the knowledge of the Issuer after due and careful enquiry, any director, officer, agent, employee or Affiliate of the Issuer or its Subsidiaries, is aware of or has taken any action, directly or indirectly, that would result in a violation by such persons of any applicable anti-bribery and anti-corruption laws, including, without limitation, the UK Bribery Act of 2010 and the Foreign Corrupt Practices Act of 1977, as amended, and the rules and regulations thereunder (the "FCPA"), including, without limitation, making use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay or authorisation of the payment of any money, or other property, gift, promise to give, or authorisation of the giving of anything of value to any "foreign official" (as such term is defined in the FCPA) or any foreign political party or official thereof or any candidate for foreign political office, in contravention of the FCPA; and the Issuer, the Company, the Subsidiary Guarantor and every of its subsidiaries and, to the best knowledge of the Issuer (after due and careful enquiry), its respective affiliates have conducted their respective businesses in compliance with all applicable anti-bribery or anti-corruption laws and regulations and have instituted and maintained policies and procedures designed to ensure continued compliance with, and prevent violation of, such laws, rules and regulations.

2. These representations and warranties of the Issuer shall survive the issuance of the LTNCDs up to Maturity Date, and shall be complied with and performed fully and faithfully by the Issuer at all times while the LTNCDs or any portion thereof remains outstanding. These representations and warranties shall be true and correct as long as the LTNCDs remain outstanding.

12. Covenants

The Issuer hereby covenants and agrees that, for as long as the LTNCDs remain outstanding, it shall:

a. pay all amounts due under the LTNCDs and the Contracts at the times and in the manner specified in, and perform all its obligations, undertakings, and covenants under the LTNCDs and the Contracts;

b. pay and discharge all taxes, assessments, and government charges or levies imposed upon it or upon its income or profits or upon any properties belonging to it prior to the date on which penalties are assessed; pay and discharge when due all lawful claims which, if unpaid, might become a lien or charge upon any of its properties; and take such steps as may be necessary in order to prevent its properties from being subjected to the possibilities of loss, forfeiture, or sale; Provided, that it shall not be required to pay any such tax, assessment, charge, levy, or claim which is being contested by it in good faith and by proper proceedings;

c. preserve and maintain its corporate existence;

d. maintain adequate financial records and prepare all financial statements in accordance with Financial Reporting Standards in the Philippines for banks consistently applied and in compliance with the regulations of the government body having jurisdiction over it, and, subject to receipt of a written request from a Holder, within a reasonable period, furnish to such requesting Holder updates and information as may be reasonably requested by the Holder pertaining to the Issuer's business or operations affecting the Issuer's ability to perform its obligations under the LTNCDs;

e. duly and punctually comply with all reporting, filing and similar requirements imposed by the BSP, the SEC and the PSE in accordance with any applicable Philippine law and regulations from time to time relating to the LTNCDs and the Contracts;

f. fully and satisfactorily comply with all BSP directives, orders, issuances, findings, and letters, including those regarding its capital, licenses, risk management, and operations and satisfactorily take corrective measures that may be required under BSP audit reports;

g. ensure that the LTNCDs are insured with, and continue to be insured by the PDIC, and shall comply with all rules and regulations of the PDIC;

h. use the net proceeds from the LTNCDs in accordance with the purpose of issuance provided in the Offering Circular;

i. pay all indebtedness and other liabilities and perform all contractual obligations pursuant to all agreements to which it is a party or by which it or any of its properties may be bound, except those being contested in good faith and by proper proceedings; or as could not be reasonably regarded to have a Material Adverse Effect on its business, assets, condition or operations;

j. ensure that any documents related to the LTNCDs will, at all times, comply in all material respects with the applicable laws, rules, regulations, and circulars, and, if necessary, make the appropriate revisions, supplements, and amendments to make them comply with such laws, rules, regulations, and circulars;

k. as soon as possible and in any event within five (5) Banking Days after the occurrence of any default on any of the obligations of the Issuer, or other event which, with the giving of any notice and/or with the lapse of time, would constitute a default under any agreement of the Issuer with any party, including, without limitation the Contracts, serve a written notice to the Holders, through the Registrar and Paying Agent, of the occurrence of any such default, specifying the details and the steps which the Issuer is taking or proposes to take for the purpose of curing such default, including the Issuer's estimate of the length of time to correct the same;

l. ensure that there shall at all times be a Registrar and Paying Agent for the purposes of the LTNCDs, as provided in the Registry and Paying Agency Agreement;

m. when so requested in writing, provide any and all information reasonably needed by the Market Makers, the Paying Agent and/or Registrar, as the case may be, to enable them to respectively comply with their respective responsibilities and duties under the Regulations and the Contracts; provided, that, in the event that the Issuer cannot, for any reason, provide the required information, the Issuer shall immediately advise the party requesting and shall perform such acts as may be necessary to provide for alternative information gathering;

These covenants of Issuer shall survive the issuance of the LTNCDs up to Maturity Date, and shall be complied with and performed fully and faithfully by the Issuer at all times while the LTNCDs or any portion thereof remains outstanding.

13. Events of Default

The Issuer shall be considered in default under the LTNCDs in case any of the following events shall occur:

a. *Non-payment.* The Issuer fails to pay any principal and/or interest due on the LTNCDs.

b. *Non-performance.* The Issuer fails to perform any of its undertakings, covenants, or obligations under this Certificate.

c. *Representation/Warranty Default.* Any of the representations and warranties by the Issuer herein is or becomes untrue or misleading while the LTNCDs or any portion thereof remain outstanding.

d. *Levy on the Bank's Assets.* Any judgment, writ, warrant of attachment or execution, or similar process shall be issued or levied against all or more than half of the Issuer's assets and such judgment, writ, warrant, or similar process shall not be released, vacated or fully bonded within thirty (30) days after its issue or levy.

e. *Suspension of Operation.* The government or any competent authority takes any action to suspend the whole or the substantial portion of the operations of the Issuer, or condemns, seizes, or expropriates all or substantially all of the properties of the Issuer.

f. *Voluntary Suspension of Operation.* The Issuer voluntarily suspends or ceases operations of a substantial portion of its business for a continuous period of fifteen (15) days, except in the case of strikes or lockouts when necessary to prevent business losses, or when due to fortuitous events or force majeure, or when there is no Material Adverse Effect on the business operations or financial condition of the Issuer.

g. *Judgment and Final Award.* Any final and executory judgment, decree, or arbitral award for the sum of money, damages, fine, or penalty in excess of Pesos: Five Hundred Million (₱500,000,000.00) or its equivalent in any other currency is entered against the Issuer and the enforcement of which is not stayed, or is not paid, discharged, or duly bonded within thirty (30) days after the date when payment of such judgment, decree or award is due under the applicable law or agreement.

h. *Indebtedness. (i)* Any indebtedness of the Issuer with respect to borrowed money (such as bills payable and deposits) is not paid when due; or (ii) any indebtedness of the Issuer with respect to borrowed money (such as bills payable and deposits) becomes (or is capable of becoming) fully due and repayable prematurely by reason of a default under the document relating to such indebtedness; provided, that in any of the foregoing cases, the aggregate amount of indebtedness exceeds ₱500,000,000.00 or its equivalent in any other currency.

i. *Insolvency.* The Issuer becomes insolvent or is unable to pay its debts when due, or commits or permits any act of bankruptcy, including (i) filing, in accordance with applicable laws and regulations, of a voluntary or involuntary petition by or against the Issuer, as the case may be in any bankruptcy, reorganization, winding-up, suspension of payment, liquidation, or other analogous proceeding; (ii) the appointment of a trustee or receiver over all or a substantial portion of its assets, and such appointment is not lifted, discharged, or dismissed within thirty (30) days from the Issuer's receipt of notice of such appointment; (iii) the making of an assignment for the benefit of its creditors over all or substantially all of its assets; (iv) admission in writing of its inability to pay its debts; or (v) entry of any final and executory order or judgment of any court, tribunal, or administrative agency or body confirming the insolvency of the Bank, or approving any reorganization, winding-up or liquidation, of the Bank or a substantial portion of its assets.

14. Effects of Default

In the case of any of the Events of Default referred to in the following Events of Default above: items (a): Non-Payment or (i): Insolvency ("Acceleration Event of Default"), a Holder may, without need of any notice, demand, presentment, waiver, consent, or approval from any other Holder, by notice to the Registrar stating the Acceleration Event of Default relied upon, declare the principal and all accrued interest (including default interest, as specified below) and other charges (including any incremental tax that may be due on the interest income already earned under the LTNCDs), if any, insofar as the particular LTNCDs registered under such Holder's name in the Registry are concerned, to be immediately due and payable.

The Registrar, within three (3) Banking Days from receipt of the notice from the Holder of the occurrence of an Acceleration Event of Default, shall issue a Notice of Declaration of Default to the Issuer.

For the avoidance of doubt, a Holder need not be joined with any other Holder to declare the Issuer in default due to an Acceleration Event of Default with respect to the particular LTNCDs registered under its name as appearing in the Registry. Nothing herein, however, shall be construed as conveying upon a Holder the right and privilege to declare the principal or accrued interest including Default Interest, as specified below, or other charges (including any incremental tax that may be due on the interest income already earned under the relevant LTNCDs), if any, on any or all other LTNCDs as immediately due and payable.

Upon the occurrence of any Event of Default other than an Acceleration Event of Default referred to in the following Events of Default above: items: (b) Non-performance; (c) Representation/Warranty Default; (d) Levy on the Bank's Assets; (e) Suspension of Operation; (f) Voluntary Suspension of Operation; (g) Judgment and Final Award; and (h) Indebtedness ("Non-Acceleration Event of Default"), the Registrar, within three (3) Banking Days from receipt of notice from the Holder of the occurrence of a Non-Acceleration Event of Default, shall issue a Notice of Meeting to all the Holders of the Certificate. In the said meeting, the Holders holding, representing or accounting for more than fifty percent (50.0%) of the aggregate outstanding principal amount of the LTNCDs (the "Majority Holders") shall determine whether it shall waive the Non-Acceleration Event of Default. If the Non-Acceleration Event of Default is not waived by the Majority Holders, the Registrar shall, within three (3) Banking Days from receipt of the notice from the Majority Holders that the Non-Acceleration Event of Default has not been waived, issue a Notice of Declaration Default to the Issuer and declare the principal and all accrued interest (including Default Interest, as specified below) on all the LTNCDs and other charges thereon (including any incremental tax that may be due on the interest income already earned under the LTNCDs), if any, to be immediately due and payable; provided, that the Majority Holders may, by written notice to the Issuer thereafter rescind and annul such declaration and its consequences or waive any past default of the Issuer under the LTNCDs (other than a breach of any Acceleration Event), upon such terms, conditions and agreements, if any, as they may determine; but no such rescission and annulment shall extend or shall affect any subsequent default or shall impair any right arising therefrom. Any such waiver shall be conclusive and binding upon all the Holders and upon all future Holders and owners of such LTNCDs, or of any Certificate issued in lieu thereof or in exchange therefor, irrespective of whether or not notation of such waiver is made upon the LTNCDs.

In case any amount payable by the Issuer under the LTNCDs, whether for principal, interest, or otherwise, is not paid on due date, the Issuer shall, without prejudice to its obligations to pay the said principal, interest, and other amounts, pay interest on the defaulted amount(s) at the rate of one percent (1.0%) *per month* or twelve percent (12.0%) *per annum*, net of applicable withholding taxes (the "Default Interest") from the time the amount falls due until it is fully paid.

15. Payment in the Event of Default

Subject to the applicable laws of the Philippines on bankruptcy, winding-up or liquidation and the preferences established by law and under the Master Certificate, the Issuer covenants that upon the occurrence of any Event of Default, then in any such case, the Issuer will pay to the Holders, entitled to such payment, through the Registrar, the whole amount which shall then have become due and payable on all such outstanding Certificate with interest at the rate borne by the LTNCDs on the overdue principal, net of applicable withholding taxes, and with Default Interest thereon, when applicable, and, in addition thereto, the Issuer will pay to the Registrar the actual amounts to cover the cost and expenses of collection, including reasonable compensation to the Registrar, its agents, attorneys and counsel, and any reasonable expenses or liabilities incurred without negligence or bad faith by the Registrar.

16. Application of Payments

Subject to the Registry and Paying Agency Agreement, any money delivered to the Paying Agent upon the occurrence of an Event of Default shall be applied by the Paying Agent in the order of preference as follows: *first,* to the pro-rata payment to the Registrar, Paying Agent, Selling Agents, and Market Maker, and its agents, attorneys and counsel, of their costs, expenses, fees, and other charges, including reasonable compensation to them, their agents, attorneys, and all reasonable expenses and liabilities incurred or disbursements made by them, without negligence or bad faith, including any costs, expenses, fees and other charges resulting from an Event of Default; *second*, to the payment of all outstanding interest then due and unpaid on the LTNCDs owing to the Holder(s), including the default interest in the order of the due dates for the payment of such interests; *third*, to the payment of the whole amount of the principal; *and fourth*, the remainder, if any, shall be paid to the Issuer, its successors, or assigns, or to whoever may be lawfully entitled to receive the same, or as a court of competent jurisdiction may direct.

17. Remedies; Ability to File Suit; Limitations

(a) All remedies conferred by these Terms and Conditions to the Holders shall be cumulative and not exclusive and shall not be so construed as to deprive the Holders of any legal remedy by judicial or extra judicial proceedings appropriate to enforce such direct rights under these Terms and Conditions.

(b) No delay or omission by the Holders, or any one of them, to exercise any right or power arising from or on account of any Event of Default hereunder shall impair any such right or power, or shall be construed to be a waiver of any such Event of Default or an acquiescence thereto; and every power and remedy given by these Terms and Conditions to the Holders may be exercised from time to time and as often as may be necessary or expedient.

(c) Nothing herein shall be deemed to create a partnership or collective venture between the Holders. Each Holder shall be entitled, at its option, to take independent measures with respect to its obligations and rights and privileges under these Terms and Conditions with respect to the particular Certificate registered under its name as appearing in the Registry, and it shall not be necessary for the other Holders to be joined as a party in any judicial or other proceeding for such purpose.

(d) Notwithstanding any other provisions in these Terms and Conditions, in no instance shall any of the parties be liable for special, indirect, consequential, nominal, exemplary, or punitive damages (including, without limitation, any loss of profits, business or anticipated savings).

18. Notices

All notices, statements, and requests hereunder shall be in writing and shall be sent by personal delivery, courier, registered mail with postage prepaid, confirmed facsimile, confirmed electronic mail, or such other method as is deemed acceptable under the circumstances, to the party at its respective address, facsimile number, and e-mail address and for the attention of the specified representative, as set forth as follows:

(a) To the Issuer/Selling Agent:

Union Bank of the Philippines
UnionBank Plaza, Meralco Avenue corner Onyx and Sapphire Roads,
Ortigas Center, Pasig City
Tel. No.: (632) 638 0352
Fax No.: (632) 638 0368
E-mail: jrsreyes@unionbankph.com
Attention: Jesus Roberto S. Reyes

(b) To the Selling Agents:

The Hongkong and Shanghai Banking Corporation Limited
HSBC Centre, 3058 Fifth Avenue West
Bonifacio Global City, Taguig City
Tel. No.: (632) 834 7425
Fax No.: (632) 755 5474
E-mail: corriepurisima@hsbc.com.ph
Attention: Maria Corazon D. Purisima

Multinational Investment Bancorporation
22nd Floor, Multinational Bancorporation Center,
6805 Ayala Avenue, Makati City
Tel. No.: (632) 811 0059

Fax No.: (632) 819 0347
E-mail: dcaguiat@mib.com.ph
Attention: Dindo Antonio T. Caguiat

(c) To the Registrar and Paying Agent

Deutsche Bank AG, Manila Branch
Global Transaction Banking
Direct Securities Services
23/F Tower One, Ayala Triangle
Ayala Avenue, Makati City
Tel. No.: (632) 894 6976
Fax No.: (632) 894 6977
E-mail: hannah-vina.nunez@db.com
Attention: Hannah Nuñez

All notices shall be deemed to have been duly given on the date of receipt (if delivered personally), or the date ten (10) Banking Days after posting (if sent by registered mail), or the date of transmission with confirmation (if transmitted by telefax or electronic mail), or the date of receipt (if sent through other means). Each party may change its addressee, address, facsimile number, or e-mail address for purposes of receiving written notice under this Certificate.

For security and quality of service purposes, all telephone and other communications between the parties and the Holders may be recorded in any manner, and the Holders shall be deemed to have consented to such recording and to the production of such recordings as evidence in any proceedings brought in connection with the LTNCDs.

19. Meetings of the Issuers

All meetings of the Holders shall be held in Pasig City upon prior notice.

Subject to the terms of the Registry and Paying Agency Agreement, notice of every meeting of the Holders, setting forth the time, place, and purpose of such meeting in reasonable detail, shall be sent by the Registrar to the Issuer and to each of the registered Holders not less than fifteen (15) days nor more than forty-five (45) days prior to the date fixed for the meeting and shall likewise be published in at least two (2) newspapers of general circulation in the Philippines for two (2) consecutive days at any time prior to the date stated in the notice for the date of the meeting; *provided*, that all reasonable costs and expenses incurred by the Registrar for the proper dissemination of required information on the requested meeting shall be reimbursed by the Issuer within three (3) Banking Days from receipt of the duly supported billing statement.

20. Governing Law

Laws of the Republic of the Philippines

21. Venue

In case any legal action or proceeding arising out of or in connection with these Terms and Conditions, the exclusive venue shall be in the proper courts of the City of Manila, to the exclusion of all other courts.

PURPOSE OF ISSUANCE

The net proceeds of the issue of the LTNCDs, after deducting fees, commissions, and other related expenses will be utilized to improve the Bank's deposit maturity profile and support business expansion plans.

CAPITALIZATION AND INDEBTEDNESS

The following table sets forth the Bank's unaudited interim consolidated capitalization and indebtedness extracted from the unaudited consolidated interim consolidated financial statements of the Bank as of June 30, 2013, and as adjusted to give effect to the issuance of the LTNCDs. This table should be read in conjunction with the Bank's unaudited interim consolidated financial statements as of and for the six months ended June 30, 2013.

	As of June 30, 2013	
	Actual	As Adjusted
	(₱ in millions)	
Liabilities		
Deposit Liabilities	259,546.1	[*]
Bills Payable...	15,208.0	15,208.0
Notes Payable	3,750.0	3,750.0
Other Liabilities..	17,102.6	17,102.6
TOTAL LIABILITIES	295,606.7	[*]
Capital funds		
Common Stock[1]	6,414.2	6,414.2
Additional Paid-in Capital	5,819.9	5,819.9
Surplus Free..	37,602.3	37,602.3
Surplus Reserves	149.6	149.6
Net Unrealized Gains (Losses) On Available-for-sale Financial Assets	(4,964.7)	(4,964.7)
Non-controlling Interest.................................	12.4	12.4
TOTAL CAPITAL FUNDS	45,033.7	45,033.7
TOTAL CAPITALIZATION AND INDEBTEDNESS	**340,640.4**	**[*]**

Note: (1) Par value P10.0 per share; authorized: 670,000,000 shares; as of June 30, 2013, 641,422,420 shares of common stock were issued and outstanding.

DESCRIPTION OF THE BANK

Introduction

UnionBank is a publicly-listed universal bank. The Bank distinguishes itself through superior technology, unique branch sales and service culture, and centralized backroom operations. UnionBank's superior technology allows delivery of online, real time business solutions to meet the customers' changing and diverse needs through innovative and customized cash management products and service offerings. The Bank's unique branch sales and service culture ensures efficient and quality service as well as mitigates operational risk. Its distinct centralized backroom operations enables the Bank to provide responsive, scalable, and secure transaction processing.

Aligned with its thrust of being at the forefront of technology-based banking in the Philippines, the Bank endeavors to elevate its systems and processes to be at par with international standards and best practices. It obtained ISO 9001:2000 QMS Certification for its CPS in 2008, making it then the FIRST and ONLY bank awarded for its entire centralized backroom operations. In 2010, the Bank received ISO 9001:2008 certification, an upgrade from the previous. Thereafter, UnionBank was certified for ISO 27001:2005 Information Security Management System, attesting to the Bank's unwavering commitment to become an acknowledged leader and benchmark for service quality, technological advancement, and operational excellence. The Bank also achieved ISO 9001:2008 certifications for its Customer Service Group in 2012 and Branch Operations Management in 2013, and has consistently been certified as having zero non-conformance every year from date of certification during quality audits, demonstrating the Bank's dedication to uphold quality in its business processes.

Notwithstanding volatility in trading-related earnings, the Bank has a proven track record for delivering consistent and strong performance from treasury businesses. Gains from the Bank's treasury businesses have historically accounted for a significant and consistent portion of the Bank's operating income.

UnionBank's clientele encompasses retail, middle-market and corporate customers, as well as major government institutions. The Bank believes that its use of technology, and marketing and operational structure has enabled it to capture and secure a loyal customer base, and to achieve high levels of efficiency and productivity.

The Bank offers a broad range of products and services, which include deposit and related services; corporate and middle market lending, consumer finance loans such as mortgage, auto loans and credit card; investment, treasury & capital market; trust and fund management; remittance, cash management and electronic banking; as well as pre-need insurance through its subsidiary, First Union Plan, Inc.

The Bank's consolidated total assets amounted to ₱279.7 billion as of December 31, 2012 and reached ₱340.6 billion as of June 30, 2013. Net income was ₱7.6 billion for the year ended December 31, 2012 and ₱6.2 billion for the six months ended June 30, 2013. The Bank's Tier 1 and Total Capital Adequacy Ratios remained greater than the minimum ten percent (10.0%) regulatory requirement, ending the year 2012 at 18.0% and 20.7%, respectively. As of June 30, 2013, the Bank continued to exhibit above industry performance on key financial ratios, with return on shareholders' equity, return on assets and cost-to-income ratios at 26.7%, 4.0% and 44.9%, respectively. Based on consolidated quarterly reports filed with the Philippine SEC, the Bank's return on assets and return on shareholders' equity were the highest, and its cost-to-income ratio was the second most efficient, among private domestic commercial banks in the Philippines.

The authorized share capital of the Bank is 670,000,000 shares with a par value of ₱10.0 each. As of June 30, 2013, there were 641,422,420 issued and outstanding common shares, fully paid. Based on the closing price of its shares on the PSE on June 28, 2013, the Bank had a market capitalization of approximately ₱89.5 billion.

As of and for the year ended December 31, 2012 and as of and for the six months ended June 30, 2013, the Bank's key performance indicators were as follows:

Key Performance Indicator	Ratio		Method of calculation
	December 31, 2012	June 30, 2013	
Capital to risk assets	20.7%	19.5%	Total qualifying capital divided by total risk-weighted assets (inclusive of credit, market and operational risk charge)
Return on average assets	3.0%	4.0%	Net income divided by average total resources for the period indicated
Return on average equity	17.0%	26.7%	Net income divided by average total capital funds for the period indicated
Net non-performing loan ratio[1]	3.3%	(0.2%)	Total non-performing loans less specific loan loss reserves divided by total loans inclusive of interbank loans receivables
Non-performing loan cover	104.2%	112.6%	Total allowance for loan losses divided by total non-performing loans
Cost-to-income ratio	47.8%	44.9%	Total operating expenses divided by the sum of net interest income and other income

Note: (1) On September 2002, the BSP issued Circular No. 351 allowing banks that have no unbooked valuation reserves to exclude from non-performing classification loans classified "loss" in the latest examination of the BSP which are fully covered by allowance for impairment, provided that interest on said loans shall not be accrued. On October 16, 2012, the BSP issued Circular No. 772, amending computation of net NPL ratio effective January 2013 to exclude specific allowance for credit losses on the total loan portfolio from the gross NPLs; provided that such specific allowance for credit losses on the total loan portfolio shall not be deducted from the total loan portfolio.

UnionBank's registered office is at UnionBank Plaza, Meralco Avenue corner Onyx & Sapphire Roads, Ortigas Center, Pasig City, 1605, Philippines. The Bank provides its relevant target customers' information and transaction needs through its consolidated network of 229 strategically located branches and 267 ATMs nationwide as of June 30, 2013, supplemented by a call center under the Bank's ISO-certified Customer Service Group. To complement its brick and mortar presence and strengthen its digital footprint, UnionBank has a Web site, www.unionbankph.com. The information on the Bank's Web site is not incorporated by reference into, and does not constitute part of, this Preliminary Offering Circular.

History

UnionBank, originally known as "Union Savings and Mortgage Bank", was incorporated in the Philippines on August 16, 1968. The Bank's common shares were listed in the PSE on June 29, 1992.

It was granted the license to operate as a universal bank on July 15, 1992. UnionBank became the 13th and youngest universal bank in the country in only its 10th year of operation as a commercial bank.

The Bank's major shareholder groups include Aboitiz Equity Ventures, one of the largest conglomerates in southern Philippines engaged primarily in the business of power generation and distribution, financial services, real estate, food manufacturing and industrial production; Social Security System ("SSS"), the country's provider of social security to workers in the private sector; and Insular Life Assurance Co., Ltd., one of the leading and largest Filipino-owned life insurance companies in the Philippines.

UnionBank has undertaken two bank mergers with Interbank in 1993 and iBank in 2006, catapulting it to being one of the 10 largest universal banks in the Philippines based on asset size.

On January 8, 2013, UnionBank's BOD approved the purchase of CitySavings, a premier thrift bank specializing in granting teachers' loans under the DepEd's APDS, at a purchase price of ₱5.7 billion based on 2.5 times the audited book value of CitySavings' shares as of December 31, 2012. The transaction was approved by the Monetary Board of the BSP on March 21, 2013. The acquisition of CitySavings is aligned with the Bank's business plans and long-term strategy of building businesses based on consumers.

Competitive Strengths

The Bank considers the following to be among its principal competitive strengths:

The Bank is a leading bank in providing technologically advanced and customized products and services to cater to the specific needs of its customers.

The Bank is an established and recognized provider of technologically advanced banking products and services in the Philippines. The Bank believes that it has successfully established itself as a leading bank in using state-of-the-art technology to provide advanced banking solutions to customers, and this has enabled it to capture and secure a loyal customer base. In particular, the Bank believes that it has established itself as a market leader in certain key products and services, including corporate cash management solutions in which the Bank is able to utilize information technology in a cost-efficient manner to offer tailor-made solutions to customers. The Bank's electronic payment products and services have been adopted by several Government agencies, including the BIR, the SSS, Philhealth, Pag-Ibig and the Philippine Bureau of Customs ("BoC"). To provide corporate customers with a seamless filing and payment convenience, Bank launched the OneHub.Gov asthe first and only single Web platform offering in the Philippines that enables customers to make online payments to, and file salary loan payments and tax returns to, five government agencies, including the BIR, the SSS, Pag-IBIG, the Philippine BoC and Philhealth electronically.

The Bank's unique branch sales and service culture ensures efficient and quality service as well as mitigates operational risk.

Consistent with its purpose of "Making Da Diff", UnionBank veered away from the traditional channel-centric organizational structure. The Bank made a strategic decision to separate the branch sales and service functions with distinctly defined performance metrics, aligned with its thrust of building a customer- and product-centric sales and service organization.

To complement its branch banking franchise, it developed the entrepreneurial expertise of Relationship Managers ("RMs") in spotting and anticipating the needs of its customers. It has, likewise, defined an RM-to-branch ratio aimed at enhancing person-to-person relationship and bringing the bank closer to its target customers.

To ensure efficient and quality service and to mitigate operational risk, the Bank has honed the competencies of its branch operations managers as "franchise protectors". As a safeguard against conflict of interest, its physical branch network serves as a control mechanism that allows for check and balance in meeting the transactional requirements of its customers, geared towards providing relevant, compliant and problem-free service.

The Bank is able to maintain operational cost efficiencies, anchored on its centralized backroom operations.

The Bank is able to maintain operational efficiencies by streamlining operation processes through the use of technology, and believes that its continued use of technology and its operational structure has enabled the Bank to achieve high levels of efficiency and productivity. Its distinct centralized backroom operation enables the Bank to provide responsive, scalable, and secure transaction processing. For the six-month period ended June 30, 2013, the Bank, with a cost-to-income ratio of 44.9%, was the second most efficient among private domestic commercial banks in the Philippines. The Bank also ended the period as being one of the most productive, measured by deposit per branch and asset per employee ratios.

As part of its initiatives to instill a culture of "continuous improvement", the Bank continually sends high potential employees to Six Sigma Black and Green belt training programs. The Bank also developed its own six sigma orange belt training program, candidates from which are responsible for regularly initiating process improvement projects with supervision from Green and Black belts. The Bank adopts the Define-Measure-Analyze-Improve-Control methodology for all its quality improvement projects. To engrain its unwavering commitment for service quality and productivity, the Bank has made the Black Belt certification as an imperative for the career movement of its executives involved in operations. The Bank is keen on transforming Open Source systems into valuable business tools to more efficiently and better meet its customer service requirements.

The Bank enjoys consistent and strong performance from treasury businesses.

Treasury businesses form a significant part of the Bank's assets and overall operations. The Bank has strong domestic and foreign currency securities trading and investment portfolios which have yielded consistent and robust returns as well as an experienced Trading, Positioning and Funds Management ("TPFM") team with proven ability to execute a business plan and achieve results. Gains from the Bank's treasury businesses have historically accounted for a significant and consistent portion of the Bank's operating income. For the years ended December 31, 2010, 2011 and 2012, gains from securities and foreign exchange trading comprised 27.8%, 34.9% and 37.2% of operating income (comprising net interest income and other operating income), respectively. For the six months ended June 30, 2012 and 2013, the gains from securities and foreign exchange trading comprised 39.1% and 44.1% of operating income, respectively**.**

Strategy

The Bank's corporate vision is to become one of the leading banks in the Philippine market in respect to market capitalization, profits and customer coverage. To achieve this vision, it has adopted five (5) key strategic imperatives, called "FOCUS", which is an acronym for the following:

- Financial Value: Enhance the financial value of the Bank's operations;
- Operational Excellence: Increase productivity while reducing costs;
- Customer Franchise: Increase customer base and reduce customer attrition;
- UnionBank Brand/Experience: Establish a unique brand image in strategic markets; and
- Superior Innovation: Continue to offer innovative products and services.

The Bank will continue to selectively consider opportunities for acquisitions as they arise in order to support its growth strategy under its FOCUS strategy.

Financial Value: Enhance the financial value of the Bank's operations

The Bank aims to increase its return on equity by expanding its various business lines through the expansion of its customer base, the introduction of new products and services, and exploring new methods of product marketing and sales. To achieve this objective, the Bank actively develops certain areas of its business operations, including but not limited to, cash management services and products, consumer finance, credit card, treasury businesses, and trust activities. The Bank entered into new markets by further developing commercial lending and banking services to the middle market segment and maximized sales and profits by offering customized marketing and sale of the Bank's products and services through its branches. The Bank also increased its corporate lending activities, which have been maintained at lower levels since the Asian economic crisis in 1997 to minimize credit risk, to obtain a more balanced asset portfolio.

Operational Excellence: Increase productivity while reducing costs

The Bank aims to reduce its operating costs while improving its productivity and quality of service. To achieve this objective, the Bank intends to continue to streamline its operations and processes and minimize costs by eliminating redundancies, automating processes, and institutionalizing a high-standard quality of service throughout the Bank's operations. The Bank obtained ISO certification for its Central Processing Services in 2008, Information Security Management System in 2010, Customer Service Group in 2012 and Branch Operations Management in 2013. Thereafter, it has consistently been certified as having zero non-conformance every year from date of certification during quality audits, demonstrating the Bank's dedication to uphold quality in its business processes.

Customer Franchise: Increase customer base and reduce customer attrition

The Bank intends to increase and diversify its customer base by introducing new and more customized products and services to cater to a wider range of customers. To complement its brick and mortar presence, the Bank has defined a 2:1 RM-to-branch ratio with the end-objective of bringing the Bank closer to its target customers. To stimulate an increase in deposits, the Bank has, among other things, introduced a "Business Class" priority banking account for affluent retail customers and opened a "Business Class" lounge in 2005, specifically designed and created for the Bank's private banking and "Business Class" clients. As of June 30, 2013, ₱259.5 billion worth of deposit accounts was opened and outstanding with the Bank, which represented an increase of 53.7% as compared to ₱168.8 billion worth of deposit accounts as of June 30, 2012. In addition, with an enhanced branch network and widened coverage area, the Bank expects to be able to increase sales opportunities by continuing to transform its branches into business centers through which its consumer and corporate products and services are offered directly to customers. In recognition of its efforts in engaging customers and widening loyal customer base, the Bank is able to continually grow its customer accounts, expanding by more than 366,000 to 5.1 million as of June 30, 2013 from 4.8 million as of year-end 2012.

UnionBank Brand/Experience: Establish a unique brand image in strategic markets

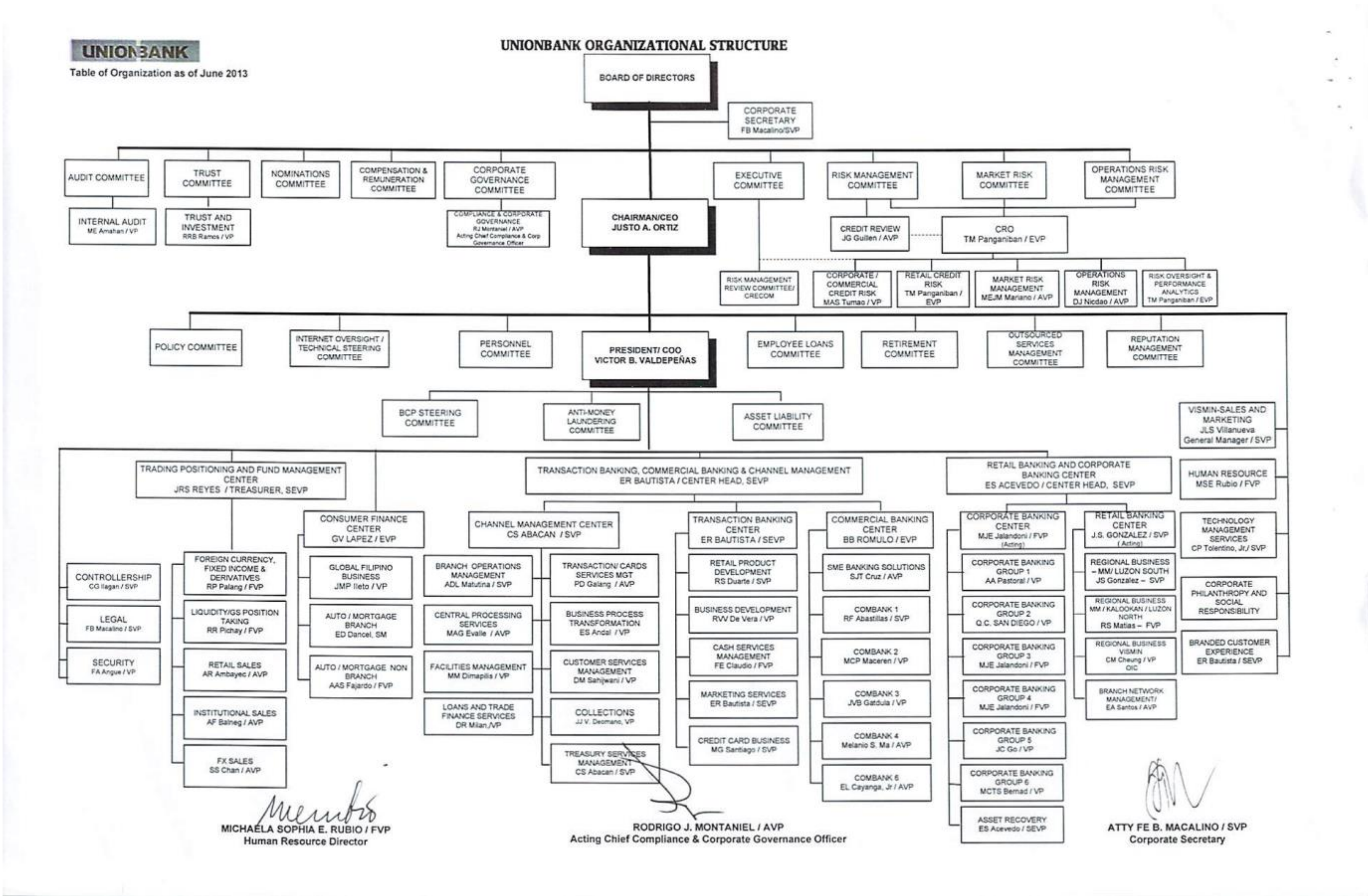
The Bank aims to distinguish itself from its competitors by establishing a unique brand image in strategic markets. To achieve this goal, the Bank braved to venture into the bold and dynamic new colors of tangerine orange and royal blue as it changed its brand in 2008 and positions itself to challenge conventions for smarter solutions for its customers. The Bank's REaCh program emboldens and fortifies its brand attributes of being relevant, expert, and challenging convention. The Bank seeks to remain at the forefront of technology-based banking in the Philippines. The Bank believes that its internet banking platform offers a strong competitive advantage as it enables a much wider range of banking services to be transacted via the internet. The Bank also believes that information technology is a strategic tool of its business operations to gain a competitive advantage in client and transaction management and that its use of technology has enabled it to achieve high levels of efficiency and productivity. The Bank intends to continue to focus on changes in customer needs and technological advances by developing and introducing technologically advanced products and services that enable customers to achieve greater levels of operational and financial efficiencies.

Superior Innovation: Continue to offer innovative products and services

To maintain its competitiveness, the Bank aims to continuously develop and offer innovative products and services, underpinned by its passion on transforming ideas in providing greater value for their target customers and the communities they serve. The Bank believes that many of its products and services contain features that are more technologically advanced than its competitors, shaping its public image of being a "high-tech" service bank. To further foster this image, the Bank continuously seeks to apply advanced technologies to allow delivery of online, real time information and business solutions to meet the diverse and changing needs of its customers.

Organizational Structure

The following chart sets out an overview of the functional organizational structure of the Bank and its key divisions as of June 2013:



Business of the Bank

Overview

The Bank's core businesses are retail banking, consumer finance, corporate banking, commercial banking (comprising middle-market banking), cash management, trust banking, and treasury, funding and trading (involving management of the Bank's liquidity and funding requirements and handling of transactions in the financial markets covering foreign exchange, fixed income trading and investments, and derivatives). These business activities are categorized into, and undertaken by, the following business centers: the Retail Banking Center, the Consumer Finance Center, the Corporate Banking Center, the Transaction Banking Center, the Commercial Banking Center, the Trust Investment Services Group, and the Trading, Positioning and Fund Management Center. Head office operations of each of the business centers and internet banking operations of the Bank are undertaken by its Channel Management Center.

Retail Banking

The Bank's retail banking activities are undertaken through the Retail Banking Center, which principally involves offering deposit products and services to retail customers comprising individuals, small businesses and sole proprietorships. The Bank's deposit products and services are also accessible to the customers through the Bank's sophisticated internet banking network, where customers can also check their balances, pay bills, transfer funds, execute wire transfers, order checkbooks, print statements and issue stop payment orders on a real-time basis.

Deposit Products

The Bank offers a comprehensive range of deposit products that contain features that are tailored to each segment's financial profile and other characteristics. The Bank's deposit products consist principally of the following:

- peso demand deposits, which do not accrue interest or accrue interest at a rate that is lower than the rate applicable to time deposits and allow customers to deposit or withdraw funds at any time;
- peso savings deposits, which allow customers to deposit and withdraw funds at any time and accrue interest at a rate set by the Bank;
- peso time deposits, which generally require customers to maintain a deposit for a fixed term during which interest accrues at a fixed rate and any withdrawal before maturity may only be made by paying penalties;
- U.S. dollar savings deposits, which require customers to maintain a deposit of at least U.S.$500 and allows customers to withdraw funds at any time and accrue interest at a rate set by the Bank;
- U.S. dollar time deposits, which generally require customers to maintain a deposit of at least U.S.$1,000 for a fixed term during which interest accrues at a fixed rate and any withdrawals before maturity may only be made by paying penalties; and
- other foreign currency time deposits, which allow customers to deposit funds denominated in Sterling Pounds, Euro, Japanese Yen or Australian dollars, generally requiring the customer

to maintain a minimum deposit amount (which varies depending on the currency of deposits) for a fixed term during which interest accrues at a fixed rate and any withdrawals before maturity may only be made by paying penalties.

The Bank offers varying interest rates on its deposit products depending on market interest rates, the rate of return on its earning assets and interest rates offered by other commercial banks. Deposits by retail customers as of December 31, 2012 and June 30, 2013 amounted to ₱114.0 billion and ₱147.5 billion, respectively, representing 60.0% and 56.8%, respectively, of the Bank's total deposits. To widen its potential customer base, the Bank has introduced a basic banking service in the form of the "EON" Visa Electron debit cards. The "EON" debit card does not have minimum opening and maintaining balance requirement. The Bank does not charge any fees for transactions made through the internet. Depending on the type and frequency of the transaction as well as the channel used to avail of the services, the Bank charges a fee between ₱10.0 and ₱15.0. As of June 30, 2013, the Bank had 386,769 EON debit cardholders. The Bank also offers "Business Class" priority banking accounts, which are targeted specifically at, and available only to, affluent retail customers with a total relationship balance of ₱1,000,000 (or its equivalent in other currencies). The "Business Class" priority banking account offers special services, such as dedicated service counters at selected branches of the Bank, financial advisory service, preferential pricing on its retail banking products and a wide range of electronic banking services, such as internet and mobile phone banking services.

Consumer Finance

The Bank's consumer finance activities are undertaken through the Consumer Finance Center. The Bank offers various types of consumer finance products to individuals, which consist principally of residential mortgage loans, auto loans, salary loans and credit cards.

The Bank reviews various factors in pricing its loan products, including the capacity of the borrower to repay the loan, estimated delinquency rates, funding costs, expenses related to making loans and a target spread. Loan terms are differentiated according to factors such as a customer's financial condition, loan purpose, collateral and the quality of relationship with the Bank.

As of December 31, 2012, the Bank's consumer finance portfolio was divided as follows: 50.8% residential mortgage, 30.4% auto loans and 18.8% credit cards. As of June 30, 2013, the proportions were 53.1% residential mortgage, 27.1% auto loans and 19.8% credit cards. This is in line with the Bank's strategy of achieving a more sustainable, risk-adjusted portfolio mix.

Residential Mortgage Loans

The large majority of the Bank's residential mortgage loans are extended to property buyers in the Philippines who intend to occupy the premises, with a small proportion being extended to individuals purchasing residential units for investment purposes. All of the Bank's home mortgage loans are secured by a first mortgage on the property. In addition, the Bank generally requires residential mortgage borrowers to have an equity interest equal to at least twenty percent (20.0%) to thirty percent (30.0%) of the value of the property. For residential mortgage loans guaranteed by the Home Guaranty Corporation ("HGC"), the Bank requires borrowers to have an equity interest of at least ten percent (10.0%) of the value of the property. Maturity of residential mortgage loans typically ranges from five (5) to 15 years. Interest rates are re-priced periodically based on prevailing market rates. Fixed rate options are also offered to provide flexibility to borrowers.

The Bank’s total residential mortgage loans as of December 31, 2012 and June 30, 2013 amounted to ₱15.0 billion and ₱14.7 billion, respectively. The Bank intends to increase its residential loan portfolio by actively marketing its residential loan products through its branch network and in partnership with leading property developers. This allows customers to apply for residential loans directly at any one of the Bank's branches and through developer sales offices and project sites.

When a borrower falls in arrears with its mortgage payments, it can either agree to a voluntary disposition of the property to the Bank or the Bank may commence foreclosure proceedings. Once the mortgaged collateral is foreclosed, the Bank classifies such collateral as ROPA and thereafter, it is managed by the Bank’s Asset Recovery Group (the “ARG”). Mortgaged collateral that has been foreclosed is generally sold by the Bank in public auctions. However, the individual mortgagor continues to have the right to repurchase such collateral within a year from the date of foreclosure in return for payment of principal and interest owed plus the Bank’s out-of-pocket expenses. See “Business - Corporate Banking Center - Asset Recovery”. In the case of residential mortgage loans guaranteed by the HGC, the Bank does not foreclose on the mortgaged collateral. Instead, the Bank files a claim with the HGC when a HGC guaranteed residential mortgage loan is in default for at least six (6) consecutive months. In general, the Bank receives the proceeds of the guarantee from the HGC within two (2) to three (3) months from the date on which a claim is filed.

Auto Loans

The Bank generates new auto loans through car dealerships, independent sales agents and the Bank’s branch network. Auto loans generated through the Bank's branches are sourced mostly from existing depositors and referral customers.

All of the Bank’s auto loans are secured by a chattel mortgage over the car being purchased. In addition to being subject to the Bank’s internal credit checks, the Bank generally requires the borrower to make a minimum down payment of twenty percent (20.0%) of the purchase price for a new car, and twenty-five percent (25.0%) to thirty percent (30.0%) in the case of a second-hand car. Maturity of auto loans generally ranges from 12 to 60 months with interest rates fixed over the life of the loan. When an installment payment falls 90 days past due, the Bank may commence foreclosure proceedings. Foreclosed cars are generally sold by the Bank through public auction. (See “Business - Corporate Banking Center - Asset Recovery”.)

Auto loan advances as of December 31, 2012 and June 30, 2013 amounted to an aggregate of ₱9.0 billion and ₱7.5 billion, respectively.

Salary Loans

The Bank offers salary loan products to the following target markets, principally through its thrift banking arm, CitySavings:

- Government teachers – salary loans under the DepEd’s APDS,
- Salary loans to private and other government employees, and
- Salary loans to employees of the Aboitiz group and affiliates.

CitySavings’ main product is its salary loan extended to public school teachers under the APDS which has been its market since inception. With over 40 years experience in this market, CitySavings’ salary loans to the teachers' market have grown to comprise more than 90.0% of its total loan portfolio as of June 30, 2013.

The guidelines for the grant of salary loans to teachers are contained in the Memorandum of Agreement ("MOA") between the DepEd and CitySavings. Among other things, the MOA stipulates the granting of right or authority to the DepEd in setting the interest rate and other fees on salary loans. The MOA is effective for five (5) years.

As of June 30, 2013, teachers' loans amounted to ₱16.9 billion, 99.8% of which is accounted for by salary loans to public school teachers while the remaining is attributable to other borrowers.

Credit Cards

Products

The Bank's credit cards were launched in 1999. As a late entrant, the Bank adopted a segmentation strategy to gain market share. The Bank has customized card products that would fit various market segments. It has used geographic, psychographic and behavioral variables to identify specific, unique and under-served market needs and customized unique products for particular market segments.

Credit card balances net of reserves as of December 31, 2012 amounted to ₱2.6 billion. Beginning in 2010, the credit card group shifted acquisition strategies to focus on the premium card segment. As a result, the bank has been able to increase the profitability of the portfolio, despite reducing the number of cards in force. Reflecting the success of this strategy, net income before operating expenses per live card increased from ₱2,074.0 to ₱4,585.0 between 2009 and 2012 respectively. Interest charged on revolved outstanding balance and deferred/installments payments ranges from 1.7% to 3.5% per month while annual fees range from ₱1,500.0 to ₱3,000.0.

As of June 30, 2013, the Bank has 303,699 cards in force. It is ranked No. 4 among Visa member banks. Its products include the UnionBank Classic, Gold and Platinum cards. It has more than 50 co-brand/affinity credit cards in partnership with companies and institutions such as retail, educational, medical, financial, service institutions, life and non-life insurance and airline to provide unique offers to each partner's customer base. The Bank has also a unique array of Specialty Credit Card products which includes Bai Visa, the first and only regional specialty card in the country focusing on the unique characteristics of Cebuanos and Cebu life as a region. In 2012, the Bank launched its latest travel specialty credit card, Miles+ Visa Platinum Card, the card that gives you unique travel experiences and the freedom to choose your travels rewards.

Corporate Banking

The Bank's corporate banking activities comprise principally of deposit and cash management products and loans offerings to large corporate customers. Corporate banking activities are undertaken through its Corporate Banking Center. The customer accounts under this group belong to the top tier corporations, conglomerates, and large multinational companies.

Deposit Products

The Corporate Banking Center offers a comprehensive range of deposit products that target different segments of the corporate market. To generate deposits and expand its corporate banking business, the Center is also focused in becoming the customers' main operating bank by meeting the cash management requirements of its top corporate customers by offering collection, disbursement and payroll solutions aside from the traditional deposit products and credit facilities. This initiative, in coordination with the Transaction Banking Center, will leverage on the Bank's technological ability to customize its products and services to meet customer needs.

Deposits by corporate customers as of December 31, 2012 and June 30, 2013 amounted to ₱38.7 billion and ₱76.4 billion, respectively, representing 20.4% and 29.4%, respectively, of the Bank's total deposits.

Loan Products

The Bank provides a wide range of loan products and services to its corporate customers, including revolving credit lines, foreign currency loans, bills purchased, acceptances, trade finance facilities, project finance, term loans and collective credit cards. It continues its corporate lending activities to obtain a more balanced asset and liability portfolio wherein thirty percent (30.0%) of its assets are from corporate loans. These are viewed as high credit quality loans and are complementary to the Bank's Cash Management business.

Most of the Bank's corporate clients are based in the Philippines and are engaged in real estate, utilities, infrastructure, manufacturing and communications. Facilities offered to corporate customers include both secured and unsecured loan products, depending on the credit risks associated with the customer and their business. The Bank primarily provides short- to medium-term financing on a bilateral basis or participates in syndicated loans.

As of June 30, 2013, the Bank's total loans made out to large corporate customers amounted to ₱28.1. billion. Including remedial accounts and contract to sell financing to corporate customers, the total portfolio of the Corporate Banking Center amounted to ₱32.1 billion in the same period.

Commercial Banking

The Bank's Commercial Banking Center provides loan products and services to customers from the middle-market. While predominantly consisting of small- to medium-sized enterprises ("SMEs") and individual entrepreneurs, the Bank adopts an expanded middle market definition by including in this portfolio all accounts that are managed like a family corporation, where decision making is centralized among family members as opposed to corporates that are usually run by professionals. The loan facilities provided to middle-market customers are predominantly composed of self liquidating working capital facilities, which include promissory note lines, various discounting lines, and trade finance lines, among others. The Bank also provides working capital funding via its SME Banking program, which offers a loan product that is fully secured by the customers' deposits or real property.

The Bank believes that the development and expansion of its middle-market customer base is essential to the growth and success of the Bank and intends to concentrate on growing its middle-market portfolio as one of the Bank's core target customer groups. Aligned with the Bank's focus on deepening customer relationship through cross-selling, loan services are bundled with cash management, treasury and trust banking products and services. The Bank will provide these regional middle-market customers with convenient channels for addressing their borrowing and cash management requirements, by offering a personalized and enhanced banking experience. The Bank believes that its current and target customer base will be receptive to the cross-selling of the wide variety of products and services both on the assets and liabilities side of the business.

The Bank is also seeking to expand its middle-market customer base through its "Community Banking" program. Under this initiative, the Bank leverages on its relationships with existing middle-market customers to identify their suppliers, customers and other business relationships and engage them as prospective clients.

As of June 30, 2013, the Bank had about 2,400 middle-market and SME Banking customers with total loans amounting to around ₱24.3 billion. Contingent assets covering various import and domestic letters of credit and standby letters of credit amounted to ₱3.3 billion for the same period.

Cash Management

The Bank offers cash management products and services to its corporate customers through its Transaction Banking Center. The Bank's cash management products and services consist of a wide range of custom-tailored disbursement, remittance, collection and information portal solutions, which the Bank believes are among the most technologically-advanced corporate cash management solutions available in the Philippines.

The Transaction Banking Center delivers its cash management products primarily through internet banking. Corporate customers can use the Bank's internet channel to electronically collect, disburse and reconcile payments, provide cash-flow related information, and make bulk payments through multiple payment methods. The Bank believes that it is one of the few local banks that provide comprehensive, sophisticated and customized cash management products to large local and multinational companies as well as middle-market customers in the Philippines. Notwithstanding that the Bank utilizes a standard operating system for all of its electronic cash management products, the Bank is able to specifically design and alter the interface of each cash management product to meet the specific needs of its customers with the end objective of helping them increase productivity, achieve cost efficiency and generate savings. This is very much in line with the Bank's purpose of fulfilling dreams and elevating the lives of its corporate customers and its stakeholders. To deliver this objective, the Bank embarks on technology-driven innovations and customizations of user interfaces and systems. One such product is the electronic invoice processing and payment (EIPP) system developed in 1997 for the fast consumer goods market, under which the Bank's customers, and their suppliers and vendors can submit invoices and receive and make payments through the internet. Like all of the Bank's cash management products, the interface of each electronic payment system is specifically designed for each customer segment. To demonstrate the Bank's customization strategy, EIPP is presently being enhanced to cater to new market segments such as the healthcare, utility and property management companies.

The Bank's electronic payment products and services have been adopted by several Government agencies, including the BIR, the SSS, Philhealth, Pag-Ibig and the Philippine BoC. To provide corporate customers with a seamless filing and payment convenience, the Bank launched the OneHub.Gov, the first and only single Web platform offering in the Philippines that enables customers to make online payments, and file salary loan payments and tax returns to five government agencies, including the BIR, the SSS, Philhealth, Pag-IBIG and the Philippine BoC electronically.

In 2004, the Bank won the bid to develop an electronic payment system for Government Service Insurance System ("GSIS") and its members, and subsequently launched the multi-functional GSIS eCard program. The GSIS eCard functions as a Visa card, a debit card, an ATM card and a biometric-based identity card through which GSIS members can also access their GSIS social security benefits such as pension schemes as well as apply for GSIS salary loans through any of these channels. Since its implementation, the GSIS eCard program has significantly improved the efficiency of the GSIS payroll and security system. The GSIS eCard program has been lauded as a model for e-commerce compliance in relation to government agencies by Visa International during its global conference on prepaid cards held in Prague on May 18, 2006.

The Bank also offers electronic bill collection services to companies that have a large customer base, such as credit card, insurance, power and utility companies. These services allow customers to make payments to these companies at branches of the Bank and through the Bank's internet Web site and ATMs.

In 2013, after passing a rigorous accreditation process, the Securities Clearing Corporation of the Philippines and PSE officially announced the addition of UnionBank as a Settlement Bank in the MOA signing held in May. As an accredited settlement bank, broker firms can now open trading accounts with UnionBank for the settlement of trade transactions. Out of the seven (7) settlement banks, UnionBank has recorded a milestone by being the only applicant bank to have passed the system testing in a single try without any errors as commended by Mr. Hans B. Sicat, PSE President and Chief Executive Officer.

As a result of embarking on numerous innovations and customization initiatives, the Bank has received recognitions from several award-giving bodies:

- 2008: Innovation Award from Financial Insights Innovation Awards
- 2010: Preferred Local Cash Management Bank from the Asian Banker
- 2013: Domestic Cash Management Bank of the Year from Asian Banking and Finance

In providing Cash Management products and services, the Bank requires its customers to maintain a minimum contractual average deposit balance and/or pay a transaction fee, depending on the nature and complexity of the required products and services.

Trust Banking

The Bank provides a wide range of trust products and services through its Trust and Investment Services Group ("TISG"). The TISG is a full service trust banking unit, which offers fund management, investment management services, custody, administratorship and collateral agency services and stock and transfer agency services, among others. In addition to offering trust services to corporate customers, the TISG provides retail customers with alternative investment opportunities through its investment fund products.

Funds managed by the TISG are sourced from corporate and retail customers. As of December 31, 2012, 58.0% of its total managed funds consisted of funds from institutional trust and agency customers, 18.9% from individual trust and agency accounts, 0.7% from other fiduciary accounts and the remaining 22.4% from the Bank's unit investment trust fund ("UITF") products. As of June 30, 2013, 59.2% of its total managed funds consisted of funds from institutional trust and agency customers, 13.3% from individual trust and agency accounts, 0.8% from other fiduciary accounts and the remaining 26.7% from the Bank's UITF products. Currently, the Bank manages nine UITF products, which are primarily marketed to retail customers. The funds seek long-term capital appreciation and are largely invested in fixed income securities of the Government and equity securities of financially sound corporations.

Total assets held in trust as of December 31, 2012 and June 30, 2013 amounted to ₱36.3 billion and ₱37.5 billion, respectively.

In accordance with regulations governing the conduct of trust business by banks, the TISG reports directly to the Bank's Trust Committee, which is composed of three members of the BOD, the President of the Bank and the Head of the TISG. The Trust Committee is, in turn, directly responsible to the Bank's BOD. All investment decisions of the TISG in respect of discretionary accounts must be approved by the Trust Committee.

Treasury Business

The Bank's treasury, funding and trading businesses are undertaken by its TPFM Center, which also has primary responsibility for managing the Bank's sources of funding, and ensuring that the Bank has adequate liquidity at all times. In addition, the TPFM Center manages the Bank's domestic and foreign currency-denominated investment instruments. The TPFM Center actively engages in trading for its own proprietary account, as well as for individual and institutional investors who are customers of the Bank. The TPFM Center also engages in derivatives transactions for proprietary position-taking, to hedge the Bank's foreign exchange and interest rate risks, as well as to service the hedging requirements of its clients. Finally, the TPFM Center is responsible for conducting the Bank's foreign exchange business and trust banking business.

The TPFM Center relies on Guava, which is an integrated system that performs front, middle and back office functions, including deal entry, accounting, risk management and information reporting. The Guava enables the TPFM Center to manage a large volume of foreign exchange, money market and derivative transactions efficiently.

Trading and Investment Securities

The TPFM Center manages the domestic and foreign currency securities trading and investment portfolios of the Bank. As an accredited Government Securities Eligible Dealer, the Bank has been an active participant in the trading of Government securities, the majority of which are normally in the form of Treasury notes. By holding most of its trading and investment securities in Treasury notes, the Bank is able to efficiently manage its liquidity risks. The Bank also invests mostly in foreign currency-denominated Government bonds to match its foreign currency-denominated liabilities, namely its foreign currency deposits, thereby reducing its foreign exchange risks.

Trading and investment securities as of December 31, 2012 and June 30, 2013 amounted to ₱89.0 billion and ₱92.8 billion, respectively, accounting for 31.8% and 27.2%, respectively, of the Bank's consolidated total resources. As of December 31, 2012 and June 30, 2013, government securities accounted for 69.2% and 70.2%, respectively, of the Bank's trading and investment securities portfolio.

For the year ended December 31, 2012, the Bank's interest income on trading and investments securities of ₱3.7 billion and securities trading gains of ₱6.5 billion represented 17.3% and 29.8%, respectively, of its gross income. For the six months ended June 30, 2013, the Bank's interest income on trading and investments securities of ₱1.8 billion and securities trading gains of ₱5.6 billion represented 12.0% and 37.2%, respectively, of its gross income.

The following table sets out, as of the dates indicated, information relating to the Bank's total investment portfolio:

	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
			(₱ in millions)		
Government securities……	59,433.0	63,297.2	61,579.7	64,637.3	65,129.0
Other debt securities…..….	9,559.4	21,316.7	19,058.7	20,660.9	18,825.9
Total debt securities…….	68,992.4	84,613.9	80,638.4	85,298.2	83,954.9
Non-debt securities………	6,745.9	5,678.7	8,573.7	5,461.7	9,124.1
Total………..……..……...	**75,738.3**	**90,292.6**	**89,212.1**	**90,759.9**	**93,079.0**
Allowance for impairment	263.0	278.2	256.3	263.7	259.4
Total……………………..	**75,475.3**	**90,014.4**	**88,955.8**	**90,496.2**	**92,819.6**

Derivatives

The Bank has a Type 2 derivative license to engage in the trading of derivative instruments, such as currency and interest rate swaps, currency and interest rate forward contracts, financial futures and options both for its proprietary and customers' accounts. Derivative transactions are entered into for the purpose of hedging currency, interest rate and liquidity risks. Guava enables the Bank to monitor the risks inherent in derivatives.

Asset Recovery Group

The Bank's ARG is responsible for the remedial management, loan restructuring and asset recovery activities of all business centers within the Bank. Once the security over the collateral provided by either retail or corporate borrowers is foreclosed, such collateral is classified as ROPA and is managed by the Bank's ARG. As of December 31, 2012, the Bank's ROPA amounted to ₱9.8 billion. Of this amount, ₱323.5 million and ₱73.9 million represented the Bank's holdings in automobiles and chattels, respectively, and the remainder represented the Bank's holdings in real property which comprised of 843 properties. As of June 30, 2013, the Bank's ROPA amounted to ₱10.3 billion. Of this amount, ₱430.7 million and ₱73.9 million represented the Bank's holdings in automobiles and chattels, respectively, and the remainder represented the Bank's holdings in real property which comprised of 1,290 properties.

The Bank generally sells its real estate ROPA through property auctions and negotiated sales. Real estate ROPA is generally sold on an installment basis over a period of 15 years and the Bank requires purchasers to make an initial down payment of at least ten percent (10.0%) of the offered price. With respect to the installment payments, which are referred to as "sales contract receivables" ("SCR"), the Bank generally charges interest of 11.0% per annum for the entire 15 years. Titles to the ROPA remain with the Bank until it receives full payment of the purchase price. Under SCR, upon default, the purchaser is deemed to forfeit all of his/her prior principal payments and the Bank records such prior payments as rental over the property while the remaining unpaid balance of the SCR will be booked as ROPA. Once the Bank repossesses the ROPA, that property is resold through auctions or negotiated sales.

For the year ended December 31, 2012, the Bank sold ₱1.6 billion worth of real estate ROPA. For the six months ended June 30, 2013, the Bank sold ₱409.9 million worth of real estate ROPA. Real estate ROPA sales settled in cash for the year ended December 31, 2012 and for the six months ended June 30, 2013 amounted to ₱300.4 million and ₱160.2 million, respectively, while the remainder was sold on installment.

The Bank also generates earnings from its real estate ROPA by leasing them on a short-term basis.

Marketing

Direct marketing and sales of the Bank's products and services are undertaken through RMs. RMs are primarily responsible for marketing retail and corporate deposit products and cross-selling other products and services of the Bank. The Bank believes that such an arrangement, as opposed to placing branch managers in charge of marketing, allows RMs to focus solely on marketing and sale of its products, which reduces inefficiencies, removes potential conflicts inherent in having the same person handling both sales and credit review, and maximizes sales. In addition, this increases the depth of relationships established with customers, which is in line with the localized customer service structure of UnionBank, and helps to create marketing and sales opportunities at each of its branches. The Bank also aims to grow its deposits, increase cross-selling of financial products and reduce costs through its network of RMs to minimize its capital expenditures.

With respect to the Bank's products that involve credit risk, RMs may only offer those products on pre-determined terms and conditions. The Bank compensates its RMs based on the value and quality of new business brought. The Bank believes that such an arrangement motivates RMs to maximize sales volumes, thereby facilitating continuous growth in deposits while improving internal controls.

To ensure the quality of and to improve the marketing skills of RMs, prospective RMs are required to undergo classroom and on-the-job training at the Bank's Relationship Manager Academy, which was established in 2003. RMs are also required to undergo periodic refresher courses. As of June 30, 2013, the Bank had a total of 427 RMs.

Branch Network

UnionBank ended 2012 with 186 branches nationwide. Select branches were relocated to strategic areas situated within and outside of Metro Manila to maximize visibility and expand customer reach. The branches have user-friendly terminals and a Web-based Signature Verification System (SVS), which promotes efficient processing of teller transactions. Customers can do over-the-counter (OTC) withdrawals and check encashment at any UnionBank branch. High-volume transaction branches are provided with Transaction Assistant Portal (TAP), an in-house developed self-service innovation, which aims to facilitate faster processing time through paperless transactions and use of a card that stores bills payment and account information. The Bank's Check Verification System utilizes Philippine Clearing House Corporation's check images, instrumental in enabling fast and reliable check clearing.

The following table sets out details of the Bank's consolidated branches and ATMs in the Philippines in operation as of the specified dates:

	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
Metro Manila	117	121	122	121	122
Other areas of Luzon	31	32	33	32	48
Visayas	21	20	19	20	43
Mindanao	17	16	12	16	16
Total	**186**	**189**	**186**	**189**	**229**
ATMs	**214**	**224**	**232**	**223**	**267**

The Bank provides 24-hour banking services through its 267 ATMs, which are located in its branches as well as at off-site locations, such as office buildings of selected key clients, hospitals and entertainment/shopping centers. Customers are given access to the ATM facilities through ATM cards, which are issued to checking and savings account holders. The Bank also is a member of Bancnet, Expressnet and Megalink, which are ATM networks that allow its customers to use ATM terminals operated by other banks in the same network. Through these networks, customers have access to approximately 9,000 additional ATMs nationwide.

The Retail Banking Center manages the entire physical branch network of the Parent Bank and monitors each branch's profitability closely. Branch managers, through their respective area or region heads, regularly communicate with the Retail Banking Center to discuss branch performance. In addition, each branch is subject to an annual operations review by the Bank's Compliance Division, as well as a comprehensive annual audit.

Call Center

Retail customer relationship and care is handled by the Bank's 24-hour call center, catering to deposit and card product queries, among others. The call center utilizes a mix of phone, postal mail, email, fax and internet as customer touch points. In handling customer complaints, it adheres to certain service-level agreements such as feedback or resolution of ATM-related concerns within five (5) Banking Days and redelivery of card within Metro Manila after five (5) days. Customer complaint handling is continuously improved through resolution tracking.

Information Technology

The Bank's Technology Management Services ("TMS") is responsible for the proper and efficient functioning of the Bank's information technology systems and infrastructure. The TMS manages the Bank's network of 267 ATMs as of June 30, 2013 and oversees the Bank's system and office automation software, hardware and network facilities.

Currently, the Bank's deposit system is operated by Infosys Finacle core banking system and its ATM network is operated by Base24 Tandem S7800. The Bank electronically stores its data in an EMC Symmetrix DMX3 disk storage system with replicating facilities. The Bank currently uses the CardPro system to manage its credit card business. The major modules in the system include card management, card authorization, card application processing and scoring, card embossing, statement processing and interfaces to the Bank's ATM network.

The Bank believes that the technologically advanced products and services it offers have shaped its image of being a "high-tech" service bank. The Bank continues to focus on changes in customer needs and technological advances by developing and introducing technologically advanced products and services that enable customers to achieve greater levels of operational and financial efficiencies. The Bank has dedicated substantial efforts to ensure security in its information technology systems. The Bank maintains three (3) storage areas in different off-site locations to store vital records of the Bank.

Acknowledging its reliance on technology, as part of the Bank's business continuity plan, the Bank undertook a Mirroring project in 2007. It is a major Information Technology initiative which mirrors the two sites of the Bank for its failover scheme to achieve disaster readiness. It is a resilient and dynamic technology on data replication, offering flexibility in choosing between the Bank's data centers in capturing real time transactions. This is a first in the Philippine banking industry, attesting to the Bank's commitment to remain at the forefront of technology.

Channel Management Center

All of the Parent Bank's head office operations, back-office operations of each of the other business centers and internet banking operations are currently undertaken by the Bank's two central processing units, one located in Makati City (Metro Manila) and the other in Cebu City. The Bank believes that such an arrangement eliminates operation process redundancy, reduces processing errors and benefits the Bank through economies of scale. The Bank's Channels Management Center also oversees these operations, which eliminates further redundancies and helps to institutionalize a high-standard quality of service throughout the Bank's operations.

Subsidiaries and Allied Undertakings

Universal banks in the Philippines, such as the Bank, may invest in the equity of banking-related companies or "allied undertakings." Financial allied undertakings include leasing companies, banks, investment houses, financing companies, credit card companies and financial institutions catering to small- and medium-scale businesses.

A publicly-listed universal or commercial bank in the Philippines may own one hundred percent (100.0%) of the voting stock of only one other commercial bank. Such universal or commercial bank may only have ownership in additional commercial banks as a minority shareholder. A universal bank may also own up to one hundred percent (100.0%) of the voting stock of thrift banks and rural banks, and generally up to one hundred percent (100.0%) of other financial and non-financial allied undertakings. Prior approval from the Monetary Board is required for investments in allied and non-allied undertakings. The total investments in equities of allied and non-allied enterprises shall not exceed fifty percent (50.0%) of the net worth of the investing bank, subject to the further requirement that the equity investment in one enterprise, shall not exceed twenty-five percent (25.0%) of the net worth of the investing bank.

As of the date of this Preliminary Offering Circular, the Bank had a total of nine (9) wholly-owned subsidiaries, out of which four (4) are currently inactive companies, and investments in one (1) allied undertaking, which is also currently inactive. As of June 30, 2013, none of the Bank's subsidiaries accounted for 10.0% or more of the consolidated net profit and loss or has a book value of 10.0% or more of the consolidated total assets.

A brief description of the Bank's subsidiaries and allied undertakings are set out below:

Union Properties, Inc. (UPI)

UPI was incorporated and registered with the SEC on December 23, 1993. It is presently engaged in the administration and management of the Parent Company's premises and other properties such as buildings, condominium units and other real estate, wholly- or partially- owned by the Bank. Pursuant to the action of the BOD of UPI approving the amendment of its Articles of Incorporation on May 13, 2004, the primary purpose of UPI was changed from a real estate developer to a real estate administrator. The SEC approved such amendment on December 13, 2004. Through its wholly-owned subsidiaries, FUPI and FUDC, UPI is also engaged in the sale of pre-need plans and marketing of financial products. For the year ended December 31, 2012, UPI's net income amounted to ₱4.9 million while its net loss for the six months ended June 30, 2013 was ₱14.2 million.

First Union Direct Corporation ("FUDC")

FUDC was established in 1999 and is a wholly-owned subsidiary of UPI. It is a direct selling company that is principally engaged in the marketing of retail financial services and related products, such as credit cards of the Bank and pre-need pension plans of FUPI. For the year ended December 31, 2012, FUDC's net income amounted to ₱2.5 million while its net loss for the six months ended June 30, 2013 was ₱0.5 million.

First Union Plans, Inc. ("FUPI")

FUPI was established in 2000 and is a wholly-owned subsidiary of UPI. FUPI is principally engaged in the business of selling pre-need pension plans to retail customers. For the year ended December 31, 2012, FUPI's net income amounted to ₱139.7 million while its net income for the six months ended June 30, 2013 was ₱177.6 million.

First Union Insurance and Financial Agencies, Inc. ("FUIFAI")

FUIFAI is a wholly owned subsidiary of UPI. FUIFAI was registered with the SEC on February 18, 2000 and started commercial operations on the same date. The company was organized primarily to engage in the business of a general agent for life and non-life insurance, and other allied financial services.

UnionBank Currency Brokers Corp. ("UCBC")

UCBC was registered with the SEC on June 14, 1994. It was organized to engage in the foreign currency brokerage business. On March 23, 2001, the BOD of UCBC approved the cessation of its business operations effective on April 16, 2001. Since then, UCBC's activities were significantly limited to the settlement of its liabilities.

Union Data Corporation ("UDC")

UDC was registered with the SEC on September 8, 1998. It was organized to handle the centralized branch accounting services as well as the processing of credit card application forms of the Parent Company and the entire backroom operations of FUPI. On July 1, 2003, the BOD of UDC approved the cessation of its business operations effective on August 30, 2003. The services previously handled by UDC are presently under the Centralized Processing Service unit of the Parent Company.

UBP Insurance Brokers, Inc. ("UBPIBI")

UBPIBI was initially established to engage in insurance brokerage business. It was incorporated and registered with the SEC on February 27, 1992. In 1995, UBPIBI ceased its operations and as of the date of this Preliminary Offering Circular, there are no definite plans as to its future business operations. UBPIBI is currently an inactive company.

UBP Securities, Inc, ("UBPSI")

UBPSI was incorporated and registered with the SEC on March 2, 1993. It was organized to engage in the business of buying, selling or dealing in stocks and other securities. In January 1995, as approved by UBPSI's stockholders and BOD, UBPSI sold its stock exchange seat in the PSE to an affiliate of the Parent Company. Accordingly, UBPSI ceased its stock brokerage activities and has settled and liquidated its customers' positions.

Interventure Capital Corporation ("IVCC")

IVCC was incorporated and registered with the SEC on October 16, 1980. It was organized to develop, promote, aid and assist financially any small- or medium- scale enterprise, and to purchase, receive, take or grant, hold, convey, sell, lease, pledge, mortgage and otherwise deal with such real and personal property, including securities and bonds of other corporations as the transaction of the lawful business of the corporation may reasonably and necessarily require, subject to the limitations prescribed by law and the constitution. IVCC has ceased operation since 1992.

City Savings Bank, Inc. ("CitySavings")

CitySavings was incorporated and registered with the SEC on December 9, 1965. It was organized to provide financial services to people of moderate means. The Cebu-based thrift bank is primarily engaged in extending salary loans to public school teachers under the DepEd's APDS and in accepting deposits from the public through its branches nationwide. Its net income attributable to equity holders of the Parent for the six months ended June 30, 2013 was at ₱314.5 million.

OTHER MATTERS (GENERAL INFORMATION)

Insurance

The Bank's policy is to adequately insure all of its properties (including ROPA) against fire and other risks inherent to its business. The Bank also has a policy of requiring appropriate insurance coverage for any collateral provided by its customers. The Bank's insurance policies are subject to exclusions which are customary for insurance policies of the type held by the Bank, including those exclusions which relate to war and terrorism-related events.

Consistent with standard practice in the Philippine banking industry, the Bank does not have business interruption insurance covering loss of revenues in the event that its operations are affected by unexpected events, since it has determined that its existing insurance policies and the security systems in place, including off-site backup for its data systems to minimize operational down-time, provide sufficient security against loss resulting from business interruption.

The Bank believes that its insurance policies as described above are appropriate for its business.

Properties

As of June 30, 2013, the Bank owned 26 properties (excluding ROPA) with an aggregate floor area of approximately 70,241.7 square meters in the Philippines. Most of these properties are used as banking offices for its head office, branch offices or for back office operations. These properties are not subject to any mortgage, lien or encumbrance. In addition, the Bank also leases properties with an aggregate floor area of approximately 35,908.7 square meters in the Philippines. These leased properties are used as banking offices for the Bank's 215 branches. The Bank paid ₱400.5 million in rentals for the year ended December 31, 2011 and ₱399.3 million for the year ended December 31, 2012. The average term of these leases is five (5) years.

Save as disclosed above and excluding its ROPA portfolio, the Bank does not own any other real property.

Intellectual Property

The Bank has registered a number of trademarks and tradenames, including the logo of the Bank, "UnionBank" and "Union Bank of the Philippines". Patents registered by the Bank include the UnionBank business check writing system and device. The Bank also has a number of registrations filed with the Intellectual Property Office at the Department of Trade and Industry of the Philippines, which are currently pending. The Bank has registered all of its registrable intellectual property rights with the Intellectual Property Office. The Bank has not been the subject of any disputes relating to its intellectual property rights.

Legal Proceedings

The Bank is a defendant/respondent in various legal actions, most of which are claims for damages arising in the ordinary course of business. The results of these actions, however, are not expected to have a material effect on the Bank's financial position. The Bank is not aware of (1) any bankruptcy petition filed by or against any business of which a director, person nominated to become a director, executive officer, or control person of the Bank was a general partner or executive officer either at the time of the bankruptcy or within two years prior to that time; (2) any director, person nominated to become a director, executive officer, or control person of the Bank being convicted by final judgment in a criminal proceeding or being subject to a pending criminal proceeding; (3) any order, judgment, or decree, not subsequently reversed, suspended or vacated, of any court of competent jurisdiction, permanently or temporarily enjoining, barring, suspending or otherwise limiting the involvement of any director, person nominated to become a director, executive officer, or control person of the Corporation in any type of business or banking activities.

ASSETS AND LIABILITIES

The tables below and accompanying discussions provide selected financial highlights regarding the Bank's assets and liabilities. The following audited information (except for June 30, 2012 and 2013) should be read together with the Bank's consolidated financial statements included in this Preliminary Offering Circular as well as "Risk Management" and "Business".

Funding

The Bank's funding operations are designed to ensure both a stable source of funds and effective liquidity management. The Bank's main sources of funding are time, savings and demand deposits. Deposits represented 93.2% of the Bank's sources of funding as of June 30, 2013. As of the same period, time, savings and demand deposits represented 56.4%, 9.8% and 33.8%, respectively, of total consolidated deposits of ₱259.5 billion. In recent years, the Bank has made directed efforts to increase its deposit base. The Bank also sources its funding requirements from the interbank market and general financings.

Sources of Funding

The following table sets out an analysis of the Bank's principal funding sources and the average cost of each funding source for the periods indicated:

	As of December 31					
	2010	**Average cost of funding(1)**	**2011**	**Average cost of funding(1)**	**2012**	**Average cost of funding(1)**
	(₱ in millions, except for percentages)					
Deposits by currency:						
Peso	141,738.3	2.5%	144,808.0	2.5%	150,782.5	1.9%
Foreign	51,581.2	1.3%	61,845.3	1.4%	39,058.9	1.3%
Total	**193,319.5**	**2.1%**	**206,653.3**	**2.1%**	**189,841.4**	**1.7%**
Borrowings:						
Peso	5,251.0	7.8%	3,931.4	7.0%	3,903.2	5.4%
Foreign (included under bills payable)	7, 182.4	0.8%	5,437.8	1.1%	18,388.1	1.0%
Total	**12,433.4**	**6.6%**	**9,369.2**	**5.4%**	**22,291.3**	**3.8%**

	As of June 30			
	2012	**Average cost of funding(1)**	**2013**	**Average cost of funding(1)**
	(₱ in millions, except for percentages)			
Deposits by currency:				
Peso	115,207.9	2.1%	205,106.1	1.8%
Foreign	53,605.6	1.4%	54,440.0	1.3%
Total	**168,813.5**	**1.9%**	**259,546.1**	**1.7%**

Borrowings:				
Peso	7,284.3	6.4%	9,445.8	6.6%
Foreign (included under bills payable).	9,720.5	1.1%	9,512.2	0.7%
Total	**17,004.8**	**4.2%**	**18,958.0**	**2.7%**

Note: (1) Average cost of funding represents total interest expense for the year, divided by the average daily liability for the respective period, expressed as a percentage.

Deposits

Historically, the Bank's principal source of deposits is its retail banking customers. As of December 31, 2012, retail banking customers accounted for approximately 60.0% of the Bank’s consolidated total deposit liabilities while customers of corporate banking and treasury accounted for the balance at 20.4% and 19.6%, respectively.

The Bank believes its proportion of traditional current account deposits is high amongst participants in the industry, thereby providing the Bank with a high level of low-cost funds. The Bank’s foreign currency deposits and funding are primarily handled through its FCDU operation, which is permitted to accept deposits and extend credit in foreign currencies. As of June 30, 2013, the Bank’s foreign currency deposits made up 24.8% of its total deposits.

The Bank has expanded its sources of funds in order to diversify the scheduled maturities of deposits and maintain a funding portfolio that will enable it to achieve funding stability, liquidity, and reduce the discrepancies between its loan and deposit maturities. The Bank has also introduced or plans to introduce internal and external programs to encourage increases in deposits, particularly traditional demand and savings deposits.

As of June 30, 2013, 43.6% of the Bank’s outstanding deposits were demand and savings deposits which can be withdrawn on demand without any prior notice from the customer.

The general increase in deposits was primarily the result of the Bank's efforts to expand its deposit business, as well as the growth of the Philippine economy. The following table sets out an analysis of the maturities of the deposit base of the Bank:

	As of December 31			**As of June 30**	
	2010	**2011**	**2012**	**2012**	**2013**
			(₱ in millions)		
Demand……………………………	109,468.2	114,752.3	62,811.8	72,728.7	87,824.4
Savings…………………. ………..	25,208.4	22,521.9	23,868.7	17,817.4	25,418.6
Time…….…………………………					
Up to one year……………….	58,486.3	69,091.4	102,878.1	78,103.0	139,749.6
Up to five years……………..	150.0	132.4	80.8	164.4	454.1
Over five years………………	6.6	155.3	202.0	-	6,099.4
Total time deposits…………..	58,642.9	69,379.1	103,160.9	78,267.4	146,303.1
Total………………………………	**193,319.5**	**206,653.3**	**189,841.4**	**168,813.5**	**259,546.1**

The Bank also maintains credit lines with domestic commercial banks and financial institutions in the interbank market primarily for treasury management purposes. Interbank borrowings are typically for short-term duration of between one day and a few weeks. Interbank deposits do not usually form a significant part of the Bank’s funding base but, together with the Philippine government bond market, are important in the management of the Bank's liquidity. The BSP is a lender of last resort to the Philippine banking industry. The Bank has not had to resort to this facility but has managed its liquidity through its participation in the interbank market in the Philippines.

The Bank is a member of the PDIC which insures all deposits up to a maximum of ₱500,000.00 per depositor. The PDIC is funded by semi-annual assessment fees at a prescribed percentage of the Bank's deposit liabilities less certain exclusions.

Bills Payable

The Bank's bills payable represent borrowings from local and foreign banks. As of December 31, 2012 and June 30, 2013, bills payable amounted to ₱18.5 billion and ₱15.2 billion, respectively, of which 99.2% and 62.5%, respectively, are denominated in foreign currencies.

Subordinated Notes

The Bank's notes payable as of December 31, 2010 of ₱5.0 billion pertain to the outstanding balance of unsecured subordinated notes (the "Notes"), of which ₱3.7 billion was issued by the Bank on October 14, 2009 due on October 14, 2019 and callable on October 15, 2014; and ₱1.3 billion was issued by the former iBank on March 23, 2006 due on September 24, 2016 and callable on September 26, 2011. On July 22, 2011, the BOD approved to exercise the call option on the latter unsecured subordinated note. Accordingly, on the call option date of September 26, 2011, the Bank exercised the option and redeemed the outstanding note from Noteholders. Consequently, the balance of the Notes as of December 31, 2012 and 2011 amounted to ₱3.7 billion. No gain or loss was recognized on the transaction.

Among the significant terms and conditions of the Notes follow:

- The Notes were issued on the initial issue date at 100% of the face value of the Notes. Subsequent issuance of the Notes, if any, will be issued at par, discount or premium depending on market conditions at the time of its issuance (and will include a price adjustment for the interest accrued as of the initial issue date) based on a formula to be uniformly applied per tranche;

- The Notes shall not be used as collateral for any loan made by the Parent Company or any of its subsidiaries and affiliates. The Noteholders or their transferees shall not be allowed, and waive their right to set-off any amount that may be due to the Parent Company;

- The Notes constitute direct, unconditional, unsecured and subordinated obligations of the Parent Company. Claims of Noteholders in respect of the Notes shall at all times rank pari passu and without any preferences among themselves; and,

- The Notes shall not be redeemable or terminable at the instance of the Noteholders before the maturity date, unless otherwise expressly provided therein.

The ₱3.7 billion Notes bear interest at the rate of 7.375% per annum payable quarlterly in arrears to the Noteholders on October 14, January 14, April 14, and July 14 of each year, with the first interest payment date on January 14, 2010 for the period from and including the issue date up to but excluding the first Banking Day of the 21st interest period (if the call option is not exercised) or the call option date (if the call option is exercised). The interest rate from and including October 14, 2014 up to but excluding October 14, 2019 will be reset and such step-up interest rate shall be payable to the Noteholders beginning on the 21st interest period up to the last interest period in the event that the Parent Company does not exercise the call option.

On the other hand, the ₱1.3 billion Notes bore interest at the rate of 9.5% per annum payable semi-annually in the arrears to the Noteholders on September 23 and March 23 of each year, with the first interest payment date on September 23, 2006 for the period from and including the issue date up to but excluding the last day of the 11th interest period (if the call option was not exercised) or the call option date (if the call option was exercised).

Interest expense on notes payable amounted to ₱0.3 million in 2012, ₱0.4 million in 2011 and ₱0.4 million in 2010 and is included under the Interest Expense on Bills Payable and Other Liabilities account in the statements of income.

Liquidity

The Bank manages its liquidity to meet financial liabilities arising from the withdrawal of deposits, repayments of deposits at maturity and working capital needs. Funds are required to create assets in the form of loans and extensions of other forms of credit, investments in securities, trade financing, and capital investments. The Bank seeks to ensure sufficient liquidity through a combination of active management of liabilities, a liquid asset portfolio, the securing of ample money market lines and swap lines, and the maintenance of repurchase facilities.

Currently, peso deposits and deposit substitute liabilities are subject to a Unified Reserve Requirement (URR) of eighteen percent (18.0%). On March 29 2012, the BSP issued Circular No. 753, which provided for the unification of the statutory/legal and liquidity reserves requirement. Circular No. 753 also provides guidelines for the non-remuneration of the URR, exclusion of vault cash and demand deposits as eligible forms of reserve requirement compliance. Under the same circular, the reserves are required to be in the form of deposits placed in the Demand Deposit Account (DDA) with the BSP. The BSP also requires banks to maintain foreign currency asset cover of a hundred percent (100.0%) for foreign currency liabilities of their FCDUs, of which thirty percent (30.0%) must be in liquid assets and seventy percent (70.0%) should be denominated in the same currency of such liabilities. The Bank has consistently complied with the reserve requirements for peso deposits and the cover requirements for FCDU described above.

The Bank’s liquid assets as of December 31, 2012 and June 30, 2013 amounted to ₱129.2 billion and ₱204.6 billion, respectively, representing 46.2% and 60.1%, respectively, of the Bank’s total consolidated assets. Liquid assets include cash and other cash items, due from BSP, due from other banks, interbank loans receivable and trading and investment securities.

The following table sets out information with respect to the Bank's liquidity position as of the dates indicated:

	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
	(₱ in millions, except percentages)				
Liquid assets[1]	95,742.7	138,676.1	129,151.3	128,942.0	204,565.2
Financial Ratios:					
Liquid assets to total assets	37.7%	50.9%	46.2%	53.2%	60.1%
Liquid assets to total deposits	49.5%	67.1%	68.0%	76.4%	78.8%
Net loans to total deposits	49.2%	50.8%	63.1%	51.8%	38.4%

Note: (1) Liquid assets includes cash and cash items, deposits with the BSP and deposits with other banks, interbank loans receivable and trading and investment securities but excludes held-to-maturity investments.

Loan Portfolio

As of December 31, 2012, the Bank's total loan portfolio amounted to ₱91.1 billion, representing approximately 32.6% of its total assets as of that date while the total portfolio for the six months ended June 30, 2013 amounted to ₱104.1 billion representing approximately 30.6%.

The following table sets out the Bank's consolidated gross loans and advances by principal lending units, as of the dates indicated:

	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
	(₱ in millions)				
Corporate Banking	28,737.0	26,662.0	32,100.9	30,750.3	32,121.9
Commercial Banking	19,420.6	29,023.8	25,375.4	25,636.4	24,280.5
Consumer Finance	19,878.4	25,682.2	29,503.1	28,569.6	27,763.9
Others[1]	2,759.3	3,937.2	4,145.3	2,986.5	19,975.5
Total loan portfolio	**70,795.3**	**85,305.2**	**91,124.7**	**87,942.8**	**104,141.8**

Note: (1) Others consist of: Bills Purchase, Branch Loans, Community Banking, Salary Loans, HR Loans, and other adjustments. As of June 30, 2013, Others also include the Loan Portfolio of CitySavings.

Industry Concentration

As of June 30, 2013, the real estate, renting and business service industry represented the largest sector of the Bank's consolidated loan portfolio at 24.1%. The majority of lending to the real estate, renting and business service sector takes the form of working capital loans. The Bank has no specific limits with respect to portfolio mix, except for the regulatory limits for loans to the real estate sector and credit concentration limit to a particular industry or economic activity.

Loans to real estate business are limited by BSP regulations to twenty percent (20.0%) in the aggregate of the Bank's total loan portfolio. Excluded from this ceiling are loans not exceeding ₱3.5 million to finance the acquisition or improvement of residential units, provided that the aggregate real estate loans including the loans not exceeding ₱3.5 million shall not exceed thirty percent (30.0%) of the Bank's total loan portfolio. The BSP also imposes a credit concentration limit of thirty percent (30.0%) of Total Loan Portfolio to any industry or economic activity. The Bank has historically been within the prescribed limits set by the BSP.

BSP regulations require banks to allocate twenty-five percent (25.0%) of their loanable funds for agricultural credit in general, of which at least ten percent (10.0%) must be made available for agrarian reform credit. Alternatively, a bank may temporarily meet all or a portion of its agrarian reform and agricultural lending requirements by investing in eligible government securities under certain conditions. As of December 31, 2013 and June 30, 2013, the Bank provided ₱2.0 billion and ₱2.2 billion, respectively, in agricultural loans.

The following tables set out an analysis of the Bank's loans by economic activity, as defined and categorized by the BSP:

	As of December 31					
	2010	**%**	**2011**	**%**	**2012**	**%**
	(₱ in millions, except percentages)					
Manufacturing (various industries)	5,343.0	7.6%	8,686.7	10.2%	7,382.4	8.1%
Other community, social and personal activities	6,943.7	9.8%	16,734.50	19.6%	17,792.2	19.5%
Transportation, storage and communication	14,546.1	20.5%	7,173.2	8.4%	6,345.7	7.0%
Wholesale and retail trade	5,488.4	7.8%	9,308.8	10.9%	9,708.7	10.7%
Real estate, renting and business services	15,937.9	22.5%	20,683.9	24.2%	26,013.1	28.5%
Financial intermediaries	9,443.8	13.3%	13,495.8	15.8%	13,393.2	14.7%
Private households with employed persons	785.3	1.1%	1,035.9	1.2%	1,334.7	1.5%
Electricity, gas and water	8,848.1	12.5%	6,545.1	7.7%	6,600.9	7.2%
Hotels and restaurants	338.5	0.5%	400.4	0.5%	952.2	1.0%
Others(1)	3,120.5	4.4%	1,240.9	1.5%	1,601.6	1.8%
Total	**70,795.3**	**100.0%**	**85,305.2**	**100.0%**	**91,124.7**	**100.0%**

	As of June30			
	2012	**%**	**2013**	**%**
	(₱ in millions, except percentages)			
Manufacturing (various industries)	8,462.3	9.6%	6,718.5	6.4%
Other community, social and personal activities	17,919.8	20.4%	19,177.4	18.4%
Transportation, storage and communication	6,648.2	7.6%	9,263.9	8.9%
Wholesale and retail trade	8,522.7	9.7%	9,478.8	9.1%
Real estate, renting and business services	25,336.9	28.8%	25,066.1	24.1%
Financial intermediaries	10,811.7	12.3.%	7,765.6	7.5%
Private households with employed persons	1,044.3	1.2%	1,121.1	1.1%
Electricity, gas and water	6,743.7	7.7%	8,139.1	7.8%
Hotels and restaurants	559.3	0.6%	963.3	0.9%
Others(1)	1,893.9	2.1%	16,448.0	15.8%
Total	**87,942.8**	**100.0%**	**104,141.8**	**100.0%**

Note: (1) Others include agriculture, hunting and forestry, fishing, mining and quarrying, construction, public administration and defense, education, health and social work.

The Bank intends to continue to focus its lending activities on consumer loans, SMEs and other high growth sectors of the economy, in particular the real estate, power and infrastructure industries.

The Bank maintains a flexible policy toward exposure to the Philippine economy, in principal avoiding exposure of more than thirty percent (30.0%) to a particular individual sub-sector of the economy in accordance with regulatory requirements. The Bank also monitors its exposure to specific sectors of the economy, specifically the real estate sector, to ensure compliance with specific pre-determined lending requirements imposed by law on all Philippine banks. The Bank must likewise comply with legal requirements to make loans available to SMEs. Mandatory credit allocation laws require all Philippine banks to allocate eight percent (8.0%) of their loan portfolios to small-sized enterprises and two percent (2.0%) to medium-sized enterprises.

Maturity

Over half of the Bank's loans to customers consist of loans that are due within one year. As of December 31, 2012 and June 30, 2013, loans due within one year represented 42.8% of the Bank's total loans. Loans repayable on demand principally comprise inter-bank loans, while short-term loans principally comprise loans to corporates for working capital and loans to consumers and SMEs. Medium- and long-term loans are typically granted to corporations and businesses to finance capital expenditures and mortgages advanced for property purchases. The percentage of the Bank’s loans with longer maturities has decreased recently due primarily to paydown, repayment and amortization of term loans.

The following table sets out an analysis of the Bank’s loans by maturity:

	As of December 31					
	2010	**%**	**2011**	**%**	**2012**	**%**
	(₱ in millions, except percentages)					
Within one year	29,883.1	42.3%	39,006.1	45.8%	38,924.4	42.8%
One to five years	25,900.2	36.7%	25,962.0	30.5%	27,913.1	30.7%
More than five years	14,807.4	21.0%	20,165.3	23.7%	24,147.5	26.5%
Total	**70,590.7**	**100.0%**	**85,133.4**	**100.0%**	**90,985.0**	**100.0%**

	As of June 30			
	2012	**%**	**2013**	**%**
	(₱ in millions, except percentages)			
Within one year	35,487.5	40.4%	44,450.0	42.8%
One to five years	29,193.3	33.3%	32,426.8	31.3%
More than five years	23,104.7	26.3%	26,869.2	25.9%
Total	**87,785.5**	**100.0%**	**103,746.0**	**100.0%**

Currencies

The Bank provides loans to customers in peso and certain foreign currencies. The Bank maintains its practice of extending foreign currency loans primarily to exporters who have an identifiable source of foreign currency earnings from which to repay the loans or otherwise hedged, and to importers who have authorization from the BSP to purchase foreign currency to service their foreign currency obligations.

As of June 30, 2013, 87.9% of the Bank's loan portfolio was denominated in pesos with 12.1% being denominated in foreign currencies, the majority of which comprised U.S. dollars. As of June 30, 2012, 89.9% of the Bank's loan portfolio was denominated in pesos with 10.1% in foreign currencies. Substantially, all of the Bank's foreign currency-denominated loans are loans to corporate customers.

The following table shows an analysis of the Bank's gross loans by currency:

	As of December 31					
	2010	%	2011	%	2012	%
	(₱ in millions, except percentages)					
Pesos	63,530.0	89.7%	76,131.1	89.2%	81,675.7	89.6%
Foreign currency	7,265.3	10.3%	9,174.1	10.8%	9,449.0	10.4%
Total	**70,795.3**	**100.0%**	**85,305.2**	**100.0%**	**91,124.7**	**100.0%**

	As of June 30			
	2012	%	2013	%
	(₱ in millions, except percentages)			
Pesos	79,073.2	89.9%	91,532.7	87.9%
Foreign currency	8,869.6	10.1%	12,609.1	12.1%
Total	**87,942.8**	**100.0%**	**104,141.8**	**100.0%**

Interest Rates

An important component of the Bank's asset and liability policy is its management of interest rate risk, which is the relationship between market interest rates and the Bank's interest rates on its interest-earning assets and interest-bearing liabilities. (See "Risk Management — Interest Rate Risk Management".)

The Bank's loan pricing is set by the Bank's Asset and Liability Committee. The Bank's loan pricing is driven by market factors, the Bank's funding position and the credit risk associated with the relevant borrower. The lending market in the Philippines is principally based on floating rate lending. The Bank's floating rate loans are re-priced periodically by reference to the Philippine domestic interest rates, typically by reference to a margin of between 0.5% and 5.0%, and to the Bank's internal cost of funds known as the Transfer Pool Rate plus a spread. As a result, the Bank's exposure to interest rate fluctuations is significantly reduced. (See "Risk Management— Interest Rate Risk Management".) The Bank's pricing policy with respect to its interest-bearing liabilities is set by the Bank's Asset and Liability Committee. Current account and savings account deposits do not pay any interest for deposits falling below a maintaining balance. The basic rate for savings account deposits that are above the minimum threshold is 0.10% per annum. The Bank also offers special interest rates for deposits under its time deposits account. These larger deposits are placed on pre-agreed terms and pay interest rates that generally track Philippine domestic interest rates.

Size and Concentration of Loans

The BSP generally prohibits any bank from maintaining a financial exposure to any single person or group of connected persons in excess of twenty-five percent (25.0%) of its net worth. As of June 30, 2013, the Bank's single borrower limit ("SBL"), set by the BSP, was at ₱10.4 billion. In determining whether the Bank meets the SBL, the Bank includes exposure to related accounts (including accounts of subsidiaries and parent companies of the borrower). This limit does not apply to loans which are secured with non-risk assets, including cash deposits and government securities. The Bank has complied with the SBL on all of its loans.

As of June 30, 2013, the Bank's single largest corporate borrower accounted for 4.3% of the Bank's outstanding loan portfolio. As of the same period, the Bank's ten largest performing borrowers (including groups of individuals and companies) accounted for ₱25.4 billion or 24.4% of the Bank's outstanding loan portfolio. Of the Bank's top ten borrowers, none were related parties. (See "Related Party Transactions".)

The following table presents a breakdown of total loans by principal amount as of the periods indicated:

	As of December 31					
	2010		2011		2012	
	(₱ in millions)	%	(₱ in millions)	%	(₱ in millions)	%
₱5,000,000 or less	24,383.9	34.5%	30,077.5	35.3%	33,929.6	37.2%
₱5,000,001 to ₱10,000,000	4,521.4	6.4%	6,253.3	7.3%	6,883.4	7.6%
₱10,000,001 to ₱15,000,000	2,356.9	3.3%	2,945.8	3.4%	3,019.2	3.3%
More than ₱15,000,000	39,533.1	55.8%	46,028.6	54.0%	47,292.5	51.9%
Total	**70,795.3**	**100.0%**	**85,305.2**	**100.0%**	**91,124.7**	**100.0%**

	As of June 30			
	2012		2013	
	(₱ in millions)	%	(₱ in millions)	%
₱5,000,000 or less	32,794.0	37.3%	48,914.7	47.0%
₱5,000,001 to ₱10,000,000	6,808.2	7.7%	6,595.1	6.3%
₱10,000,001 to ₱15,000,000	3,117.2	3.6%	2,896.5	2.8%
More than ₱15,000,000	45,223.4	51.4%	45,735.5	43.9%
Total	**87,942.8**	**100.0%**	**104,141.8**	**100.0%**

Secured and Unsecured Loans

The Bank principally focuses on cash flows and cash generating capabilities in assessing the creditworthiness of borrowers. However, the Bank will secondarily seek to minimize credit risk with respect to a loan by securing loans with collateral or guarantees. Where it has determined that collateralization of a loan is desirable, with respect to chattels (primarily auto loans), the Bank's policy is to secure one hundred forty percent (140.0%) to two hundred percent (200.0%) of the loan. With respect to real estate, the Bank's policy is to secure between one hundred twenty-five percent (125.0%) and one hundred sixty-six percent (166.0%) of the loan. As of June 30, 2013, approximately

22.5% of the total loans were extended on a secured basis, with approximately 61.0% of the secured loans backed by real estate mortgages.

In accordance with BSP guidelines, the Bank's policy is that the maximum loan value of real estate loans should not be in excess of seventy percent (70.0%) of the appraised value of the property provided as security for such loans, except for home mortgage loans in respect of which the maximum value should not be in excess of eighty percent (80.0%). The Bank typically reassesses mortgaged property every two years (2) in accordance with BSP guidelines. The Bank appraises real estate collateral using an internal appraiser and also uses independent appraisers when required for special cases or for regulatory compliance.

The following table sets out the Bank's secured and unsecured loans, classified (in the case of secured loans) according to type of security:

	As of December 31					
	2010	%	2011	%	2012	%
	(₱ in millions, except percentages)					
Secured:						
Government securities						
Real estate	12,241.7	17.4%	15,514.8	18.2%	14,475.4	15.9%
Chattel mortgage	7,496.5	10.6%	8,600.5	10.1%	6,692.0	7.3%
Assignment of receivables…………….	-	-	269.1	0.3%	154.3	0.2%
Mortgage trust indentures	-	-	-	-	-	-
Deposit hold-out	564.6	0.8%	2,574.5	3.0%	699.3	0.8%
Others	426.1	0.6%	1,677.5	2.0%	1,176.1	1.3%
Total Secured	20,728.9	29.4%	28,636.4	33.6%	23,197.1	25.5%
Unsecured[(1)]	49,861.8	70.6%	56,497.0	66.4%	67,787.9	74.5%
Total	**70,590.7**	**100.0%**	**85,133.4**	**100.0%**	**90,985.0**	**100.0%**

	As of June30			
	2012	%	2013	%
	(₱ in millions, except percentages)			
Secured:				
Government securities	0.0	0.0%	0.0	0.0%
Real estate	14,299.2	16.3%	14,221.3	13.7%
Chattel mortgage	6,187.0	7.0%	6,735.8	6.5%
Assignment of receivables…………….	210.4	0.2%	136.0	0.1%
Mortgage trust indentures				
Deposit hold-out	1,010.1	1.2%	848.3	0.8%
Others	597.6	0.7%	1,356.5	1.4%
Total Secured	22,304.3	25.4%	23,297.9	22.5%
Unsecured[(1)]	65,481.2	74.6%	80,448.1	77.5%
Total	**87,785.5**	**100.0%**	**103,746.0**	**100.0%**

Note: (1) Unsecured Loans consist of loans granted on clean basis, assignment of receivables, club shares, cross guaranty of Parent Company, negative pledge on all assets, surety and joint and several signatures.

Loan Administration and Loan Loss Provisioning

Loan Classifications

The Bank classifies loans as non-performing in accordance with BSP guidelines. The guidelines require banks to classify their loan portfolios based on perceived levels of risk to encourage timely and adequate management action to maintain the quality of their loan portfolios. These classifications are then used to determine the minimum levels of allowances for loan losses which banks are required to maintain. All of the Bank's risk assets, in particular the Bank's loan portfolio, are either classified or unclassified. Those loans which do not have a greater than normal risk, and for which no loss on ultimate collection is anticipated, are unclassified. All other loan accounts, comprising those loan accounts which have a greater than normal risk, are classified, as follows:

Loans especially mentioned. These are loans that the Bank believes have potential weaknesses that deserve management's close attention, and which deficiencies, if left uncorrected, could affect repayment. Weaknesses include repayment capability which may be endangered by economic/market conditions as reflected in the borrower's deteriorating financial performance, the existence of technical defects in the supporting collateral, and insufficient credit information about the borrower.

Sub-standard loans. This classification includes loans that the Bank believes represent a substantial and unreasonable degree of risk to the Bank. Those loans classified as sub-standard have a weakness that is well-defined that jeopardizes their liquidation. Such weaknesses may include adverse trends of a financial, managerial, economic or political nature, or a significant weakness in collateral.

Doubtful loans. These are sub-standard loans for which the Bank believes collection in full, either according to their terms or through liquidation, is highly improbable, and substantial loss is probable.

Loss loans. Loans which fall under this category are considered impossible to collect or are worthless.

The appropriate classification is generally made once payments on a loan are in arrears for more than 90 days, but may be made earlier when the loan is not yet past due if there are, among other things, indications of the deterioration of the creditworthiness of the borrower. Once interest on a loan is past due for 90 days, the Bank will classify the entire principal outstanding under such loan as past due, and it may initiate calling on all loans outstanding to that borrower as due and demandable.

Provisions

Under existing BSP regulations, a general provision for loan losses shall be established as follows: (i) five percent (5.0%) of the outstanding balance of unclassified restructured loans less the outstanding balance of restructured loans which are considered non-risk under existing laws and regulations; and (ii) one percent (1.0%) of the outstanding balance of unclassified loans other than restructured loans less loans which are considered non-risk under existing laws and regulations.

In accordance with BSP guidelines, the Bank makes the appropriate specific loan loss allowance as follows:

	Loan loss allowance (% of principal amount of loan)
Risk Classification:	
Especially mentioned	5.0%
Sub-standard (secured)	10.0%
Sub-standard (unsecured)	25.0%
Doubtful	50.0%
Loss	100.0%

The specific loan loss provision determined under BSP guidelines may differ from that determined under PAS 39. PAS 39 requires the level of loan loss provisioning to be determined on the basis of future recoverable amounts of the loans and receivables discounted at their original effective interest rates. If the loan or receivable has a variable interest rate, the discount rate for measuring the recoverable amount is the current effective interest rate determined under the contract. If the loan or receivable is collateralized and foreclosure is probable, the Bank should measure the level of loan loss provisioning based on the fair value of the collateral.

The BSP conducts an annual audit on the Bank's individual loans to determine the classifications the Bank must apply to its loans when reporting classified loans to the BSP. The last audit (with a cut-off of December 31, 2012) was completed in May 2013 with the final report expected to be received soon. The following is a summary of the risk classification of the aggregate loan portfolio (as a percentage of total outstanding loans) and allowance for impairment of the Bank as reported to the BSP on a non-consolidated basis as of the dates indicated below:

	As of December 31					
	2010	**%**	**2011**	**%**	**2012**	**%**
	(₱ in millions, except percentages)					
Risk Classification:						
Especially mentioned	3,824.5	5.4%	1,965.8	2.3%	4,372.4	4.8%
Sub-standard - secured	869.2	1.2%	390.0	0.4%	1,081.2	1.2%
- unsecured	183.5	0.3%	2,295.4	2.7%	52.2	0.0%
Doubtful	444.2	0.6%	326.0	0.4%	333.4	0.4%
Loss	5,811.5	8.2%	6,296.8	7.4%	7,371.3	8.1%
Total classified	11,132.9	15.7%	11,274.0	13.2%	13,210.5	14.5%
Unclassified	59,662.4	84.3%	74,031.2	86.8%	77,914.2	85.5%
Total	**70,795.3**	**100.0%**	**85,305.2**	**100.0%**	**91,124.7**	**100.0%**
Allowance for impairment:						
Classified	7,434.4	91.8%	8,193.6	90.8%	9,803.6	92.2%
Unclassified	667.7	8.2%	831.6	9.2%	823.8	7.8%
Total	**8,102.1**	**100.0%**	**9,025.2**	**100.0%**	**10,627.4**	**100.0%**

	As of June 30			
	2012	**%**	**2013**	**%**
	(₱ in millions, except percentages)			
Risk Classification:				
Especially mentioned	1,921.5	2.2%	6,700.8	6.5%
Sub-standard - secured	596.5	0.7%	1,062.6	1.0%
- unsecured	2,218.4	2.5%	127.5	0.1%
Doubtful	333.8	0.4%	321.0	0.3%
Loss	6,385.4	7.2%	7,201.1	6.9%
Total classified	11,455.6	13.0%	15,413.0	14.8%
Unclassified	76,487.2	87.0%	88,728.8	85.2%
Total	**87,942.8**	**100.0%**	**104,141.8**	**100.0%**
Allowance for impairment:				
Classified	8,487.7	91.6%	9,889.3	90.6%
Unclassified	774.2	8.4%	1,026.2	9.4%
Total	**9,261.9**	**100.0%**	**10,915.5**	**100.0%**

Allowance for impairment on classified accounts is based on the total principal balance outstanding. Loans classified as "loss" assets are generally written off by the Bank in accordance with BSP guidelines. The BOD of the Bank has discretion as to the frequency of write-off provided that these are made against provisions for impairment or against current operations. The prior approval of the Monetary Board is required for the write-off of directors, officers, stockholders and related interests ("DOSRI") loans.

In addition to making specific allowances for impairment based on the risk classification of its loan portfolio, the Bank's allowances for impairment also include general allowances of one percent (1.0%) of the gross loan portfolio plus five percent (5.0%) of unclassified restructured loans. Generally, movements in the Bank's allowances for impairment represent provisions charged to operations. Since 2004, however, loan loss provisioning has fluctuated because of the implementation of IAS in 2005.

On a monthly basis, all past-due accounts are updated for movements according to Aging of Past Due Accounts reports, which are summarized for portfolio tracking purposes and used to implement pro-active strategies. Going forward, the Bank may consider sales of a portion of its NPLs to manage its liabilities and performance.

The following table sets out the Bank's reconciliation of its balance of reserves for loan losses on a consolidated basis over the periods indicated:

	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
	(₱ in millions)				
Balance of reserves at beginning of period	7,341.0	8,102.1	9,025.2	9,025.2	10,627.4
Provision during the year	449.5	1,254.7	1,632.9	260.1	369.6
Other Adjustments	311.6	(331.6)	(30.7)	(23.4)	(81.5)
Balance at end of period	**8,102.1**	**9,025.2**	**10,627.4**	**9,261.9**	**10,915.5**

Non-performing Assets

In accordance with BSP guidelines, loans and other assets in litigation are classified as non-performing assets ("NPAs"). The Bank's NPAs principally comprise ROPA and NPLs. The table below sets out details of the Bank's NPLs, non-accruing loans, ROPA, NPAs, restructured loans, and write-offs for loan losses for the specified periods on a consolidated basis:

	As of December 31			As of June 30	
	2010	**2011**	**2012**	**2012**	**2013**
	(₱ in millions, except percentages)				
NPLs - gross	8,704.3	8,973.7	10,200.2	9,524.2	9,694.7
NPLs - net	3,772.9	2,771.1	3,185.8	3,321.5	(243.6)
Classified loans	11,132.9	11,274.0	13,210.5	11,455.6	15,413.0
Total loans (without IBCL)	70,795.3	85,305.2	91,124.7	87,942.8	104,141.8
Total loans (including IBCL)	78,265.8	98,294.3	96,628.2	90,735.2	117,204.5
Total loans - net of reserves (without IBCL)	62,693.2	76,280.0	80,497.3	78,680.9	93,226.3
Total loans - net of reserves (including IBCL)	70,163.7	89,269.1	86,000.8	81,473.3	106,289.0
Total NPLs to total loans (including IBCL)(1)	4.8%	2.8%	3.3%	3.7%	(0.2%)
Total NPLs to total loans (without IBCL)(1)	5.3%	3.2%	3.5%	3.8%	(0.2%)
Classified loans/total loans (including IBCL)	14.2%	11.5%	13.7%	12.6%	13.2%
Classified loans/total loans (without IBCL)	15.7%	13.2%	14.5%	13.0%	14.8%
Non-accruing loans	9,032.6	9,258.9	10,576.2	9,791.0	10,166.6
Non-accruing loans to total loans (without IBCL)	12.8%	10.9%	11.6%	11.1%	9.8%
NPAs	19,420.6	19,374.7	20,239.2	19,089.9	20,249.2
NPAs as a percentage of total assets	7.7%	7.1%	7.2%	7.9%	5.9%
Allowance for impairment (loans) as a percentage of total NPLs	93.1%	100.6%	104.2%	97.2%	112.6%
Allowance for impairment (total) as a percentage of NPAs	41.7%	46.6%	52.5%	48.5%	53.9%
Total restructured loans(2)	1,236.8	1,324.5	1,336.3	1,352.4	1,119.8
Classified as performing	118.8	80.2	195.0	162.8	209.5
Classified as non-performing	1,118.0	1,244.3	1,141.3	1,189.6	910.3
Restructured loans as a percentage of total loans (without IBCL)	1.7%	1.6%	1.5%	1.5%	1.1%
Allowance for impairment (total) as a percentage of NPAs and restructured loans classified as performing	41.5%	46.4%	52.0%	48.1%	53.4%
Allowance for impairment (total) as a percentage of NPAs and restructured loans classified as non-performing	39.5%	43.8%	49.7%	45.7%	51.6%

Notes: (1) On September 2002, the BSP issued Circular No. 351 allowing banks that have no unbooked valuation reserves to exclude from non-performing classification loans classified "loss" in the latest examination of the BSP which are fully covered by allowance for impairment, provided that interest on said loans shall not be accrued. On October 16, 2012, the BSP issued Circular No. 772, amending computation of net NPL ratio effective January 2013 to exclude specific allowance for credit losses on the total loan portfolio from the gross NPLs; provided that such specific allowance for credit losses on the total loan portfolio shall not be deducted from the total loan portfolio 3.3% (including IBCL).

(2) Total Restructured Loans include Restructured Credit Card Receivables.

Loans are classified as non-accruing (or past due) if (i) any repayment of principal at maturity or any scheduled payment of principal or interest due quarterly (or longer) is not made when due and (ii) in the case of any principal or interest due monthly, if the amount due is not paid and has remained outstanding for three (3) months. In the case of (i), such loans are treated as non-performing if the payment is not made within a further 30 days. In the case of (ii), such loans are treated as non-performing upon the occurrence of the default in payment.

Accrued interest arising from loan accounts are classified according to the classification of their corresponding loan accounts except for those which remain uncollected after six (6) months from the date such loans or installments have matured or have become past due for which a hundred percent (100.0%) allowance for uncollected accrued interest receivables is made.

The Bank's NPLs on a non-consolidated basis and a consolidated basis each represented approximately (0.2%) of the Bank's total consolidated gross loan portfolio (net of IBCL) as of June 30, 2013.

Ten Largest NPLs

As of June 30, 2013, the Bank's ten largest NPLs accounted for 1.7% of its total loans to customers and 18.2% of its gross NPLs to customers. As of June 30, 2013, the Bank's exposure to its ten largest NPLs ranged from ₽63.8 million to ₽600.0 million, and amounted to approximately ₽1.8 billion in aggregate.

As of June 30, 2013, only one individual borrower or group accounted for more than 5.0% of the Bank's total amount of gross NPLs.

The following table sets out certain information relating to the Bank's gross top ten (10) NPLs as defined by industry or economic activity as of June 30, 2013:

Industry	Type of Banking Arrangement	Gross Principal Outstanding	Provisions	Principal Outstanding Net of Provisions for Credit Losses	Type of Collateral[2]
		(₽ in millions)			
Manufacturing……….........	L & D[1]	829.3	829.3	-	Clean, MTI, JSS, REM, CHM
Real Estate, Renting and BusinessActivities…………	L & D	552.1	326.9	225.2	REM, CSA
Miscellaneous Business Activities……………….......	L & D	210.1	210.1	-	Clean
Wholesale & Retail Trade...	L & D	171.4	171.4	-	Clean
TOTAL……………………		**1,762.9**	**1,537.8**	**225.2**	

Notes: (1) L & D means loans and discounts.
(2) Type of collateral presented are real estate mortgage (REM), mortgage trust indenture (MTI) chattel mortgage (CHM), Joint and Several Signatures (JSS) and Continuing Surety Agreement (CSA).

Loan Restructuring

The Bank has, from time to time, restructured those NPLs which it considers suitable for restructuring in order to manage its loan portfolio and reduce its exposure to non-performing loans. The decision to restructure a NPL, as well as the method of restructuring, is borrower-specific. The Bank has restructured loans through extensions of maturity or rescheduling interest or principal payments based on expected cash flows of the borrower. The Bank has, in some instances, agreed to debt-for-asset swaps as part of a broader restructuring scheme.

In accordance with BSP guidelines, NPLs which are successfully restructured are considered to be current and no longer treated by the Bank as non-performing, generally following three (3) consecutive payments of required amortization of principal and/or interest, and for restructured loans with capitalized interest and which are not fully secured, six (6) consecutive payments are generally required for the loan to be considered performing. However, these loans may only be removed from classified status following a review by the BSP or the credit review unit of the Bank.

Foreclosure and Disposal of Assets

The Bank's preferred strategy for managing its exposure to NPLs that are secured is to foreclose on a NPL if the borrower cannot or will not repay the loan on acceptable terms. In the case of larger loans, the Bank may also consider accepting a *dacion en pago* arrangement.

The Bank had real estate ROPA of ₱9.9 billion and ₱9.4 billion as of December 31, 2011 and 2012, respectively. This represents a net decrease of 5.2% from December 31, 2011 as a result of its creative and aggressive disposal effort which include cutting up of properties into saleable lots and on line marketing initiatives. In 2012, a total of ₱667.3 million worth of properties were foreclosed by the bank. Real estate ROPA remains at ₱9.8 billion consisting of 1,290 properties as of June 30, 2013.

For details of the Bank's NPLs, non-accruing loans, ROPA, NPAs, restructured loans, and write-offs for loan losses as of and for the periods indicated, please refer to the table on NPAs above.

RISK MANAGEMENT

The Bank is exposed to a range of potential risks arising from its business activities. It enters into financial instruments contracts, which consist of financial assets at fair value through profit or loss, available-for-sale (AFS) financial assets, held-to-maturity investments, loans and receivables, interbank loans receivable, and financial liabilities such as deposits, bills and acceptances payable and notes payable to finance the Bank's operations. The Bank also enters into derivative transactions such as interest rate swaps and forward currency contracts to manage the interest rate and currency risks arising from its operations.

The Bank's goal in risk management is to ensure that it identifies, understands, measures and monitors the various risks that arise from its business activities, such as credit risk, market risk, interest rate risk, operational risk, liquidity risk, strategic/business risk, reputation risk and compliance risk.

The BOD is primarily responsible for approving the risk parameters, credit policies and the overall risk capacity of the Bank. Committees have been established by the BOD to oversee the increasingly varied risk management activities of the Bank with the active participation of senior management. The Executive Committee reviews and approves credit proposals and transactions beyond management's level of credit authority. The Risk Management Committee is responsible for reviewing risk management policies and procedures relating to credit risk, including asset recovery and ROPA sales. These policies require the respective administrative and business units to assist in the identification, assessment and management of credit risk. The Market Risk Committee reviews market risk management policies, including liquidity, interest rate risk, foreign exchange risks and limits relating thereto. The Operations Risk Committee reviews various operations risk policies and practices. The Audit Committee provides direction to and monitors the quality of internal audit activity that is responsible for evaluating the Bank's operations and control functions.

Executive Committee

The Executive Committee (EXCOM), composed of seven (7) members of the BOD, exercises certain functions as delegated by the BOD including, among others, the approval of credit proposals, asset recovery and ROPA sales within its delegated limits.

Risk Management Committee

The Risk Management Committee (RMC), composed of seven (7) members of the BOD, is responsible for the development and oversight of the Bank's risk management program. It assists the BOD in overseeing all matters relating to risk management including providing a comprehensive and bank-wide oversight of all risks and the management of such risks, formulating and reviewing all of the Bank's material risk policies, strategies, and procedures. Among its specific duties are to identify and evaluate exposures, develop risk management strategies, implement risk management plans and review such plans as necessary. The RMC provides oversight, direction, and counsel to the Market Risk Committee and the Operations Risk Management Committee. The RMC is supported by the different risk management units (Credit Risk, Market Risk and Operations Risk).

Market Risk Committee

The Market Risk Committee (MRC) composed of five members (5) of the BOD, sets policies and standards for the management of the market risk, liquidity risk and interest rate risk in the banking book. The MRC also monitors the sensitivity of the Bank's financial condition to the effects of market volatility and adverse price changes on the Bank's portfolio of financial instrument and oversees the Bank's liquidity position.

Asset and Liability Committee

The Asset and Liability Committeee (ALCO) is responsible for ensuring that the Bank's liquidity management process is adequate and that the Bank maintains adequate liquidity and sufficient capital. The ALCO manages the Bank's balance sheet and ensures that business strategies are consistent with the Bank's liquidity, capital and funding strategies as well as sets targets for balance sheet size. It also establishes asset/liability pricing policies appropriate to the Bank's balance sheet objectives, and determines the level of stress condition the Bank is experiencing.

The ALCO is composed of the President, the Treasurer, Center Heads and Group Heads. The ALCO is chaired by the President.

Operations Risk Management Committee

The Operations Risk Management Committee (ORMC) comprises three (3) members of the BOD and two members from senior management. It is responsible for reviewing various operations risk policies and practices, including among others, those policies and practices of the Bank's branches, internet banking, CPS and treasury operations.

Audit Committee

The Audit Committee is a committee of the BOD that is composed of five (5) members, most with accounting, auditing, or related financial management expertise or experience. The Audit Committee believes that the skills, qualifications, and experience of its members are appropriate for them to perform their duties as laid down by the Board. Two (2) of these five (5) members are independent directors, including the Chairman.

The Audit Committee serves as principal agent of the BOD in ensuring independence of the Bank's external auditors and the internal audit function, the integrity of management, and the adequacy of disclosures and reporting to stockholders. It also oversees the Bank's financial reporting process on behalf of the BOD. It assists the BOD in fulfilling its fiduciary responsibilities as to accounting policies, reporting practices and the sufficiency of auditing relative thereto, and regulatory compliance.

Corporate Governance Committee

The BOD is primarily assisted by the Corporate Governance Committee in fulfilling its corporate governance responsibilities. The Committee recommends governance policies to the BOD based on the regulations of the BSP, the Philippine SEC, the PSE, as well as those which are internationally recognized as industry best practices. It serves as the primary resource for the BOD to study and evaluate itself, as a body, and its Committees' structure, policies and practices with the objective of raising the bar for the Bank's corporate governance.

The Committee has seven (7) members of the BOD, three (3) of whom are Independent Directors, including the chairman, and one (1) belonging to the Bank's senior management. The Committee annually evaluates the governance state of the Bank by using as benchmark the Corporate Governance Scorecard of the Institute of Corporate Directors for publicly listed companies and banks, the PSE's Corporate Governance Guidelines Disclosure and other relevant governance metrics.

The specific duties of the Committee include, among others, making recommendations to the BOD regarding continuing education of directors and overseeing its periodic performance evaluation, its Committees and senior management. It has two (2) sub-committees, namely, the Nominations Committee and the Compensation and Remuneration (CompRem) Committee.

The Nominations Committee is comprised of seven (7) voting members of the BOD, one (1) of whom is an independent Director, and one (1) non-voting member in the person of the Human Resources Director. The Nominations Committee is responsible for reviewing the qualifications of and screening candidates for the BOD, and key officers of the Bank. It oversees the implementation of programs for identifying, retaining and developing critical officers and the succession plan for various units in the organization.

The CompRem Committee is composed of five (5) members of the BOD, one (1) of whom is an Independent Director. It is responsible for overseeing implementation of the programs for salaries and benefits of Directors and senior management. It monitors adequacy, effectiveness and consistency of compensation program vis-à-vis corporate philosophy and strategy.

Credit Risk

Credit risk is the risk of loss resulting from the failure of a borrower or counterparty to honor its financial or contractual obligation to the Parent Company. The risk may arise from lending, trade finance, treasury, investments, derivatives and other activities undertaken by the Parent Company. Credit risk is managed through strategies, policies and limits that are approved by the BOD. Further, the Parent Company has a well-structured and standardized credit approval process and credit scoring system for each of its business and/or product segments.

The Risk Management Unit (RMU) undertakes several functions with respect to credit risk management. The RMU independently performs credit analysis and review for both retail and corporate/commercial financial products to ensure consistency in the Parent Company's risk assessment process. It also ensures that the Parent Company's credit policies and procedures are adequate and are constantly updated to meet the changing demands of the business. The RMU is also responsible for developing procedures to streamline and expedite the processing of credit applications.

The RMU reviews the Parent Company's loan portfolio quality in line with the Parent Company's policy of avoiding significant concentrations of exposure to specific industries or groups of borrowers. Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features. Concentrations indicate the relative sensitivity of the Parent Company's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Parent Company's policies and procedures include guidelines for maintaining a diversified portfolio (e.g. concentration limits). Identified concentrations of credit risks are controlled and managed accordingly. RMU also monitors compliance to the BSP's limit on exposure to any single person or group of connected persons to an amount not exceeding twenty five percent (25.0%) of the Parent Company's adjusted capital accounts.

Credit Risk Assessment for Corporate Lending

Corporate lending activities are undertaken by the Bank's Corporate Banking Center. The customer accounts under this group belong to the top tier corporations, conglomerates and large multinational companies. The Bank undertakes a comprehensive procedure for the credit evaluation and risk assessment of large corporate borrowers based on its Internal Credit Risk Rating System. The rating system assesses risks on a three-dimensional level: Borrower Risk, Facility Risk and Security Risk. It also has established concentration limits depending on the Borrower Risk Rating and overall credit quality.

Borrower risk is evaluated by considering (i) quantitative factors, such as profitability, liquidity, capital adequacy and sales growth; (ii) qualitative factors, such as management skills and management integrity; and (iii) industry risk. Industry risk is assessed by considering certain industry characteristics, such as its importance to the economy, growth outlook, cyclicality, industry structure and relevant government policies.

Based on foregoing factors, each borrower is assigned a Borrower Risk Rating (BRR), a 10-scale scoring system that ranges from AAA to D, with AAA to A as High Grade, BBB to B as Standard Grade and CCC and lower as Sub-standard grade. Borrowers with high grade BRRs are considered to have very strong credits where the Parent Company may be comfortable giving clean short-term facilities. Borrowers with standard BRRs are similarly acceptable credits but may require collateral to mitigate the credit risk. On the other hand, borrowers with sub-standard BRRs are deemed high risk requiring very strong collateral to be an acceptable credit risk.

In addition to the BRR, the Bank assigns a loan exposure rating (LER), a 100-point system which is comprised of a Facility Tenor Rating (FTR) and a Security Risk Rating (SRR). The FTR measures the maturity risk based on the length of loan exposure, while the SRR measures the quality of the collateral and risk of its potential deterioration over the term of the loan. The FTR and the SRR, each a 100-point scoring system, are given equal weight in determining the LER.

Once the BRR and the LER have been determined, the credit limit to a borrower is determined under the Risk Asset Acceptance Criteria (RAAC) which is a range of acceptable combinations of the BRR and the LER. For example, under the RAAC, a borrower with a high BRR will have a broader range of acceptable LERs.

The credit rating for each borrower is reviewed annually or earlier if the borrower has a higher risk profile or when there are extraordinary or adverse developments affecting the borrower, the industry and/or the Philippine economy. Any major change in the credit scoring system, the RAAC range and/or the risk-adjusted pricing system is presented to and approved by the RMC.

Credit Risk Assessment for Commercial Lending

The Parent Company's commercial banking activities are undertaken by its Commercial Banking Center. These consist of banking products and services rendered to customers which are entities that are predominantly SMEs. These products and services are similar to those provided to large corporate customers, as well as trade finance-related products and services.

ComBank uses a separate 10-point credit scoring system for commercial accounts, comprised of: an Obligor Risk Rating (ORR), a Facility Risk Adjustment (FRA) and a Final Risk Rating (FRR). An Estimated Cash Risk Position is indicated to determine the secured and unsecured portion of the obligation relative to collateral.

The ORR is an assessment of the creditworthiness of the borrower (or guarantor) without considering the type or amount of the facility, or its security arrangements. It is an indicator of the probability that a borrower cannot meet its credit obligations in the foreseen manner. In determining the ORR, the focus lies on the outlook of the borrower. Although the borrower's financial condition is evaluated on the basis of the historical financial statements, this is primarily to determine any trend in the company's financial position going forward, and how it will impact the company's future solvency or debt-service capabilities.

Based on above factors, each borrower is assigned an ORR that ranges from 1 to 10, with 1 to 3 as High Grade, 4 to 6 as Standard Grade and 7 and lower as Substandard Grade. Borrowers with high grade ORRs are usually granted clean short-term loan facilities. Borrowers with standard ORRs may be required by the Bank to give collateral to enhance their credit rating. On the other hand, borrowers with substandard ORRs are deemed to be high risk, thus, may be required by the Bank to pledge high grade collateral.

Basically independent from influence by any transactional factors, the ORR is combined with the FRA to allow a more precise depiction of risk. The FRA takes into account the conduct or handling of the borrower's loan and depository accounts. The combination of the ORR and the FRA results in a borrower risk rating which may be combined with other relevant factors to determine the FRR.

Credit Risk Assessment for Consumer Lending

The consumer loan portfolio of the Bank is composed of three main product groups, namely: credit cards, auto and residential mortgage loans. Each of these product groups has their own risk guidelines and risk assessment system. Although each loan application is examined through an individual credit evaluation process (combined manual and automated process), the consumer loans are managed on a portfolio basis with respect to defaults as well as accept, reject and review standards.

For the Bank's credit card business, the main risk assessment tool is the applications scoring model which has been revised and fine-tuned through the years using the Bank's own credit experience in the credit card business. The current applications scoring model uses nine variables which have been identified as likely predictors of credit behavior of credit card applicants.

The Bank has categorized the scorecard into three levels: Outright Accept, Review Band and Outright Reject. The Outright Accept category refers to applicants that are within the risk profile acceptable to the Bank and their applications are automatically approved, provided that all information in the application are verified to be accurate based on a validation system presently in place. The Outright Reject category refers to applicants that are below the minimum risk profile acceptable to the Parent Company and their applications are automatically rejected. Applications that fall within the Review Band are borderline cases which are accepted or rejected based on the predetermined review parameters. The Parent Company utilizes statistical modeling in updating its application score cards.

Credit Approval Process

Before any extension of credit, the Bank identifies the needs of the prospective borrower, analyzes the appropriateness of the exposure and evaluates inherent risks. The lending officers are responsible for soliciting target customers, identifying borrowing requirements and initiating credit lines. The Risk Management units independently perform credit risk assessment and evaluation (See "— Credit Risk Assessment for Consumer Lending" and "—Credit Risk Assessment for Corporate Lending".) and prepares the credit application for approval by the relevant approving authority.

The Risk Management Review Committee (RMRC) is responsible for reviewing credit facilities approved within management's credit authority limit and screening credit proposals which exceed management-delegated authorities before endorsement to the Executive Committee and the BOD. The RMRC is a senior level group comprised of a chairman (the Chief Risk Officer) and four (4) members who are senior credit officers of the Bank. The Risk Management Review Committee is also responsible for the following:

1. reviewing credit policy recommendations, credit issues and other credit matters before endorsement to the Executive Committee and the BOD;

2. approving credit procedural guidelines underlying new credit policies and enhancements in the existing procedures; and

3. reviewing collection reports, loan portfolio reports, past due loans, items in litigation, ROPA and NPLs prior to presentation at the monthly Risk Management Committee meetings.

The EXCOM may modify portions of the credit proposal package as it sees fit based on the Bank's current risk tolerance policy. All credit proposals approved by the Executive Committee are confirmed by the BOD. Credit proposals exceeding the EXCOM's credit authority limit and those which carry an unusual or material risk require approval of the BOD. The BOD has the ultimate authority to approve credit transactions and is also the only body with authority to approve DOSRI loans.

Credit Approval Authority

The BOD, being the ultimate approving authority of the Bank, has delegated specific approval limits to certain committees and senior credit officers. These approval limits reflect the BOD' level of risk tolerance based on the type of borrower, type of credit facility, size of maximum credit exposure, collateral, tenor and qualification of the credit officer.

For credit cards, all applications are approved by the Bank's automated credit scoring system. In certain exceptional cases, a senior credit officer is allowed to approve a credit extension based on the relevant approval limit set by the BOD, subject to a joint approval of another senior credit officer in the Risk Management Group.

Credit Monitoring and Review Process

Pursuant to the BSP's regulations, the Bank is required to establish a system of identifying and monitoring existing or potential problem loans and other risk assets and of evaluating credit policies vis-à-vis prevailing circumstances and emerging portfolio trends. In compliance with this requirement, the Risk Management units, on a regular basis or as circumstances require, establish and maintain a system for monitoring the financial condition of individual accounts or a portfolio of accounts and updates senior management accordingly.

Specifically for corporate and commercial lending, the Risk Management units monitor individual accounts to:

- ensure that the Bank is aware of and understands the current financial condition or credit quality of the borrower or the counterparty;
- ensure that all accounts are in compliance with existing covenants;
- identify and monitor the purposes of which customers make use of approved credit lines;
- ensure that projected cash flows on major credits meet debt servicing requirements;
- ensure that, where applicable, collateral provides adequate coverage relative to the borrower's current financial condition; and
- identify and classify potential problem credits or accounts on a timely basis.

All individual accounts of corporate and commercial lending are reviewed at least once a year together with the credit line renewal. Larger exposures and lower rated-borrowers or counterparties are reviewed more frequently, as necessary.

The Credit Review unit is responsible for reviewing the Bank's credit process and loan portfolio quality. It reports credit policy exceptions to the senior management of the Bank, evaluates compliance of lending units to existing credit management policies and procedures and, together with the relevant business units, recommends the loan classifications in accordance with the standard classifications prescribed by the BSP.

Credit Risk Management units and Credit Review are also responsible for monitoring compliance with DOSRI rules and guidelines. The Bank and its subsidiaries, from time to time and in the ordinary course of business, enter into loan transactions with DOSRI. All such loans are on a commercial and arm's-length basis. The General Banking Law (Republic Act No. 8791) ("General Banking Law") and BSP regulations require that (a) the amount of individual outstanding loans, other credit accommodations and guarantees to DOSRI should not exceed an amount equivalent to their unencumbered deposits and the book value of their paid-in capital investment in the bank, (b) unsecured loans, other credit accommodations and guarantees to each of the Bank's DOSRI may not exceed thirty percent (30.0%) of their respective total loans, other credit accommodations and guarantees, (c) the aggregate outstanding borrowings of DOSRI may not, without the prior approval of the Monetary Board, exceed fifteen percent (15.0%) of the Bank's total loan portfolio or a hundred percent (100.0%) of the Bank's net worth, whichever is lower and (d) that the total unsecured DOSRI borrowings do not exceed thirty percent (30.0%) of the aggregate ceiling or the outstanding loans, whichever is lower. On January 31, 2007, the BSP issued Circular No. 560, imposing lower ceilings on loans, other credit accommodations and guarantees granted to subsidiaries and affiliates of banks and quasi-banks. (See "Banking Regulation and Supervision – Loans to DOSRI".)

As of June 30, 2013, DOSRI loans amounted to ₱854.9 million, or approximately 0.8% of the Bank's total loans. There were no outstanding loans to the Aboitiz Group. Of the total DOSRI loans, ₱783.3 million were loans granted to Directors and Officers under the Fringe Benefit program.

Market Risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rate, foreign exchange rates and equity prices. The Bank classifies exposures to market risk into either trading book or banking book. The market risk for the trading portfolio is managed and monitored based on a Value-at-Risk (VaR) methodology. Meanwhile, the market risk for the non-trading positions are managed and monitored using other sensitivity analyses.

The Bank applies a VaR methodology to assess the market risk of positions held and to estimate the potential economic loss based upon a number of parameters and assumptions for various changes in market conditions. VaR is a method used in measuring financial risk by estimating the potential negative change in the market value of a portfolio at a given confidence level and over a specified time horizon.

The Bank uses the parametric VaR approach in assessing the possible changes in the market value of held-for-trading and AFS securities based on historical data for a rolling one year period. The VaR models are designed to measure market risk in a normal market environment. The models assume that any changes occurring in the risk factors affecting the normal market environment will follow a normal distribution. The use of VaR has limitations because it is based on historical correlations and volatilities in market prices and assumes that future price movements will follow a statistical distribution. Due to the fact that VaR relies heavily on historical data to provide information and may not clearly predict the future changes and modifications of the risk factors, the probability of large market moves may be underestimated if changes in risk factors fail to align with the normal distribution assumption.

VaR may also be underestimated or overestimated due to the assumptions placed on risk factors and the relationship between such factors for specific instruments. Even though positions may change throughout the day, the VaR only represents the risk of the portfolios at the close of each business day, and it does not account for any losses that may occur beyond the 99% confidence level.

The VaR figures are backtested daily against actual and hypothetical profit and loss of the trading book to validate the robustness of the VaR model. To supplement the VaR, the Bank performs stress tests wherein the trading portfolios are valued under extreme market scenarios not covered by the confidence interval of the Bank's VaR model.

Market Risk Management Process

Treasury, in coordination with the Market Risk Management Unit, develops a risk measurement and management process that is appropriate for the Bank's business and such process is approved by the MRC and the BOD. A product program manual which sets out, among other things, a standardized process of measuring and managing credit, market and liquidity risks, operational procedures and controls and approval procedures, is then prepared for each product.

Market Risk Limits

The Bank also manages its market risks through application of various limits set by the MRC and approved by the BOD. Such limits primarily include the following:

- Aggregate Control Limits (ACL) — The ACL places a ceiling on the total volume of trading/ownership of given product lines at given tenors.
- Aggregate VaR Limit — Aggregate VaR Limits places a ceiling on the monetary amount of potential loss on the Held-for-Trading and AFS Portfolios of the Bank deemed tolerable by management.
- Nominal Position Limits — Nominal Position Limits determine the maximum size of open risk positions that may be held by the Bank within a given time period. Such limits include overnight and daylight position limits which may vary for overbought and oversold positions. These limits must conform to the regulatory limits set by the BSP.
- Management Action Trigger (MAT)/Loss Alert/Stop Loss Limits — These limits establish management's tolerance levels for accepting cumulative year-to-date and month-to-date market risk losses on trading positions.
- Trader/Dealer Limits — These limits set the maximum volume of transactions that a trader/dealer may execute and is determined relative to the depth of experience and level of expertise of the personnel making the risk-bearing decision.

Compliance with the above limits is closely monitored and reported in accordance with an escalation process established by the MRC.

The Internal Audit Division is responsible for conducting back-testing to compare hypothetical and actual trading results with the Bank's internal model-generated risk measures at the end of each quarter. Based on the results of the back-testing, if a certain market risk is not addressed by the Bank's internal model, the internal model is modified to capture such risk. The Market Risk Management Unit is also responsible for conducting quarterly stress tests on the Bank's portfolio of financial instruments and reporting the results of such tests to the MRC for a more concrete assessment of the risks. The stress tests evaluate the Bank's potential losses resulting from changes in market factors, such as foreign exchange rates and interest rates, caused by simulated hypothetical scenarios or historical events where extreme movements have been observed.

Interest Rate Risk

A critical element of the Bank's risk management program consists of measuring and monitoring the risks associated with fluctuations in market interest rates on the Bank's net interest income and ensuring that the exposure in interest rates is kept within acceptable limits.

The Bank employs "gap analysis" to measure the interest rate sensitivity of its resources and liabilities. The gap analysis measures, for any given period, any mismatch between the amounts of interest-earning resources and interest-bearing liabilities which would mature or reprice during the period. A positive gap occurs when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities while a negative gap occurs when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. Accordingly, during a period of rising interest rates, a company with a positive gap will have more interest rate sensitive assets repricing at a higher interest rate than interest rate sensitive liabilities which will be favorable to it. During a period of falling interest rates, a company with a positive gap will have more interest rate sensitive assets repricing at a lower interest rate than interest rate sensitive liabilities, which will be unfavorable to it.

The following table sets out the interest rate sensitive asset/liability gap position for the Bank's operations as of December 31, 2012 and June 30, 2013:

	As of December 31, 2012			
	Up to Six Months	**Beyond Six Months to One Year**	**Beyond One Year**	**Total Outstanding Balance**
	(₱ in millions)			
Resources				
Placements	5,503.5	-	30,449.6	35,953.1
Loans	92,524.9	8,607.5	18,584.2	119,716.6
Investments	1,272.9	777.8	86,905.1	88,955.8
	99,301.3	9,385.3	135,938.9	244,625.5
Liabilities				
Deposit Liabilities	101,848.4	1,131.3	86,861.6	189,841.3
Bills Payable	18,380.3	6.6	154.3	18,541.2
Notes Payable	-	-	3,750.0	3,750.0
	120,228.7	1,137.9	90,765.9	212,132.5
Asset-Liability Gap	(20,927.4)	8,247.4	45,173.0	32,493.0

	As of June 30, 2013			
	Up to Six Months	**Beyond Six Months to One Year**	**Beyond One Year**	**Total Outstanding Balance**
	(₱ in millions)			
Resources				
Placements	68,443.7	-	39,465.7	107,909.4
Loans	48,822.1	8,574.8	42,354.3	99,751.2
Investments	1,044.9	63.2	91,711.5	92,819.6
	118,310.7	8,638.0	173,531.5	300,480.2
Liabilities				
Deposit Liabilities	130,497.0	9,829.5	119,219.6	259,546.1
Bills Payable	10,861.2	19.0	4,327.8	15,208.0
Notes Payable	-	-	3,750.0	3,750.0
	141,358.2	9,848.5	127,297.4	278,504.1
Asset-Liability Gap	(23,047.5)	(1,210.5)	46,234.1	21,976.1

As of December 31, 2012 and June 30, 2013, the Bank's short-term interest rate sensitive assets, which either have maturities of less than one year or are repriceable monthly, quarterly, semi-annually or annually amounted to ₱108.7 billion and ₱126.9 billion, respectively. These short-term interest rate sensitive assets approximately represent 44.4% and 42.2% of the Bank's total interest rate sensitive assets as of December 31, 2012 and June 30, 2013, respectively.

The Bank also maintains a large portion of its deposit base in short-term deposits, which are normally rolled over. As of December 31, 2012 and June 30, 2013, short-term deposits totaling to ₱103.0 billion and ₱140.3 billion, respectively, have maturities of less than one year. As a matter of policy, the Bank sets the interest rates payable on its deposits at conservative levels.

The following table sets out, for the year ended December 31, 2012 and June 30, 2013, the impact of changes in interest rates on the Bank's net interest income:

	As of December 31, 2012		**As of June 30, 2013**	
Change in interest rates (in basis points)	**100**	**(100)**	**100**	**(100)**
Change in annualized net interest income (₱ in millions)…………………………………	(212.9)	212.9	(135.7)	135.7
As a percentage of 2012 net interest income (%)……………………........................	(2.9%)	2.9%	(1.9%)	1.9%

This sensitivity analysis is performed for risk management purposes and assumes no other changes in the repricing structure. Actual changes in the Bank's net interest income may vary from the model.

Foreign Exchange Risk

Foreign exchange risk is the risk to earnings or capital arising from changes in foreign exchange rates.

The Bank's net foreign exchange exposure, taking into account any spot or forward exchange contracts, is computed as foreign currency assets less foreign currency liabilities. The foreign exchange exposure is limited to the day-to-day, over-the-counter buying and selling of foreign exchange in the Bank's branches, as well as foreign exchange trading with corporate accounts and other financial institutions. The Bank is permitted to engage in proprietary trading to take advantage of foreign exchange fluctuations.

The Bank's foreign exchange exposure during the day is guided by the limits set out in the Bank's Market Risk Policy Manual. These limits are within the prescribed ceilings mandated by the BSP. At the end of each day, the Bank reports to the BSP on its compliance with the mandated foreign currency exposure limits. In addition, it also reports to the BSP on the respective foreign currency positions of its subsidiaries.

As of December 31, 2012 and June 30, 2013, the Bank's net foreign exchange exposure was US$14.5 million (short) and US$45.7 million (short), respectively.

Liquidity Risk

Liquidity risk is the risk that there are insufficient funds available to adequately meet the credit demands of the Bank's customers and repay deposits on maturity. The ALCO and the Treasurer of the Bank ensure that sufficient liquid assets are available to meet short-term funding and regulatory requirements. Liquidity is monitored by the Bank on a daily basis and under stressed situations. A contingency plan is formulated to set out the amount and the sources of funds (such as unused credit facilities) that are available to the Bank and the circumstances under which the Bank may use such funds.

The Bank also manages its liquidity risks through the use of a Maximum Cumulative Outflow (MCO) limit which regulates the outflow of cash on a cumulative basis and on a tenor basis. To maintain sufficient liquidity in foreign currencies, the Bank has also set an MCO limit for certain designated foreign currencies. The MCO limits are endorsed by the MRC and approved by the BOD.

As of December 31, 2012 and June 30, 2013, the total amount of funds that were available to the Bank under credit facilities for secured and unsecured borrowings, swaps and settlement were ₱194.5 billion and ₱204.0 billion, respectively.

The Bank takes a multi-tiered approach to maintaining liquid assets. BSP regulations require the Bank to maintain minimum cash reserves and liquid assets as a proportion of its overall deposits. See "Banking Regulation and Supervision". The Bank's principal source of liquidity is comprised of ₱4.2 billion of cash, deposits with other banks of ₱3.0 billion, due from the BSP of ₱27.5 billion and short-term interbank loans receivable with maturities of less than one year amounting to ₱5.5 billion as of December 31, 2012. In addition to regulatory reserves, the Bank maintains what it believes to be a sufficient level of secondary reserves in the form of liquid assets such as investment securities that can be realized quickly. Total portfolio of investment securities of the Bank amounted to ₱89.0 billion as of December 31, 2012.

Operational Risk

To standardize the practice and to conform to international standards, the Parent Company has adopted the Basel Committee's definition of operational risk. This is formalized in the Parent Company's approved Operational Risk Management Framework. Operational risk is the risk of loss arising from inadequate or failed internal processes, people, and systems or external events. This definition includes legal risk, but excludes strategic and reputational risk. This also covers potential losses that could occur as a result of the Parent Company's exposure in the use of technology-related products, services, delivery channels, and processes.

Each specific unit of the Parent Company has its roles and responsibilities in the management of operational risk and these are clearly stated in the operational risk management framework. At the BOD level, an ORMC was formed to provide overall direction in the management of operational risk.

Operational Controls and Procedures in Branches

The Bank has operating manuals detailing the procedures for the processing of various banking transactions and the operation of the application software. Amendments to these manuals are implemented through circulars sent to all offices.

When taking a deposit from a new customer, the Bank requires the new customer to complete a relationship form, which details the terms and conditions for providing various banking services. Photographs of customers are also obtained for its records, and specimen signatures are scanned and stored in the system for online verification. The Bank enters into a relationship with a customer only after it verifies the customer's identity. When time deposits become due for repayment, the deposit is paid to the depositor thru his elected savings deposit settlement account. Time deposits are all classified as "auto-renew" on due date unless there is a specific instruction from the client.

The Bank has a scheme of delegation of financial powers that sets out the monetary limit for each employee concerned with respect to the processing of transactions in a customer's account. Withdrawals from customer accounts are controlled by dual authorization. Senior officers have delegated power to authorize larger withdrawals. The Bank's operating system validates the check number and balance before permitting withdrawals. Cash transactions over a certain limit are subject to special scrutiny to avoid laundering. The Bank's banking software has multiple security features to protect the integrity of applications and data.

The Bank gives importance to computer security and has a comprehensive information technology security policy. Most of the information technology assets including critical servers are hosted in centralized data centers, which are subject to appropriate physical and logical access controls.

Operational Controls and Procedures for Internet Banking

The Bank has established a multi-factor security system to improve internet banking security. The Bank issues each customer that opens an internet banking account a user identity and password to access his account online. For security purposes, the customer will be required to change the default password on his first successful log in attempt. To further strengthen the security, the customer shall also be required to enroll a transaction password for his internet banking account. This transaction password will be required for every internet banking transaction made by the customer, to ensure the transaction's authenticity. Encryption, authentication, and validation are also in place for internet-based transactions. Network controls are implemented for secured internet banking.

Operational Controls and Procedures in CPS locations

To improve operational controls, enhance customer service at the Bank's physical locations, reduce operating costs, and capitalize on economies of scale, the Bank handles processing of common transactions at central locations by taking away such operations from each business center.

With two (2) operating locations, one in Metro Manila and the other in Cebu City, CPS, the Bank's main backroom operations hub, uses high level of automation in its operations. Except for some critical processes that are jointly handled by both Manila and Cebu as a business continuity strategy, each CPS location, in general, houses its own centralized processes, thus setting it apart from the other location. The CPS location in Cebu City handles branch accounting, subsidiaries accounting, account reconciliation, expense accounting and regulatory reporting while the CPS location in Metro Manila handles centralized production of cards, operation processes of check clearance as well as back office activities for auto and residential mortgage loans and other administrative support services.

In 2008, CPS was certified by TUV Rheinland with ISO 9001:2000 for QMS for the entire bank-end operations, a first in the banking industry. Two years after, it received ISO 9001:2008 certification, an upgrade from the previous. It has consistently been certified as having zero-nonconformance every year from date of certification during quality audits.

Operational Controls and Procedures in Treasury

The Bank has a high level of automation in trading operations. The Bank uses technology to monitor risk limits and exposures. The Bank's front office, middle and back office and accounting and reconciliation functions are fully segregated. The respective middle offices use various risk monitoring tools such as counter-party limits, nominal position limits, aggregate control limits, aggregate VaR limit, earnings-at-risk limits, MCO limits, stop loss, loss alert and individual dealer limits (per trader, position limits, stop loss and loss alert, among others). Procedures for reporting breaches in limits and escalation to management are also in place.

The Bank's front office treasury operations cover transactions in fixed income securities, inter-bank money markets, and foreign exchange. The Bank’s traders analyze the market conditions and take views on price movements. Thereafter, they enter into transactions in conformity with various limits relating to counterparties, securities and brokers. The agreements are confirmed by the middle office and then forwarded to the back office for settlement. The Bank also monitors delayed transactions.

The Treasury Middle Office Unit confirms trades and monitors counter-party credit risk limits and the Market Risk Management Unit evaluates the mark-to-market impact on various positions taken by dealers and monitors market risk exposure of the investment portfolio and adherence to various market risk limits set up by the MRC.

The Bank’s back office undertakes the settlement of funds and securities. The back office has procedures and controls for minimizing operational risks, including procedures with respect to deal confirmations with counterparties, verifying the authenticity of counter-party checks and securities, ensuring receipt of contract notes from brokers, monitoring receipt of interest and principal amounts on due dates, ensuring transfer of title in the case of purchases of securities, reconciling actual security holdings with the holdings pursuant to the records and reports any irregularity or shortcoming observed.

Audit

The Internal Audit Division (IAD) is an independent unit responsible for providing assurance and consulting activity designed to add value and improve the Bank’s operations. It helps the bank accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

The IAD is responsible for undertaking a comprehensive audit of all business groups and other functions, in accordance with a risk-based audit plan and provides an independent appraisal of the adequacy and effectiveness of the risk management and control processes in operation throughout the Bank. Various components of information technology from applications to databases, networks and operating systems are covered under the annual audit plan. The audit plan for every fiscal year is approved by the Audit Committee.

The Head of the IAD reports directly to the Audit Committee and the BOD. These reporting lines and organizational structures ensure that the IAD has the full support and access required to efficiently and systematically conduct its work independently. The IAD issues various reports to the Audit Committee, the Chairman of the Board, management and other relevant parties throughout the year, including audit reports, compulsory audit reports of branch visits and periodic reports issued to the Audit Committee, the BOD and management.

Anti-money laundering controls

Under the Anti-Money Laundering Act, the Bank is required to submit a "covered" transaction report involving a single transaction in cash or other equivalent monetary instruments in excess of ₱500,000.00 within one (1) Banking Day. The Bank is also required to submit a "suspicious" transaction report to the Anti-Money Laundering Council ("AMLC") of the BSP if there is reasonable ground to believe that any amounts processed are the proceeds of money-laundering activities. The Bank is required to establish and record the identities of their clients based on official documents. In addition, all records of transactions are required to be maintained and stored for five (5) years from the date of a transaction. Records of closed accounts must also be kept for five (5) years after their closure.

In an effort to further prevent any money laundering activities through the Bank, it has adopted more stringent KYC policies and guidelines. Under the KYC guidelines, each business unit is required to validate the true identity of a customer based on official or other reliable identifying documents or records before an account is opened. Each business unit is also required to monitor account activities to determine whether transactions conform to the normal or expected transactions for a customer or an account. Persons with higher potential or risk for money laundering require enhanced due diligence. Decisions to enter into a business relationship with a higher risk customer, such as a politically exposed person or a private individual holding a prominent position, are made exclusively at the senior management level.

Legal Risk

The uncertainty of the enforceability of the obligations of the Bank's customers and counterparties, including foreclosure on collateral, creates legal risk. Changes in law and regulation could adversely affect the Bank. Legal risk is higher in new areas of business where the law is often untested by the courts. The Bank seeks to minimize its legal risk by using stringent legal documentation, employing procedures designed to ensure that transactions are properly authorized and consulting internal and external legal advisors.

RELATED PARTY TRANSACTIONS

The Bank transacts and intends to continue to transact with its subsidiaries, certain of its DOSRI and its majority shareholder, Aboitiz Equity Ventures, Inc., in the ordinary course of business. As of the date of this Preliminary Offering Circular, Aboitiz Equity Ventures, Inc. held 47.1% of the issued and outstanding share capital of the Parent Company. In accordance with the Bank's existing policies, these transactions are made substantially on the same terms and conditions as transactions of comparable risks with other unrelated individuals and businesses.

Major related party transactions entered into by the Bank for the year ended December 31, 2012 are set out below:

- The Bank entered into a sales management agreement with FUDC an indirect wholly-owned subsidiary of the Bank, to sell and market the Bank's credit cards through FUDC's direct selling networks.

The Bank's other related party transactions include banking transactions with its subsidiaries and advances made to dormant subsidiaries for the payment of various operating expenses, all of which are conducted in the ordinary course of business.

For further information on the Bank's related party transactions, including detailed breakdowns of amounts receivable from related parties and the income and expenses relating to related party transactions, see Note 30 of the Bank's financial statements as of and for the years ended December 31, 2011 and 2012, respectively.

DOSRI Loans and Deposits

In the ordinary course of business, the Bank has loans, deposits and other transactions with its related parties and with DOSRI. Under the Bank's existing policies, these transactions are made substantially on the same terms and conditions as transactions with other individuals and businesses of comparable risks. The amount of individual loans to DOSRI, of which seventy percent (70.0%) must be secured, should not exceed the amount of the deposit and book value of their investment in the Bank. In the aggregate, loans to DOSRI generally should not exceed the total equity or fifteen percent (15.0%) of the total loan portfolio of the Bank, whichever is lower. As of December 31, 2010, 2011, and 2012, the Bank is in compliance with these regulatory requirements.

On January 31, 2007, BSP issued Circular No. 560 which provides the rules and regulations that govern loans, other credit accommodations and guarantees granted to subsidiaries and affiliates of banks and quasi-banks. Under the said circular, the total outstanding exposures to each of the bank's subsidiaries and affiliates shall not exceed ten percent (10.0%) of bank's net worth, the unsecured portion of which shall not exceed five percent (5.0%) of such net worth. Further, the total outstanding exposures to subsidiaries and affiliates shall not exceed twenty percent (20.0%) of the net worth of the lending bank. On June 16, 2011, the BSP issued Circrular No. 725, which included "Non-governmental organization (NGOs)/Foundations that are engaged in retail microfinance operations which are incorporated by any of the stockholders and/or directors and/or officers of related banks," under 'Related Interests'.

The following table sets out certain information relating to the Bank's DOSRI loans as of the periods indicated:

	As of December 31			As of June 30	
	2010	2011	2012	2012	2013
	(₱ in millions)				
Total outstanding DOSRI loans:	670.3	652.1	878.4	960.0	854.9
Stockholders	54.9	-	5.0	14.6	5.0
Directors and officers	513.4	640.0	823.1	892.6	783.3
Other related interests	102.0	12.1	50.3	52.7	66.6
Percentage of DOSRI loans to total loans	0.7%	0.6%	0.7%	1.1%	0.8%
Percentage of unsecured DOSRI loans to total DOSRI loans	11.7%	14.5%	13.6%	11.1%	18.7%
Percentage of past due DOSRI loans to total DOSRI loans	0.0%	0.0%	0.0%	0.0%	0.0%
Percentage of non-accruing DOSRI loans to total DOSRI loans	0.0%	0.0%	0.0%	0.0%	0.0%

The Bank’s transactions with its subsidiaries are as follows:

- Sales management agreement with FUDC to sell the Bank’s credit card through FUDC’s direct selling network; and
- Other transactions with subsidiaries consisting of regular banking transactions and advances for payment of various operating expenses of dormant subsidiaries.

The Bank's other related party transactions include banking transactions with its subsidiaries and advances made to dormant subsidiaries for the payment of various operating expenses, all of which are conducted in the ordinary course of business.

For further information on the Bank’s related party transactions, including detailed breakdowns of amounts receivable from related parties and the income and expenses relating to related party transactions, see Note 30 of the Bank’s financial statements as of and for the years ended December 31, 2011 and 2012, respectively.

MANAGEMENT, PRINCIPAL SHAREHOLDERS AND EMPLOYEES

Board of Directors

The overall management and supervision of the Bank is undertaken by its BOD. The BOD is empowered to direct, manage and supervise, under its collective responsibility, the affairs of the Bank. It is also responsible for the proper administration and management of the Bank's trust business. The Articles of Incorporation of the Bank currently provide for a BOD of not more than 15 Directors. Directors are elected at the annual meeting of shareholders which is, in accordance with the Bank's by-laws, held on the fourth Friday of May each year. The 15 candidates receiving the highest number of votes shall be declared elected. Each elected Director has a term of office of one year and is eligible for re-election the following year. Currently, the Board consists of 15 Directors.

The following is a brief description of the business experience of each of the Directors:

Justo A. Ortiz, serves as the Chairman of the Board and Chief Executive Officer (CEO) of the Bank. He is also currently the Chairman of Union Properties, Inc. (UPI), a director in Aboitiz Equity Ventures, Inc., Megalink and LGU Guarantee Corporation. Mr. Ortiz is a member of World Presidents Organization. Prior to joining the Bank, he had 16 years of business experience at Citibank (Manila).

Jon Ramon M. Aboitiz, serves as the Vice-Chairman of the Board of the Bank. He is currently Chairman of Aboitiz & Co., Inc. and Aboitiz Equity Ventures, Inc., a Cebu-based investment and management enterprise, engaged in numerous and diverse business concerns ranging from power-generation and distribution, banking and financial services, real estate development, construction, food, ship building, ship management/ crewing/ international shipping closely linked to nation building and progress. Mr. Aboitiz began his career with the Aboitiz Group in 1970. From manager of the Aboitiz Shipping Corporation, Mr. Aboitiz was promoted to President of the company in 1976 and became President of Aboitiz & Company in 1991 until 2008. He was President and CEO of Aboitiz Equity Ventures from 1993-2008. Currently, Mr. Aboitiz holds various positions in the Aboitiz Group including Chairman of the Board, Aboitiz Jebsen Bulk Transport Corporation. He is Vice-Chairman of Aboitiz Power Corporation and Director of CitySavings. He is also a Director of the International Container Terminal Services, Inc. and Bloomberry Resorts Corporation. He serves as President/Trustee of the Aboitiz, Foundation, Inc., Vice President and Trustee of the Ramon Aboitiz Foundation, Inc. and in the Board of Trustees of Santa Clara University, Santa Clara, California, USA. He is a member of the board of Advisors for the Association of Foundations as well as the Coca Cola Bottlers Philippines, Inc. Mr. Aboitiz holds a B.S. Commerce degree major in Management from the University of Santa Clara, California.

Vicente R. Ayllon, serves as the Vice-Chairman of the Board of the Bank. He is currently the Chairman of the Board and Chief Executive Officer of The Insular Life Assurance Co., Ltd. He also sits as Chairman and President of the Insular Property Holdings, Inc. (formerly Vigan Realty, Inc.) and is the Chairman of Insular Investment Corporation, Insular Health Care, Inc., Insular Foundation, ILMADECO and Home Credit Mutual Building & Loan Association, Inc. Mr. Ayllon is also Vice Chairman of Mapfre Insular Insurance Corporation. From 2003 to 2004, he was director of the Philippine Stock Exchange, Inc. From 1995 to 2003, he served as Chairman of the Board and President of The Insular Life Assurance Co., Ltd. His other directorships include Pilipinas Shell

Petroleum Corporation, Shell Company of the Philippines, Ltd., Rockwell Land Corporation and The Palms Country Club.

Victor B. Valdepeñas, serves as the President and Chief Operating Officer of the Bank. He is also currently director of Union Properties, Inc. (UPI). He served as Executive Vice President and Chief Financial Officer of the Bank from 1993 to 1998. Prior to joining the Bank, he was the Vice-President and the Country Treasurer of Citibank Manila from 1987 to 1994, Deputy Treasurer/Group Head of all Trading Divisions of Citibank Manila from 1981 to 1986, Country Economist of Citibank Manila from 1974 to 1980. Prior to Citibank he was the Assistant Director of National Economic & Development Authority's Economic Planning & Research, Consultant to the Chairman of the National Economic Council and was a Faculty Member of the University of the Philippines and professorial lecturer at the University of Santo Tomas. He was previously the President of the Philippine Economics Society and Foreign Exchange Association of the Philippines. He was likewise Chairman and President of UBP Currency Brokers, Inc.

Erramon I. Aboitiz, serves as Director of the Bank. He currently sits as President and Chief Executive Officer of Aboitiz Equity Ventures, Inc. and he holds the same position for Aboitiz Power Power Corporation and Aboitiz & Company, Inc. He is also the Chairman of Aboitiz Renewables, Inc., Therma Power, Inc., SN Aboitiz Power, Davao Light & Power Co., Cotabato Light & Power Co., Subic EnerZone Corp., CitySavings, Visayan Electric Co., San Fernando Electric Light and Power Co., and Aboitiz Foundation, Inc. He also sits as Director of Pilmico Foods Corp., Aboitiz Land, Inc., and Family Business Development Center (Ateneo de Manila University).

Iker M. Aboitiz, serves as Director of the Bank. He is also currently First Vice President/Chief Financial Officer/Corporate Information Officer of Aboitiz Power Corporation. He is also the Director and Chief Financial Officer of Abovant Holdings, Inc. and East Asia Utilities Corporation; Chief Financial Officer and Treasurer of Hijos de F. Escaño; and Director of Cebu Private Power Corporation, Cotabato Light & Power Company, Southern Philippines Power Corporation, Hedcor Benguet, Inc., Therma Power, Inc. and Aboitiz Renewables, Inc.; and Board of Adviser of Aboitiz & Co., Inc. Mr. Aboitiz began his career with the Aboitiz & Company, Inc. in 1994. He held various positions in the Aboitiz & Company, Inc. including Analyst - Corporate Planning Department from 1994- 1995, Trader - Treasury Department from Feb. 1995 to June 1995, Assistant Treasurer - Treasury Department from 1995 to 1997 and Assistant Vice-President, Head - Corporate Finance Dept. from 1998 to 1999. He served also as Treasurer of Davao Light & Power Company, Inc. and Cotabato Light & Power Company from 1998 to 1999. He was previously Adviser to the Board of Directors of CitySavings from 1998 to 1999. Mr. Aboitiz was also Executive Assistant to the Chairman & CEO of UnionBank and Member of UnionBank Asset and Liability Committee (ALCO) from 1999 to 2000. He served as Analyst – Corporate Finance Group of Credit Lyonaisse SA Exchange Capital Corp. from 2000 to 2003 and Chief Finance Officer of Aboitiz Construction Group Inc. from 2003 to 2007. He worked for FBMA Marine Inc. in several positions including Chief Finance Officer, Member of the Board of Directors and Executive Committee from 2003 to 2007. Mr. Aboitiz has a Bachelor of Science Degree in Business Management major in Finance, Cum Laude from the Boston College, Newton, Massachusetts.

Sabin M. Aboitiz is the President and Chief Executive Officer of Pilmico Foods Corporation, a wholly-owned subsidiary of Aboitiz Equity Ventures (AEV) and Aseagas Corporation, a joint venture between AEV and UK-based Gazasia. Concurrently, he is the President of Philippine Flour Millers

Association, Inc. (PAFMIL). He also sits as Director of Aboitiz Jebsen Company, Inc., SN Aboitiz Power Group and Manila Oslo Renewable Energy. He spent most of his professional life with Aboitiz Transport, Inc. and his last position was as President and Chief Executive Officer of one of its subsidiaries, Aboitiz One, Inc., (owner of the 2GO brand) which is now called 2GO Group, Inc. He graduated from Gonzaga University in the USA with a degree of B.S. Business Administration major in Finance.

Juan Antonio E. Bernad, serves as Director of the Bank. He is also currently Senior Vice - President of Aboitiz Equity Ventures, Inc. (since 1995), Executive Vice - President – Strategy & Regulatory Affairs of Aboitiz Power Corporation (since 1998) and Director Cotabato Light & Power Corporation (since 1989). His other directorships include Visayan Electric Co. (since 2009), San Fernando Electric Company (since 2001), Mamerto Escano Inc. (since 1987) and EVP-Regulatory Affairs of Davao Light & Power Corporation (since 1989).

Stephen G. Paradies, serves as Director of the Bank. He also serves as Director of Union Properties, Inc., Chairman of the Operations Risk Management Committee and Vice Chair of the Audit Committee of the Bank. He is a director of several Aboitiz subsidiaries including Pilmico Foods Corp., Pilmico Animal Nutrition Corp., Aboitiz Construction Group Inc. and CitySavings. He sits on the board of Int'l. Container Terminal Services Inc. and several of its subsidiaries, including ICTSI Int'l. He is currently Senior Vice President/Finance of Aboitiz and Co. Inc, and Senior Vice President/Chief Finance Officer of Aboitiz Equity Ventures, Inc.

Emilio S. de Quiros, Jr., serves as Director of the Bank. He also sits as Director of Philhealth Insurance Corporation, Belle Corporation (September 30, 2010 to present). He is the President and CEO of the Social Security System from August 16, 2010 to present.

Eliza R. Antonino, serves as Director of the Bank. She is also a Director of Philex Mining Corporation and Philamlife Tower Management Corporation. In addition, she has been a sitting Commissioner of the Social Security Commission since September 2010.

Mayo Jose B. Ongsingco, serves as Director of the Bank. He has been the President and Chief Operating Officer, and a Trustee of Insular Life Assurance Co. Ltd since 2004. He concurrently holds the position of Chairman of the Board for Insular Life Employees' Retirement Fund and Insular Life General Insurance Agency, Inc. He is Vice Chairman and President of Insular Life Management & Development Corp. He is also Vice Chairman of Insular Health Care, Inc., Insular Life Property Holdings, Inc. and Home Credit Mutual Building & Loan Association. His other directorships include Insular Investment Corporation, Insular Life Foundation, Keppel Philippines Holdings, Inc., Mapfre Insular Insurance Corp., Pilipinas Shell Petroleum Corp. and PPI Prime Venture, Inc.

Armand F. Braun, Jr., serves as Independent Director of the Bank. He is also currently the Chairman and President of AF Braun Company and Holdings, Inc. He was the President of UnionBank from 1990 to 1997. His business experience includes directorships in UBP Capital Corporation and Union Properties, Inc. before their merger in December, 2004, after which merger, he was a director of the surviving entity, Union Properties, Inc., until July 2005; Alrose Foods Corp., Iligan Pizza Corp., North Iligan Food Services, Inc., Central Iligan Fast foods, Bern Bakery Specialists, Inc. – Store 1, Bern Bakery Specialists, Inc. – Store 2, Beefoods Corp., and Philam Asset Management, Inc.

Carlos B. Raymond, Jr., serves as Independent Director of the Bank. He retired from Eli Lilly and Company on February 28, 2003 after almost 24 years with the company. Eli Lilly is a U.S. multinational pharmaceutical company based in Indianapolis, Indiana. His last position was President and General Manager of Eli Lilly Philippines. His previous assignments with Lilly included positions in Puerto Rico, Indianapolis, Singapore as Regional Head of Southeast Asia Operations and at Lilly Taiwan as President/General Manager. He graduated from the University of the Philippines with a degree of B.S. Business Administration. Prior to joining Lilly, he worked at Unicor Inc. (Doctors Pharmaceuticals' marketing arm) for 11 years (July 1968 to May 1979) with his last position as General Manager.

Reynato S. Puno, serves as Independent Director of the Bank. He was a former Chief Justice of the Supreme Court from 2007 to 2010. He also serves as an Independent Director of San Miguel Corporation, San Miguel Corporation (Hongkong) and Apex Mining. He was also reappointed on 2012 as Regent of the UP Board of Regents. He was then an Independent Director of Manila Bulletin from 2010 to 2011. He also held various positions in the government such as – Assistant Solicitor General in the Office of the Solicitor General from 1971 to 1982; Associate Justice in the Intermediate Appellate Court from 1983 to 1984; Deputy Minister in the Ministry of Justice from 1984 to 1986; and Associate Justice of the Court of Appeals from 1986 to 1993 and Associate Justice of the Supreme Court from 1993 to 2007.

Executive Officers

The executive officers (“Executive Officers”) of the Bank, subject to control and supervision of the Board, collectively have direct charge of all business activities of the Bank. They are responsible for the implementation of the policies set by the Board.

The following is a brief description of the business experience of each of the Executive Officers. For the business experience of Justo A. Ortiz and Victor B. Valdepeňas, please refer to the previous section "Board of Directors".

Victor B. Valdepeñas, serves as the President and Chief Operating Officer of the Bank. He is also currently director of Union Properties, Inc. (UPI). He served as Executive Vice President and Chief Financial Officer of the Bank from 1993 to 1998. Prior to joining the Bank, he was the Vice-President and the Country Treasurer of Citibank Manila from 1987 to 1994, Deputy Treasurer/Group Head of all Trading Divisions of Citibank Manila from 1981 to 1986, Country Economist of Citibank Manila from 1974 to 1980 and the Assistant Director of National Economic & Development Authority’s Economic Planning & Research. He was also Consultant to the Chairman of the National Economic Council and was a Faculty Member of the University of the Philippines and professional lecturer at the University of Santo Tomas. He was previously the President of the Philippine Economics Society and Foreign Exchange Association of the Philippines. He was likewise Chairman and President of UBP Currency Brokers, Inc.

Edwin R. Bautista, serves as Senior Executive Vice-President, Head of the Transaction Banking, Commercial Banking and Channel Management Centers of the Bank. He was also appointed as President of International Exchange Bank following the merger. He was Senior Vice-President of the Bank from 1997 to 2001. He previously worked as Senior Brand Manager at Procter and Gamble Mfg. from 1983 to 1987, Marketing and Sales Director of the Philippines and Guam at American

Express International from 1990 to 1991, and the Vice-President and Group Head of Transaction Banking at Citibank, Philippines from 1991 to 1997.

Eugene S. Acevedo, serves as Senior Executive Vice-President, Head of the Retail Banking and Corporate Banking Centers. He was previously President, Vice Chairman and Chief Executive Officer of Philippine National Bank from May 2010 to July 2011. Before that he was with Citibank for 23 years and his last posts with the firm were as Managing Director and Country Treasurer for Hong Kong, and Global Markets Head for Hongkong-Taiwan Cluster. From 1984 to 1985, he was a Physics lecturer at the University of the Philippines.

Jesus Roberto S. Reyes, serves as Senior Executive Vice-President and Tresurer of the Bank. Prior to joining the Bank, he spent 10 years in Security Bank and his last position was Head of Treasury and Investment Banking Segment. Prior to Security Bank, he was Deputy Treasurer of HSBC-Manila from 1994-1999.

Genaro V. Lapez, serves as Executive Vice-President and Center Head for Consumer Finance, Credit Cards Marketing and Global Filipino of the Bank. Prior to joining the Bank, he was an experienced Business Leader in leading Local and Multinational Companies – both at multi-country and single-country level – with extensive Marketing/New Business Development experience and solid track-record in Turnarounds. His career has spanned to numerous consumer product categories from personal care, OTC (over-the-counter) pharmaceuticals, "content" products (publishing & music and video licensing), food & beverage (both alcoholic and non-alcoholic), and "e-financial" services.

Teodoro M. Panganiban, serves as Executive Vice-President and Chief Risk Officer of the Bank. He was Senior Vice-President of the Bank from 1997 to 2001. Prior to joining the Bank, he was Vice-President and Senior Country Operations Officer at Citibank N.A., Philippines. He held several positions at Citibank N.A. from 1971 to 1997 in Manila, Cebu, Hong Kong, Belgium and New Zealand. He is currently Director of the Philippine Clearing House Corporation and Member of the Operations Committee of the Bankers Association of the Philippines.

Beatriz R. Barredo-Romulo, serves as Executive Vice-President and the Head of the Commercial Banking Center of the Bank. She was previously the Executive Vice-President and the Head of the Corporate Banking Cluster of International Exchange Bank. Prior to that, she was the Senior Vice-President and the Head of the Account Management Division of United Coconut Planters Bank (UCPB) from 1991 to 1995. She was also the vice-chairman of UCPB Leasing and Finance Corporation and was a director for various subsidiaries of UCPB from 1992 to 1995.

Catalino S. Abacan is Executive Vice-President and Head of Channels Management Center effective September 2011. His past positions in UnionBank are the following: Vice-President/Region Service Operations Officer in 1997 to 2000, Vice President/Operations Head of UnionBank Visa Credit Card Unit in 2000 to 2004 and Senior Vice-President/Head of Liabilities Products/Branch/Credit Card Operations in 2004 to September 2011. From 1994 to 1997, he was Vice-President for Operations, Manila Offshore Banking Unit of Lippo Bank of Indonesia. From November 1996 to April 1997, he was instrumental in setting up a branch of Lippo Bank in Phnom Penh, Cambodia. He held several positions in Philippine Banking Corporation from 1975 to 1993 namely Credit Investigator-Appraiser, Head of Credit Investigation-Appraisal Unit, Branch Cashier, Branch Manager and Area Head for Manila 31 branches. The last position he held was Group Head for Operations in Transaction Banking, International/FCDU and Treasury.

Roberto F. Abastillas, serves as Senior Vice-President of the Bank. He was previously Senior Vice-President and Head of the Account Management Center I at International Exchange Bank. From 1987 to 1995, he was Vice- President and Head of the Account Management Group for UCPB.

Ramon G. Duarte, serves as Senior Vice-President and Head of Retail Product Development of the Bank. He was previously Chief Technology Officer of Dotenable, Inc. from 2000 to 2001; Head of Electronic Banking Transaction Services at ABN AMRO Philippines from 1999 to 2000; and Assistant Vice-President of Product Management under Global Transaction Services at Citibank from 1996 to 1999.

Joyce S. Gonzalez, serves as Senior Vice-President of the Bank and Deputy Center Head of Retail Banking Center of the Bank. She started her career in Unionbank as Branch Manager of the Main Office Branch in 1994. After a few months, she was given an expanded role as Sales Director of the Makati 1 Region. Her stint as Sales Director over the years saw major growth in the deposit and fund generation business, and the development of a very capable sales management team. In recognition of her contribution to the business, Joyce was promoted to Senior Vice President and was given an additional task to develop and lead Customer Segment Management and bring greater customer centricity in UnionBank's pursuit in delighting its customers, given her seasoned abilities, and exposure in the business of Retail Banking.

Atty. Cesar G. Ilagan serves as Senior Vice President and Financial Controller of the Bank. Prior to this, he was the Asia Regional Controller for Cypress Semiconductor Philippines, Inc. from 1998 to 1999. He served as Controller, General Counsel and Corporate Secretary of Intel Philippines Manufacturing, Inc. and Intel Technology Philippines, Inc. from 1982 to 1998. He was Vice President for Finance and Administration of Fil-Hispano Ceramics, Inc. and Fil-Mosaic Corporation, where he worked from 1978 to 1982.

Atty. Fe B. Macalino, serves as Senior Vice-President, Corporate Secretary and General Counsel of the Bank. She began her career with the Bank in 1989. Her business experience includes an extensive legal and corporate practice in the fields of banking, investment and financial leasing services, manufacturing, trading, air chartering, cargo and bulk handling, shipping, security services. She previously worked at the Family Savings Bank prior to its acquisition by the Bank of the Philippine Islands from 1979 to 1982. She was Assistant Vice-President in charge of legal and collection at the State Investment House, Inc. from 1982 to 1985. She also served as the President of the Bank Administration Institute (BAI), Philippine Chapter. She was also the Corporate Secretary, Vice President and Corporate Legal Counsel for the Philippines in Asian Alcohol Corporation, Far East Molasses Corporation, Ayala Molasses Company, Total Bulk Corporation, Asian Air Charters, Inc., and Chairman and CEO of Bulldog Security Agency, Inc.

Angelo Dennis L. Matutina, holds the position of Senior Vice-President and head of Branch Operations Management. He was hired in Unionbank on March 2002 as First Vice President; previously he was Assistant Vice President in Citibank and prior thereto as Product Manager.

Manuel G. Santiago, Jr., holds the position of Senior Vice-President and Credit Cards Product Business Head. He previously worked as Director for Operations in American Express Bank in Indonesia and prior thereto, Director for Operations in American Express International, Manila.

Ceferino P. Tolentino, Jr., serves as Senior Vice-President of the Bank. Prior to joining the Bank, he was Vice President in charge of the technical services at Dynamic Software Solutions International from 1987 to 1989 and Assistant Vice-President of technology services of Metrobank from 1989 to 1994.

Jose Levi S. Villanueva is Senior Vice-President and Head of Retail Banking Center of the Bank. Prior to joining the Bank, he was General Manager for PILTEL in the Visayas Region, Segment Manager for IBM-VISMIN and Vice-President for Sales Management and Control under the Consumer Banking Group in Citibank.

Michaela Sophia E. Rubio, serves as First Vice President of the Bank and HR Director. She joined the Bank in 2004 as Vice President and handled the Human Resource Services, Training and Organization Development 32 divisions. Subsequently, she became the Deputy HR Director. Prior to joining the Bank, she was the Vice President and Country Human Resource, Quality and Corporate Communications Head in the Philippines of the global electrical and power company, Asea Brown Boveri (ABB) from 1999 to 2001. She worked from 2001 to 2003 as a Senior Consultant in OTi Consulting Singapore working with government owned and private organizations on Singapore Quality Class/Award, People Developer, Industry Capability Upgrading (ICAP) and Work Life and Work Redesign of which she was certified by SPRING Singapore. Before a career in Human Resource, she worked for 10 years in the semiconductor and electronics manufacturing industry handling engineering and managerial functions in Statistical Process Control and Quality.

Myrna E. Amahan, serves as Vice-President and Internal Auditor of the Bank. She is a Certified Public Accountant (CPA), Certified Internal Auditor (CIA), Certified Information Systems Auditor (CISA) and has the designation of Certification in the Governance of Enterprise Information Technology (CGEIT). On top of these certifications in the field of internal audit and information technology, Mrs. Amahan is a qualified internal audit external validator for having undertaken the necessary training as well as passing the required exams. As qualified external validator, Mrs. Amahan is qualified to conduct a quality assessment of internal audit units as required under the International Standards for the Professional Practice of Internal Auditing. She previously worked as supervising IS auditor at Equitable-PCI Bank from 1996 to 2000 and was Head of the System Consultancy Services of the Commission on Audit from 1993 to 1996. Also while with the Commission on Audit, Mrs. Amahan was among the government auditors sent to various United Nations agencies to conduct information systems audit. Mrs. Amahan graduated Magna Cum laude with the degree of Bachelor of Science in Commerce Major in Accounting from the University of San Carlos. She obtained a Masters Degree in Public Management from the Development Academy of the Philippines in 1994.

Robert B. Ramos, serves as Vice-President and Trust Officer of the bank. From 1995, Mr. Ramos held various positions performing corporate finance, product/business development and wealth management functions. Mr. Ramos is a Registered Financial Consultant and a CFA Charterholder. Mr. Ramos also completed the one year course on Trust Operations with distinction.

Rodrigo J. Montaniel, serves as an Assistant Vice President and the Acting Compliance and Corporate Governance of the Bank. He was a former Sales Director of the Retail Banking Center prior to reassignment in the Internal Audit Division of the Bank as Auditor in 2012. Mr. Montaniel's banking career and experience includes Branch Operations and Accounting and Auditing. Mr. Montaniel is a Certifed Public Account and a Civil Service Professional.

Board Committees

The BOD has constituted certain committees to effectively manage the operations of the Bank, including various risk management activities. The Bank's principal committees of the BOD include the EXCOM, the RMC, the MRC, the ALCO, the ORMC, the Audit Committee, the Nominations Committee, the CompRem Committee, the Trust Committee and the Corporate Governance Committee. A brief description of the functions and responsibilities of the key committees are set out below:

Executive Committee

The EXCOM, composed of seven (7) members of the BOD, exercises certain functions as delegated by the BOD including, among others, the approval of credit proposals, asset recovery and ROPA sales within its delegated limits.

Risk Management Committee

The RMC, composed of seven (7) members of the BOD, is responsible for the development and oversight of the Bank's risk management program. It assists the BOD in overseeing all matters relating to risk management including providing a comprehensive and firm-wide oversight of all risks and the management of such risks, formulating and reviewing all of the Bank's material risk policies, strategies, and procedures. Among its specific duties are to identify and evaluate exposures, develop risk management strategies, implement risk management plans and review such plans as necessary. It also provides oversight, direction, and counsel to the other committees including the MRC and the ORMC.

The RMC is supported by the different risk management units (Credit Risk, Market Risk and Operations Risk).

Market Risk Committee

The MRC composed of five (5) members of the BOD, sets policies and standards for the management of the market risk, liquidity risk and interest rate risk in the banking book. The MRC also monitors the sensitivity of the Bank's financial condition to the effects of market volatility and adverse price changes on the Bank's portfolio of financial instrument and oversees the Bank's liquidity position.

Assets and Liability Committee

The ALCO is responsible for ensuring that the Bank's liquidity management process is adequate and that the Bank maintains adequate liquidity and sufficient capital. The ALCO manages the Bank's balance sheet and ensures that business strategies are consistent with the Bank's liquidity, capital and funding strategies as well as sets targets for balance sheet size. It also establishes asset/liability pricing policies appropriate to the Bank's balance sheet objectives, and determines the level of stress condition the Bank is experiencing.

The ALCO is composed of the President, the Treasurer, Center Heads and Group Heads. The ALCO is chaired by the President.

Operations Risk Management Committee

The ORMC comprises three (3) members of the BOD and two (2) members from senior management. It is responsible for reviewing various operations risk policies and practices, including among others, those policies and practices of the Bank's branches, internet banking, CPS locations and treasury operations. Management Committees and units, which are directly involved in managing activities of the Bank, which may result in operations risk expsosure are mandated to report to the Committee. Among these are: Technology Steering Committee, Anti-Fraud Management Unit, Fraud Investigation Unit, Operations Risk Management Division and Control Division.

Audit Committee

The Audit Committee is a committee of the BOD that is composed of five (5) members, most with accounting, auditing, or related financial management expertise or experience. The Audit Committee believes that the skills, qualifications, and experience of its members are appropriate for them to perform their duties as laid down by the Board. Two (2) of these five (5) members are independent directors, including the Chairman.

Please refer to the extensive discussion on the functions of the Audit Committee under “Risk Management”.

Nominations Committee

The Nominations Committee is comprised of at least three (3) voting members of the BOD, one of whom is an independent Director and one (1) non-voting member who is the Human Resources Director. The Nominations Committee is responsible for promulgating guidelines and criteria and putting in place screening policies and parameters to enable it to effectively review the qualifications of candidates for the BOD, key officers of the Bank and nominees for independent Directors.

Compensation and Remuneration Committee

The CompRem Committee is composed of five (5) members of the BOD and is responsible for overseeing employee compensation and benefits and approving recommendations of promotions and compensation adjustments.

Trust Committee

The Trust Committee comprises five (5) members including three (3) Directors appointed by the Board on a regular rotation basis. The Trust Committee is primarily responsible for (i) the acceptance and closure of trust and other fiduciary accounts, (ii) the initial review of assets placed under the custody of a trustee or a fiduciary, (iii) the investment, reinvestment and disposition of trust funds and properties and (iv) the review and approval of transactions between trust and fiduciary accounts.

Corporate Governance Committee

The Committee has seven (7) members of the BOD, three (3) of whom are Independent Directors, including the chairman, and one (1) belonging to the Bank’s senior management. The Committee annually evaluates the governance state of the Bank by using as benchmark the Corporate Governance Scorecard of the Institute of Corporate Directors for publicly listed companies and banks, the PSE’s Corporate Governance Guidelines Disclosure and other relevant governance metrics.

The specific duties of the Committee include, among others, making recommendations to the BOD regarding continuing education of directors and overseeing its periodic performance evaluation, its Committees and senior management. It has two (2) sub-committees, namely, the Nominations Committee and the CompRem Committee.

Please refer to the extensive discussion on the functions of the Corporate Governance Committee under "RISK MANAGEMENT".

Compliance with Corporate Governance Practices

The Bank is compliant with various regulations and established practices on corporate governance. It has complied with the requirement of the Philippine SEC on the one-time submission of its Corporate Governance Self Rating Form in July 2003. For the fiscal year 2012, it has also submitted its Annual Corporate Governance Report to the Philippine SEC. These reports are in addition to the Bank's annual certification to SEC of its compliance with its Manual on Corporate Governance.

The Bank also annually accomplishes and submits its Corporate Governance Guidelines Disclosure to PSE. Since 2010, it has been 97.0% compliant with the corporate governance practices and recommendations of the PSE.

The Bank also participates annually in the Corporate Governance Scorecard Survey of the Institute of Corporate Directors (ICD) for publicly listed companies (PLCs) as required by the Philippine SEC. The Corporate Governance Scorecard Survey for PLCs evaluates a company's corporate governance based on disclosure and transparency (25.0% weight), board responsibilities (25.0%), rights of shareholders (20.0%), equitable treatment of shareholders (20.0%) and role of stakeholders (10.0%). The Bank has been consistently recognized as a Silver Awardee in both 2009 and 2010 Corporate Governance Scorecard surveys for PLCs. In the last run of ICD's corporate governance scorecard for 2011, the Bank received a gold award for garnering 96.0% rating. For 2012, the Bank participated in the ASEAN corporate governance scorecard, the results of which are yet to be announced.

The Bank has adopted policies and mechanisms aimed at bolstering its current resilient corporate governance regime. Its Manual on Corporate Governance embodies leading principles and practices on good corporate governance. It lays down the details on the Bank's governance and compliance system, organizational and procedural controls, independent audit mechanism as well as the functions of the external auditor and of the Chief Compliance & Corporate Governance Officer. It further provides for policies on conflict of interest and related party transactions, disclosure and transparency and compliance system of the Bank. Most importantly, the Corporate Governance Manual underscores its recognition and continuous promotion of the rights of its stockholders, especially those of the minority.

The Bank improved its governance regime based on the BSP's Guidelines in Strengthening Corporate Governance in Financial Institutions. It has introduced changes in its BOD structure aimed at intensifying board governance, including, among others, the addition of another independent director, imposition of term limits for independent directors, and designating an independent director as chairman of the Corporate Governance Committee. The Bank is not aware of any significant governance issues or deviation from its Corporate Governance Manual.

Principal Shareholders

The following table sets out the 20 largest shareholders of the Bank as of June 30, 2013:

	STOCKHOLDERS	SHARES	%
1	ABOITIZ EQUITY VENTURES, INC.	283,237,326	44.16%
2	THE INSULAR LIFE ASSURANCE CO., LTD.	103,359,301	16.11%
3	PCD NOMINEE CORPORATION	89,236,270	13.91%
4	SOCIAL SECURITY SYSTEM	69,777,289	10.88%
5	SOCIAL SECURITY SYSTEM (1)	19,952,256	3.11%
6	PCD NOMINEE CORPORATION	19,123,715	2.98%
7	JUSTO A. ORTIZ	4,959,673	0.77%
8	VIC VALDEPENAS	3,540,502	0.55%
9	SANFIL MANAGEMENT CORPORATION	2,168,299	0.34%
10	MA. VICTORIA A. CODY	1,326,292	0.21%
11	WINDEMERE MANAGEMENT CORPORATION	1,034,116	0.16%
12	DONYA I MANAGEMENT CORP.	1,033,378	0.16%
13	RAMON ABOITIZ FOUNDATION, INC.	1,011,482	0.16%
14	MOREFUND CORPORATION	880,897	0.14%
15	LUIS MIGUEL O. ABOITIZ	852,365	0.13%
16	CIA MANAGEMENT CORPORATION	829,007	0.13%
	ASPIRA MANAGEMENT, INC.	829,007	0.13%
	FORTES MANAGEMENT, INC.	829,007	0.13%
17	AZURA MANAGEMENT, INC.	829,006	0.13%
18	GUIA C. LIM	802,338	0.13%
19	ANSO MANAGEMENT CORPORATION	792,472	0.12%
20	HAWK VIEW CAPITAL, INC.	776,924	0.12%
	PORTOLA INVESTORS, INC.	776,924	0.12%
	SUB-TOTAL	**607,957,846**	**94.78%**
	OTHER STOCKHOLDERS	33,464,574	5.22%
	TOTAL ISSUED AND OUTSTANDING SHARES	**641,422,420**	**100.00%**

Employees

As of December 31, 2012, the Bank employed 2,816 people, 123 as Executives, 1,859 as Officers, 834 as Clerical Staff and covered by Collaborative Bargaining Agreement (CBA). Of these, 1,965 are in Operations, 283 are in Non-Operations, and 568 are in Sales/Marketing. The Bank does not foresee an increase in the number of headcount within the ensuing 12 months.

	As of June 30, 2013
Sales	487
Support	970
Operations	1,897
Total	**3,354**

As of December 31, 2012, approximately 49.0% of the Bank's employees were employed at its head office and 51.0% at its branches. The average age of the Bank’s employees is 36 years, and the average employment tenure is 9 years. The normal retirement age for the Bank is 60 years.

The Bank has a funded non-contributory retirement plan covering substantially all of its officers and regular employees. As of December 31, 2012, the fair value of the assets in the retirement funds of the Bank amounted to an aggregate of ₱1.7 billion and the actuarial present value of retirement benefits of the Bank collectively amounted to ₱2.4 billion. The principal actuarial assumptions used by the Bank to determine the cost of retirement benefits include an investment earning rate of 6.0% and a salary increase of 7.0% per annum, compounded annually.

The Bank's non-managerial staff are represented by the UnionBank Employees’ Association. The current CBA between the Bank and the UnionBank Employees' Association was made in respect of the period from June 1, 2010 to May 31, 2015 and the negotiation on the economic terms of the agreement in respect to June 1, 2013 to May 31, 2015 was completed. The Bank maintains harmonious relations with the UnionBank Employees' Association.

The Bank views its employees as an important asset and regularly provides training as well as employment development programs to enhance their work capabilities, functional, managerial and leadership competencies. In the fourth Quarter of 2008, the Bank institutionalized its nine (9) academies: Self Mastery, Leadership and Management, Sales, Risk, Marketing, Operations, Information Technology, Six Sigma, Finance under the UnionBank University. The UnionBank University's aim is to grow banking leaders and build expertise. In order to support the Bank's strategy, FOCUS; the UnionBank University ensures that programs continue to raise the bar in marketing, innovation, risk and banking leadership. It maintains a structured curriculum for different job functions across the Bank and is supported by internal and external faculty and institutional partners – all experts in their field.

PHILIPPINE TAXATION

Following is a general description of certain Philippine tax aspects of investment by prospective LTNCD Holders. It is based on the Philippine National Internal Revenue Code (the "Tax Code") and its implementing regulations and rulings in effect at the date of this Offering Circular. Subsequent legislative, judicial or administrative changes or interpretations may be retroactive and could affect the tax consequences to the prospective LTNCD Holders. The tax treatment of a prospective LTNCD Holder may vary depending on such LTNCD Holder's particular situation and certain prospective LTNCD Holders may be subject to special rules not discussed below. This summary does not purport to address all tax aspects that may be important to a prospective LTNCD Holder. This general description does not purport to be a comprehensive description of the Philippine tax aspects of investment in the LTNCD and no information is provided regarding the tax aspects of acquiring, owning, holding or disposing the LTNCDs under applicable tax laws of other jurisdictions and the specific tax consequence in light of particular situations of acquiring, owning, holding and disposing the LTNCDs in such other jurisdictions.

EACH PROSPECTIVE LTNCD HOLDER SHOULD CONSULT WITH HIS OWN TAX ADVISER AS TO THE PARTICULAR TAX CONSEQUENCES TO SUCH LTNCD HOLDER OF PURCHASING, OWNING AND DISPOSING OF THE LTNCDs, INCLUDING THE APPLICABILITY AND EFFECT OF ANY STATE, LOCAL AND NATIONAL TAX LAWS.

As used in this section, the term "resident alien" refers to an individual whose residence is within the Philippines but who is not a citizen of the Philippines; a "non-resident alien" is an individual whose residence is not within the Philippines and who is not a citizen of the Philippines; a non-resident alien who is actually within the Philippines for an aggregate period of more than 180 days during any calendar year is considered a "non-resident alien doing business in the Philippines"; otherwise, such non-resident alien who is actually within the Philippines for an aggregate period of 180 days or less during any calendar year is considered a "non-resident alien not doing business in the Philippines." A "resident foreign corporation" is a foreign corporation engaged in trade or business within the Philippines; and a "non-resident foreign corporation" is a foreign corporation not engaged in trade or business within the Philippines. The term "foreign" when applied to a corporation means a corporation which is not domestic while the term "domestic" when applied to a corporation means a corporation created or organized in the Philippines or under its laws.

TAXATION OF INTEREST INCOME

The LTNCDs will be, under current interpretation of the Tax Code, treated as long-term deposits or investments. Interest income thus earned by the LTNCD Holders shall be taxed as described in the following sections.

Interest income earned by individuals

As a general rule, interest income from long-term deposits or investments earned by individual citizens of the Philippines, resident aliens and non-resident aliens engaged in trade or business in the Philippines is subject to a final withholding tax at the rate of twenty percent (20.0%). The Tax Code, however, provides for the exemption from the twenty percent (20.0%) final withholding tax of interest income from long-term deposits earned by the abovementioned individuals, provided the long-term deposit is not pre-terminated before the fifth year and the following requirements are complied with.

The long-term deposit –

(1) Must have a maturity of not less than five (5) years;

(2) Must be in the form of savings, common or individual trust fund, deposit substitutes, investment management accounts or other forms which must be prescribed by the BSP;

(3) Must be issued by banks only (not by non-bank financial intermediaries and finance companies);

(4) Must be issued to individual citizens, resident aliens, or non-resident aliens engaged in trade or business within the Philippines;

(5) Must be under the name of the individual and not under the name of the corporation or a bank or the trust department/unit of a bank;

(6) Must be in denominations of ₱10,000 or other denominations as may be prescribed by the BSP;

(7) Should not be pre-terminated by the Holder thereof before the fifth year; and

(8) Except those specifically exempted by law or regulations, any other income such as gains from trading and foreign exchange gain is not covered by income tax exemption.

LTNCD Holders who are individual citizens, resident aliens and non-resident aliens engaged in trade and business in the Philippines who shall hold on to the LTNCDs for at least five (5) years shall be exempt from the twenty percent (20.0%) final withholding tax. However, under BIR Revenue Regulations No. 14-2012, transfers or assignments of the LTNCDs by one individual Holder to another are considered pre-termination solely for tax purposes. Accordingly, should the LTNCD Holder pre-terminate the LTNCD before the fifth year or the other requirements mentioned above are not met, a final tax shall be imposed (on the basis of the holding period of the LTNCD at the rates indicated below) on the entire income and shall be deducted and withheld by the Issuer from the remaining maturity thereof, which shall be borne by the LTNCD Holder:

Four years to less than five years – 5.0%

Three years to less than four years – 12.0%

Less than three years – 20.0%

Interest income received by non-resident aliens not engaged in trade or business in the Philippines shall generally be subject to a final withholding tax of twenty five percent (25.0%). However, such tax rate may be reduced under an applicable tax treaty.

Interest income earned by corporations

Under the Tax Code, the LTNCDs are deposits. Accordingly, interest income earned by domestic and resident foreign corporations from the LTNCDs shall be subject to a final withholding tax of twenty percent (20.0%) of such interest income.

On the other hand, interest income received by a non-resident foreign corporation shall generally be subject to thirty percent (30.0%) final withholding tax. This rate may also be reduced under an applicable tax treaty.

Interest income earned by trusts

Interest income derived by individuals investing in common or individual trust funds or investment management accounts shall be exempt from the twenty percent (20.0%) final withholding tax provided the conditions on tax-exemption of long-term deposits discussed above are complied with and provided the following additional conditions are all present:

1. The investment of the individual investor in the common or individual trust fund or investment management account must be held/managed by the bank for at least five (5) years;
2. The underlying investments of the common or individual trust account or investment management accounts must comply with the requirements of Section 22(FF) of the Tax Code, as well as the requirements mentioned above; and
3. The common or individual trust or investment management account must hold on to such underlying investment for at least five (5) years.

Tax-exempt persons

All sums payable by the Bank to tax-exempt persons shall be paid in full without deductions for taxes, duties, assessments, or government charges, subject to the submission to the Registrar by the LTNCD Holder claiming the exemption of proof of such exemption as prescribed by BIR regulations. (See Terms and Conditions of the LTNCDs.)

Documentary Stamp Taxes

The Tax Code imposes a documentary stamp tax on every original issue of debt instruments at the rate of ₱1.00 on every ₱200, or fractional part thereof, of the face value of such instruments. The Bank has undertaken to pay the documentary stamp tax on the issuance of the LTNCDs.

There is currently no documentary stamp tax due on a subsequent sale or disposition of the LTNCDs.

Taxation on Gains or Losses Upon the Sale or Other Disposition of the LTNCDs

An LTNCD Holder will recognize gains or losses upon the sale or other disposition (including a redemption at maturity) of the LTNCDs in an amount equal to the difference between the amount realized from such disposition and such LTNCD Holder's base cost in the LTNCD. Under the Tax Code, any gain realized from the sale, exchange or retirement of securities, debentures and other certificates of indebtedness with an original maturity date of more than five (5) years (as measured from the date of issuance of such securities, debentures or other certificates of indebtedness) will not be subject to income tax. Since the LTNCDs have a maturity of more than five (5) years from the date of issuance, any gain realized by an LTNCD Holder from the sale of the LTNCDs will not be subject to Philippine income tax.

Value-Added Tax and Gross Receipts Tax

At issuance, no Value-Added Tax ("VAT") shall be imposable upon the LTNCDs. Subsequent transfers shall similarly be free of VAT, unless the LTNCD Holder is a dealer in securities. In that instance, the LTNCD Holder shall be liable to pay twelve percent (12.0%) VAT on the gross income derived from the trading of the LTNCDs. Under Republic Act No. 9238, services rendered in the Philippines by, among others, banks, non-bank financial intermediaries, quasi-banks, finance companies, and other financial intermediaries not performing quasi-banking functions (excluding insurance companies) are exempted from the coverage of the VAT. The exemption, which took effect retroactively on January 1, 2004, reverts to the application of the gross receipts tax ("GRT") regime on services rendered by banks, non-bank financial intermediaries, quasi-banks, finance companies, and other financial intermediaries not performing quasi-banking functions (excluding insurance companies). Rates of GRT shall be as follows:

(1) Banks and Non-Bank Financial Intermediaries Performing Quasi-Banking Functions:

(a) On interest, commission and discounts from lending activities as well as income from financial leasing, on the basis of the remaining maturities of instruments from which such receipts are derived:

Maturity period is five years or less – 5.0%

Maturity period is more than five years – 1.0%

(b) On dividends and equity shares and net income of subsidiaries – 0.0%

(c) On royalties, rentals of real or personal property, profits from exchange and all other items treated as gross income under the Tax Code – 7.0%

(d) On net trading gains within the taxable year on foreign currency, debt securities, derivatives and other similar financial instruments – 7.0%

(2) Other Non-Bank Financial Intermediaries:

(a) On interest, commission, discounts and all other items treated as gross income under the Tax Code – 5.0%

(b) On interest, commission and discounts from lending activities as well as income from financial leasing, on the basis of the remaining maturities of instruments from which such receipts are derived:

Maturity period is five years or less – 5.0%

Maturity period is more than five years – 1.0%

Estate and Donor's Tax

The transfer of the LTNCDs by a decedent to his heirs, whether or not such decedent was residing in the Philippines, will be subject to an estate tax which is levied on the net estate of the deceased at progressive rates ranging from five percent (5.0%) to twenty percent (20.0%) if the net estate is over ₱200,000.

LTNCD Holders, whether or not citizens or residents of the Philippines, will be subject to donor's tax upon the donation of the LTNCDs to strangers at a flat rate of thirty percent (30.0%) of the net gifts. A "stranger" is defined as any person who is not a brother, sister (whether by whole- or half-blood), spouse, ancestor and lineal descendant or relative by consanguinity in the collateral line within the fourth degree of relationship. A donation to a non-stranger will be subject to a donor's tax at progressive rates ranging from two percent (2.0%) to fifteen percent (15.0%) if the net gifts made during the calendar year exceed ₱100,000.

The estate tax, as well as the donor's tax in respect of the LTNCDs, shall not be collected if: (a) the deceased at the time of his death or donation was a citizen and resident of a foreign country which, at the time of his death or donation, did not impose a transfer tax of any character in respect of intangible personal property of citizens of the Philippines not residing in that foreign country; or (b) the laws of the foreign country of which the deceased or the donor was a citizen and resident at the time of his death or donation allows a similar exemption from transfer or death taxes of every character or description in respect of intangible personal property owned by citizens of the Philippines not residing in that foreign country.

TAXATION OUTSIDE THE PHILIPPINES

The tax treatment of non-resident LTNCD Holders in jurisdictions outside the Philippines may vary depending on the tax laws applicable to such Holder by reason of domicile or business activities and such Holder's particular situation. This Preliminary Offering Circular does not discuss the tax considerations on such non-resident Holders under laws other than those of the Philippines.

THE PHILIPPINE BANKING INDUSTRY

The banking industry in the Philippines is composed of universal banks, commercial banks, thrift banks, savings and mortgage banks, private development banks, stock savings and loan associations, rural banks and cooperative banks.

As of June 30, 2013, the universal and commercial banking sector consisted of 20 universal banks and 16 commercial banks. Of the 20 universal banks, 11 are private domestic banks, three (3) are government-owned, and six (6) are foreign bank branches. Of the 16 commercial banks, six (6) are private domestic banks, two (2) are subsidiaries of foreign banks, and eight (8) are branches of foreign banks.

Commercial banks are organized primarily to accept drafts and to issue letters of credit, discount and negotiate promissory notes, drafts, bills of exchange and other evidences of indebtedness, receive deposits, buy and sell foreign exchange and gold and silver bullion, and lend money on a secured or unsecured basis. Universal banks are banks that have authority, in addition to commercial banking powers, to exercise the powers of investment houses, invest in the equity of business not related to banking and own up to one hundred percent (100.0%) of the equity in a thrift bank, a rural bank or financial allied enterprise. A publicly-listed universal or commercial bank may own up to one hudred percent (100.0%) of the voting stock of only one other universal or commercial bank.

Thrift banks primarily accumulate the savings of depositors and invest them, together with their capital, in secured or unsecured loans, or in financing for home building and home development, in readily marketable debt notes, in commercial paper and accounts receivable, drafts, bills of exchange, acceptances or notes arising out of commercial transactions. Thrift banks also provide short-term working capital and medium- and long-term financing for businesses engaged in agriculture, services, industry, housing and other financial and allied services for its chosen market and constituencies, especially for SMEs and individuals. As of June 30, 2013, there were 70 thrift banks.

Rural and cooperative banks are organized primarily to make credit available and readily accessible in the rural areas on reasonable terms. Loans and advances extended by rural banks are primarily for the purpose of meeting the normal credit needs of farmers and fishermen, as well as the normal credit needs of cooperatives and merchants. Rural banks are privately owned and managed while cooperative banks are owned by cooperatives or federation of cooperatives. As of June 30, 2013, there were 577 rural and cooperative banks.

Specialized government banks are organized to serve a particular purpose. The existing specialized banks are the Development Bank of the Philippines (“DBP”), Land Bank of the Philippines (“LBP”), and Al-Amanah Islamic Investment Bank of the Philippines (“AAIIB”). DBP was organized primarily to provide banking services catering to the medium- and long-term needs of agricultural and industrial enterprises, particularly in rural areas and preferably for SMEs. LBP primarily provides financial support in all phases of the Philippines' agrarian reform program. In addition to their special functions, DBP and LBP are allowed to operate as universal banks. AAIIB was organized to promote and accelerate the socio-economic development of the Autonomous Region of Muslim Mindanao through banking, financing and investment operations and to establish and participate in agricultural, commercial and industrial ventures based on Islamic banking principles and rulings.

During the past decade, the Philippine banking industry has been marked by two major trends – liberalization and mergers and consolidation.

Foreign bank entry was liberalized in 1994, enabling foreign banks to invest in up to sixty percent (60.0%) of the voting stock of an existing bank or a new banking subsidiary, or to establish branches with full banking authority. This led to the establishment of ten (10) new foreign bank branches in 1995. The General Banking Law further liberalized the industry by providing that the Monetary Board may authorize foreign banks to acquire up to one hundred percent (100.0%) of the voting stock of one domestic bank. Under the General Banking Law, any foreign bank, which prior to the effectiveness of the said law availed itself of the privilege to acquire up to sixty percent (60.0%) of the voting stock of a domestic bank, may further acquire voting shares of such bank to the extent necessary for it to own one hundred percent (100.0%) thereof. As of June 30, 2013, there were 14 foreign banks with branches and two (2) foreign banks with subsidiaries in the Philippines.

The BSP has also been encouraging mergers and consolidations in the banking industry, seeing this as a means to create stronger and more globally competitive banking institutions. To encourage this trend, the BSP offered various incentives to merging or consolidating banks. Based on BSP data, since the new package of incentives took effect in September 1998, there have been at least 35 mergers, acquisitions, and consolidations of banks. However, while recent mergers increased market concentrations, BSP studies showed that they were not enough to pose a threat to the overall competition levels since market share remained relatively well dispersed among the remaining players.

Competition

The Bank faces competition from both domestic and foreign banks, in part as a result of the liberalization of the banking industry by the National Government. Since 1994, a number of foreign banks, which have greater financial resources than the Bank, have been granted licenses to operate in the Philippines. Such foreign banks have generally focused their operations on the larger corporations and selected consumer finance products, such as credit cards. The foreign banks have not only increased competition in the corporate market, but have as a result caused more domestic banks to focus on the commercial middle-market, placing pressure on margins in both markets.

As of June 30, 2013, based on published statement of condition, the Bank ranks seventh in terms of total assets among the leading domestic commercial banks in the Philippines. The following table sets out a comparison, based on published statements of condition, of the Bank along with the three (3) leading private domestic Philippine banks as of June 30, 2013. The Bank's data is presented on consolidated basis.

(₱ Billions)	**As of June 30, 2013**			
Consolidated	**Total Assets**	**Total Capital**	**Total Loans & Receivables**	**Total Deposits**
BDO Unibank, Inc.	1,330.5	159.8	803.8	1,015.5
Metropolitan Bank and Trust Co.	1,222.0	143.1	545.8	876.6
Bank of the Philippine Islands	1,008.1	97.2	563.9	824.5
Union Bank of the Philippines	340.6	45.0	99.8	259.5

Source: 17-A Disclosures with the Bangko Sentral ng Pilipinas

BANKING REGULATION AND SUPERVISION

Banking Regulation and Supervision

The New Central Bank Act (Republic Act No. 7653) ("New Central Bank Act") and the General Banking Law vest the BSP, through the Monetary Board with the power to regulate and supervise financial intermediaries in the Philippines. Financial intermediaries include banks or banking institutions such as universal banks, commercial banks, thrift banks (composed of savings and mortgage banks, private development banks, and stock savings and loan associations), rural banks, cooperative banks as well as branches and agencies of foreign banks in the Philippines. Entities performing quasi-banking functions, trust companies, non-stock savings and loan associations and certain other non-deposit accepting entities, while not considered banking institutions, are also subject to regulation by the Monetary Board.

The BSP's MORB is the principal source of rules and regulations to be complied with and observed by banks in the Philippines. The MORB contains regulations that include those relating to the organization, management and administration, deposit and borrowing operations, loans, investments and special financing program, and trust and other fiduciary functions, of the relevant bank. Supplementing the MORB are rules and regulations promulgated in various circulars, memoranda, letters and other directives issued by the Monetary Board.

The Supervision and Examination Sector of the BSP is responsible for ensuring the observance of applicable laws and rules and regulations by banking institutions operating in the Philippines (including Government credit institutions, their subsidiaries and affiliates, non-bank financial intermediaries, and subsidiaries and affiliates of non-bank financial intermediaries performing quasi-banking functions).

Permitted Activities

A universal bank, in addition to the general powers incidental to corporations, has the authority to exercise (i) the powers of a commercial bank, (ii) the powers of an investment house and (iii) the power to invest in non-allied enterprises. A publicly listed universal or commercial bank may own up to one hundred percent (100.0%) of the voting stock of only one other universal or commercial bank. A universal bank may also own up to one hundred percent (100.0%) of the equity in a thrift bank, rural bank, a financial allied enterprise, or anon-financial allied enterprise.

Universal banks may perform the functions of an investment house either directly, or indirectly through a subsidiary investment house. In either case, the underwriting of equity securities and securities dealing shall be subject to pertinent laws as well as rules and regulations of the Philippine SEC. Should the investment house functions be performed directly by the bank, they shall be undertaken by a separate and distinct department or similar unit in the bank. A universal bank cannot perform the functions both directly and indirectly through a subsidiary.

In addition to those functions specifically authorized by the General Banking Law and the MORB, universal and commercial banking institutions in general, save for those other types of banks with prior Monetary Board approval, are allowed to (i) receive in custody funds, documents and valuable objects, (ii) rent out safety deposit boxes, (iii) act as financial agents and buy and sell, by order of and for the account of their customers, shares, evidences of indebtedness and all types of securities and (iv) make collections and payments for the account of others and perform such other services for their customers as are not incompatible with banking business, and upon prior approval of the Monetary Board, act as managing agent, adviser, consultant, or administrator of investment management, advisory, or consultancy accounts. Commercial and universal banks are allowed to a certain extent to invest in allied (both financial and non-financial) enterprises, but only universal banks can invest in non-allied enterprises.

Financial allied undertakings include leasing companies, banks, investment houses, financial companies, credit card companies, and financial institutions catering to small- and medium-scale industries, including venture capital companies, companies engaged in stock brokerage, securities dealership and brokerage and companies engaged in foreign exchange dealership/brokerage.

Except as the Monetary Board may otherwise prescribe, the total equity investments of a universal bank in all enterprises, whether allied or non-allied, shall not exceed fifty percent (50.0%) of the net worth of the investing bank. Its equity investment in any single enterprise, whether allied or non-allied, on the other hand, shall not exceed twenty-five percent (25.0%) of the net worth of the investing bank.

"Net worth" is understood in this context to refer to the total of unimpaired paid-in capital, including paid-in surplus, retained earnings, and undivided profit, net of valuation reserves and other adjustments as may be required by the BSP. The acquisition of such equity or equities is subject to prior approval of the Monetary Board.

Regulations

The MORB and various BSP regulations impose the following restrictions on commercial, universal and thrift banks.

Minimum capitalization

Under the MORB and circulars and issuances that amend the MORB, universal banks are required to have capital accounts of at least ₱4.95 billion. Commercial banks are required to have capital accounts of at least ₱2.4 billion. Thrift banks with a head office in Metro Manila are required to have capital accounts of at least ₱1.0 billion. These minimum levels of capitalization may be changed by the Monetary Board from time to time. Currently, the BSP requires only minimum capital accounts of ₱4.95 billion for universal banks, ₱2.4 billion for commercial banks and ₱325.0 million for thrift banks with a head office in Metro Manila.

For the purposes of these requirements, the MORB provides that capital shall be unimpaired capital and surplus, combined capital accounts and net worth and shall refer to the combined total of the unimpaired paid-in capital, surplus and undivided profits, net of: (a) such unbooked valuation reserves and other capital adjustments as may be required by the BSP, (b) total outstanding unsecured credit accommodations, both direct and indirect, to DOSRI, (c) deferred income tax, (d) appraisal increment reserve (revaluation reserve) as a result of appreciation or increase in the book value of bank assets, (e) equity investment of a bank in another bank or enterprise (foreign or domestic) if the other bank or enterprise has a reciprocal equity investment in the investing bank, although if such bank or enterprise has reciprocal equity investment in the investing bank, the lower figure of the investment of the bank or the reciprocal investment of the other bank or enterprise should be used; and (f) in the case of rural banks, the Government counterpart equity, except those arising from conversion of arrears under the Rehabilitation Program.

Capital Adequacy Requirements

In July 2001, the Philippines adopted the risk based capital adequacy framework of the Basel Committee on Banking Supervision or Basel 1. The framework provides that the risk-based capital ratio of a bank, expressed as a percentage of qualifying capital to risk-weighted assets which initially covers credit risk, must not be less than ten percent (10.0%). The ratio is required to be maintained daily on both a solo basis (head office plus branches) and a consolidated basis (parent bank plus subsidiary financial allied undertakings, but excluding insurance companies). The qualifying capital refers to the sum of Tier 1 and Tier 2 or supplementary capital of the bank, less deductions of the value of certain assets. The risk-weighted assets, on the other hand, are determined by assigning risk weights to amounts of on-balance sheet assets and to credit equivalent amounts of off-balance sheet items (inclusive of derivative contracts), subject to the deduction of the following items: (a) general loan loss provision (in excess of the amount permitted to be included in Upper Tier 2 capital) and (b) unbooked valuation reserves and other capital adjustments affecting asset accounts based on the latest report of examination as approved by the Monetary Board. Any asset deducted in computing for the qualifying capital must not be included in the risk-weighted assets in computing the denominator of the ratio. The risk-weighted amount shall be the product of the book value of assets multiplied by the risk weight associated with that asset.

Under BSP Circular No. 360, effective July 2003, the capital-to-risk assets ratio is to be inclusive of a market risk charge. In August 2006, the BSP issued Circular No. 538 which contains the implementing guidelines for the revised risk-based capital adequacy framework to conform to Basel II recommendations. Under the revised framework, capital requirements for operational risk, credit derivatives and securitization exposures are to be included in the calculation of the Bank's capital adequacy. The revised framework also prescribes a more granular mapping of external credit ratings to the capital requirements and recognizes more type of financial collateral and guarantees as credit risk mitigants. Changes in the credit risk weights of various assets, such as foreign currency denominated exposures to the Philippine national government, non-performing exposures and ROPA, were also made. Exposures are required to be risk-weighted based on third party credit assessment of the individual exposure given by eligible external credit assessment institutions. Credit risk-weights range from zero percent (0.0%) to one hundred fifty percent (150.0%) depending on the type of exposure and/or credit assessment of the obligor. The new guidelines took effect on July 1, 2007.

In January 2011, BSP issued Circular No. 709 which amends the risk-based capital framework issued under Circular No. 538 particularly on the definition of qualifying capital by modifying the eligibility criteria for inclusion of capital instruments of Hybrid Tier 1 Capital and Tier 2 Capital in line with international standards. BSP Circular No. 768, issued September 2012, further amends the definition of qualifying capital to include the loss absorbency feature at the point of non-viability as one of the minimum conditions for the issuance of qualifying capital instruments, that is, it must have a provision that requires the instrument to be either written-off or converted into common equity upon the occurrence of a trigger event as determined by BSP.

In 2012, the BSP announced that Philippine universal and commercial banks were to be required to adopt the capital adequacy standards under the Basel Committee on Banking Supervision's Basel III global regulatory framework for more resilient banks and banking systems starting January 1, 2014. The Monetary Board decided to adopt the capital adequacy standards in full without recourse to a staggered implementation or a gradual phase-out of ineligible capital instruments, claiming that this approach recognizes the strong capital position of the banking industry while providing for a reasonable transition period.

In January 2013, the BSP issued Circular No. 781, prescribing the Basel III Implementing Guidelines on Minimum Capital Requirements. The new guidelines are meant to strengthen the composition of bank capital by increasing the level of core capital which is common equity. Only capital that is available to absorb losses at all times qualifies as regulatory capital. Essentially, the BSP retained the total capital ratio requirement at ten percent (10.0%), but introduced two new ratios from the Basel III agenda: Common Equity Tier 1 (CET1) at six percent (6.0%), and Tier 1 Capital at seven and a half percent (7.5%). It likewise mandated a capital conservation buffer of two and a half percent (2.5%) composed of CET1 capital on top of the minimum CET1 requirement.

The Basel III requirements are applicable only to universal and commercial banks and their subsidiary banks and quasi-banks, whereas stand-alone thrift banks, rural banks, and cooperative banks will continue to be under the Basel 1.5 framework implemented in January 2012. However, in issuing instruments which are intended to be counted as part of regulatory capital, all banks, regardless of classification, are required to comply with the new eligibility criteria.

Beginning January 2014, BSP will implement the amended guidelines on the revised risk-based capital adequacy framework particularly on the minimum capital and disclosure requirements for the Philippine banking system in accordance with the Basel III standards. The new guidelines require that the risk based capital to risk-weighted assets, shall not less than ten percent (10.0%) for the both solo and consolidated basis. Other minimum capital ratios that will be included are CET1 ratio and Tier 1 ratio of six percent (6.0%) and seven and a half percent (7.5%), respectively. A conservation buffer of two and a half percent (2.5%), comprised of CET 1 capital will also be imposed.

Reserve Requirements

Under the New Central Bank Act, the BSP requires banks to maintain cash reserves and liquid assets in proportion to deposits in prescribed ratios. If a bank fails to meet this reserve during a particular week on an average basis, it must pay a penalty to the BSP on the amount of any deficiency.

Commercial and universal banks (including the Bank) are required to maintain regular reserves of eighteen percent (18.0%) against peso demand, NOW accounts, savings and time deposits, negotiable CTDs, long-term non-negotiable tax exempt CTDs and deposit substitutes, and three percent (3.0%) against long-term negotiable CTDs.

In addition to the foregoing regular reserve requirements, universal and commercial banks are required to set up liquidity reserves against Trust and Other Fiduciary Activities (TOFA) equivalent to fifteen percent (15.0%).

Loan Limit to a Single Borrower

Under the General Banking Law and its implementing regulations, the total amount of loans, credit accommodations and guarantees that may be extended by a bank to any borrower shall at no time exceed twenty five percent (25.0%) of the net worth of such bank (or thirty percent (30.0%) of the net worth of the bank in the event that certain types and levels of security are provided). This ceiling may be adjusted by the Monetary Board from time to time. As of June 30, 2013, the applicable ceiling was twenty five percent (25.0%) (which could be increased by ten percent (10.0%) provided that additional liabilities are secured by trust receipts, shipping documents, warehouse receipts or other similar documents transferring or securing title covering readily marketable, non-perishable goods which must be fully covered by insurance, twenty five percent (25.0%) provided that the loans are for undertaking infrastructure and/or development projects under the Private Public Partnership program of the government (only allowed for a period of six (6) years from December 28, 2010), or fifteen percent (15.0%) provided that the loans are granted to finance oil importation of oil companies which are not affiliates of the lending bank engaged in energy and power generation (only allowed for a period of three (3) years from March 3, 2011 or until March 3, 2014)) of the net worth of the Bank.

Pursuant to the General Banking Law, the basis for determining compliance with the single borrower's limit is the total credit commitment of the bank to or on behalf of the borrower, which includes outstanding loans and other credit accommodations, deferred letters of credit less margin deposits, and guarantees. Except as specifically provided in the MORB, total credit commitment is determined on a credit risk-weighted basis consistent with existing regulations. Other credit accommodations refer to credit and specific market risk exposures of banks arising from accommodations other than loans such as receivables (sales contract receivables, accounts receivables and other receivables), and debt securities booked as investments. Among the items excluded from determining the loan limit are: (a) loans and other credit accommodations secured by obligations of the BSP or of the Government, (b) loans and other credit accommodations fully guaranteed by the Government as to payment of principal and interest, (c) loans and other credit accommodations secured by U.S. treasury notes and other securities issued by central governments and central banks of foreign countries with the highest credit quality given by any two (2) internationally accepted rating agencies, (d) loans and other credit accommodations to the extent covered by hold-out on or assignment of deposits maintained in the lending bank and held in the Philippines, (e) loans, credit accommodations and acceptances under letters of credit to the extent covered by margin deposits and (f) other loans or credit accommodations which the Monetary Board may from time to time specify as non-risk items.

Trust Regulation

The MORB contains the regulations governing the grant of authority to and the management, administration and conduct of trust, other fiduciary business and investment management activities of, trust corporations and financial institutions allowed by law to perform such operations. Trust corporations, banks and investment houses may engage in trust and other fiduciary business after complying with the requirements imposed by the MORB.

Foreign Currency Deposit System

Under the MORB as well as the BSP's Manual of Regulations on Foreign Exchange Transactions (MORFT), an FCDU is a unit of a local bank or of a local branch of a foreign bank authorized by the BSP to engage in foreign currency-denominated transactions pursuant to the provisions of Republic Act No. 6426, as amended. Commercial banks which meet the net worth or combined capital accounts and profitability requirements prescribed by the Monetary Board may be authorized to operate an expanded FCDU, and thrift banks with a net worth or combined capital accounts of at least ₱325.0 million if they are located in Metro Manila, and ₱52.0 million if they are located outside Metro Manila, may be authorized to operate FCDUs. In general, FCDUs of such banks may, in any acceptable foreign currency: (a) accept deposits and trust accounts from residents and non-residents,

(b) deposit with foreign banks abroad, offshore banking units ("OBUs") and other FCDUs, (c) invest in foreign currency-denominated debt instruments, (d) grant foreign currency loans as may be allowed by the BSP, (e) borrow from other FCDUs, from non-residents and OBUs, subject to existing rules on foreign borrowings (f) engage in foreign currency to foreign currency swaps with the BSP, OBUs and FCDUs, (g) engage, subject to compliance with applicable conditions, (h) engage in repurchase agreements involving foreign currency denominated government securities, (i) purchase foreign currency denominated government securities under resale agreements from other banks' FCDU, non-residential financial institutions and offshore banking units, and (j) issue Hybrid Tier 1 (HT1) capital instruments, and (k) engage in U.S. dollar denominated repurchase agreements with the BSP. In addition to the foregoing, FCDUs of commercial banks and universal banks may: (a) engage in foreign exchange trading and, with prior BSP approval, engage in financial futures and options trading, (b) on request/instruction from their foreign correspondent banks, and provided that the foreign correspondent banks deposit sufficient foreign exchange with the FCDU: (i) insure letters of credit for a non-resident importer in favor of a non-resident exporter, (c) engage in direct purchase of export bills of resident exporters subject to certain conditions, (ii) pay, accept, or negotiate drafts/bills of exchange drawn under the letter of credit and (iii) make payment to the order of the non-resident exporter, and (d) engage in securities lending activities subject to certain conditions, and (e) invest in foreign currency denominated structured products issued by banks and special purpose vehicles of high credit quality. FCDUs are required to maintain a hundred percent (100.0%) cover for their foreign currency liabilities, of which seventy percent (70.0%) should be denominated in the same currency of such liability. FCDUs of universal and commercial banks have the option to maintain, while thrift banks are required to maintain, foreign currency deposits with the BSP equivalent to fifteen percent (15.0%) of their foreign currency deposit liabilities as a form of foreign exchange cover.

Lending Policies: Secured and Unsecured Lending

Banks are generally required to ascertain the purpose of a proposed loan, and the proceeds of the loan are to be used for that purpose only. Under the General Banking Law, commercial and universal banks are generally prohibited from extending loans and other credit accommodations against real estate in an amount exceeding sixty percent (60.0%) of the appraised value of the real estate security and the insured improvements, except the following which shall be allowed a maximum value of seventy percent (70.0%) of the appraised value: (i) any loan not exceeding ₱3.5 million to finance the acquisition or improvement of residential units; and (ii) housing loans extended or guaranteed under the Government's "National Shelter Program". The MORB also provides that loans and other credit accommodations may be secured by personal properties depending on the nature of the property. Prior to lending on an unsecured basis, a bank must investigate the borrower's financial condition and ability to service the debt and must obtain certain documentation from the borrower, such as financial statements and tax returns. Any unsecured lending should be only for a time period essential for completion of the operation to be financed.

Priority Lending Requirements

In compliance with the Agri-Agra Reform Credit Act of 2009 (Republic Act No. 10000), BSP regulations currently provide that commercial and universal banks should set aside twenty five percent (25.0%) of loanable funds for loans to the agricultural sector in general, with ten percent (10.0%) of such funds being made available exclusively to agrarian reform beneficiaries. Loanable funds are defined to include the net increase in a bank's funds from the effectivity of the said Republic Act. However, a bank may temporarily meet all or a portion of its agrarian reform and agriculture lending requirements by investing in certain Government securities under certain conditions.

The MORB and BSP regulations also provide that for a period of ten (10) years from June 17, 2008 to June 16, 2018, banks are required to set aside at least eight percent (8.0%) for micro- and small-sized and at least two percent (2.0%) for medium-sized enterprises, of their total loan portfolio based on their balance sheet as of the previous quarter for lending to such enterprises. Investments in Government securities will not satisfy such obligation.

With the enactment of the Barangay Micro Business Enterprises ("BMBEs") Act, or Republic Act No. 9178, private banking and other financial institutions were encouraged to lend to BMBEs. Among the incentives of the law is that all loans granted to BMBEs shall be considered as part of alternative compliance to the rules on reservation of funds for the agricultural sector and SMEs.

Qualifications of Directors and Officers

Under the MORB, bank directors and officers must meet certain minimum qualifications. For instance, directors must be at least 25 years old, have a college degree or have at least five (5) years' business experience, while officers must be at least 21 years old, have a college degree, or have at least five (5) years' banking or trust experience.

Certain persons are disqualified from acting as bank directors, including:

(1) Persons who have been convicted by final judgment of a court for offenses involving dishonesty or breach of trust such as, but not limited to, estafa, embezzlement, extortion, forgery, malversation, swindling, theft, robbery, falsification, bribery, violation of B.P. Blg. 22, violation of Anti-Graft and Corrupt Practices Act and prohibited acts and transactions under Section 7 of Republic Act No. 6713 (Code of Conduct and Ethical Standards for Public Officials and Employees);

(2) Persons who have been convicted by final judgment of a court sentencing them to serve a maximum term of imprisonment of more than six (6) years;

(3) Persons who have been convicted by final judgment of the court for violation of banking laws, rules and regulations;

(4) Persons who have been judicially declared insolvent, spendthrift or incapacitated to contract;

(5) Directors, officers or employees of closed banks who were found to be culpable for such institution's closure as determined by the Monetary Board;

(6) Directors and officers of banks found by the Monetary Board as administratively liable for violation of banking laws, rules and regulations where a penalty of removal from office is imposed, and which finding of the Monetary Board has become final and executory; or

(7) Directors and officers of banks or any person found by the Monetary Board to be unfit for the position of directors or officers because they were found administratively liable by another government agency for violation of banking laws, rules and regulations or any

offense/violation involving dishonesty or breach of trust, and which finding of said government agency has become final and executory.

BSP Circular No. 809, issued August 23, 2013, mandates that at least twenty percent (20.0%) but not less than two (2) members of the Board of Directors shall be independent directors, and in the case of rural banks, at least one (1) independent director shall be elected to the board. For rural banks whose business model is deemed complex by the BSP, at least twenty percent (20.0%) but not less than two (2) members of the Board of Directors shall be independent directors. The circular also provides that non-Filipino citizens may become members of the Board of Directors of a bank to the extent of the foreign participation in the bank's equity, provided that majority of the directors are Philippine residents. The circular disqualifies appointive or elective officials, whether full time or part time, from being officers of a bank, except in cases where such service is incidental to financial assistance provided by the government or government-owned or -controlled corporations or in cases allowed by law.

Loans to DOSRI

Under the MORB, dealings of a bank with any of its DOSRI should be in the regular course of business and upon terms not less favorable to the bank than those offered to others. The total amount of individual outstanding loans, other credit accommodations and guarantees to DOSRI should not exceed an amount equivalent to their unencumbered deposits and book value of the DOSRI's paid-in capital investment in the bank. In the aggregate, outstanding loans, other credit accommodations and guarantees to DOSRI generally should not exceed one hundred percent (100.0%) of the bank's net worth or fifteen percent (15.0%) of the total loan portfolio of the bank, whichever is lower. In no case shall the total unsecured loans, other credit accommodations and guarantees to DOSRI exceed thirty percent (30.0%) of the aggregate ceiling or of the outstanding loans, other credit accommodations and guarantees, whichever is lower. For the purpose of determining compliance with the ceiling on unsecured loans, other credit accommodations and guarantees, banks shall be allowed to average their ceiling on unsecured loans, other credit guarantees and guarantees every week.

The credit card operations of banks shall not be subject to these regulations where the credit cardholders are the bank's directors, officers, stockholders and their related interests, subject to certain conditions.

Further, the MORB provides that total outstanding loans, other credit accommodations and guarantees to each of the bank's subsidiaries and affiliates shall not exceed ten percent (10.0%) of the net worth of the bank and the unsecured loans, other credit accommodations and guarantees to each of said subsidiaries and affiliates shall not exceed five percent (5.0%) of the bank's net worth. In the aggregate, outstanding loans, other credit accommodations and guarantees to all subsidiaries and affiliates shall not exceed twenty percent (20.0%) of the net worth of the bank. Loans, other credit accommodations and guarantees granted by a bank to its subsidiaries and affiliates engaged in energy and power generation consistent with the medium-term development plan of the National Government, shall be subject to a separate individual limit of twenty five percent (25.0%), with unsecured portions not exceeding twelve and a half percent (12.5%). These subsidiaries and affiliates should not be a related interest of any of the directors, officers and/or stockholders of the lending institution, except where such director, officer or stockholder sits in the board of directors or is appointed as an officer of such corporation as representative of the bank. However, loans, other credit accommodations and guarantees secured by assets considered as non-risk under existing BSP regulations as well as interbank call loans shall be excluded in determining compliance with these prescribed ceilings. On June 16, 2011, the BSP issued Circular No. 725, which included "Non-governmental organization (NGOs)/Foundations that are engaged in retail microfinance operations which are incorporated by any of the stockholders and/or directors and/or officers of related banks," under 'Related Interests'.

Valuation Reserves for Impairments Against Loans

As a general rule, banking regulations define past due accounts of a bank as referring to all accounts in a bank's loan portfolio, all receivable components of trading account securities, and other receivables that are not paid at maturity. In the case of loans or receivables payable in installments, banking regulations consider the total outstanding obligation past due in accordance with the following schedule:

Mode of payment	Minimum number of instalments in arrears
Monthly	3
Quarterly	1
Semester	1
Annually	1

However, when the total amount of arrears reaches twenty percent (20.0%) of the total outstanding balance of the loan or receivable, the total outstanding balance of the loan or receivable is considered past due notwithstanding the number of installments in arrears.

BSP regulations allow loans and advances to be written off as bad debts only if they have been past due for six months or more, and can be justified to be uncollectible. The board of directors of a bank has discretion as to the frequency of write-off, provided that these are made against provisions for impairment or against current operations. The prior approval of the Monetary Board is required to write off loans to the bank's directors, officers, stockholders and their related interests.

On January 26, 2003, the SPV Act came into force. The SPV Act provides the legal framework for the creation of private management companies that will acquire NPLs, real estate and other assets from financial institutions in order to encourage new lending to support economic growth. The Congress of the Philippines passed the SPV Act's implementing rules and regulations on March 19, 2003 and they came into force on April 12, 2003. Under the SPV Act, the original deadline for the creation of asset management companies entitled to tax breaks was September 19, 2004. On April 24, 2006, the Philippine President signed into law an amendment to the SPV Act extending the deadline for the creation of asset management companies entitled to tax breaks, which extension expired on July 14, 2008.

Guidelines on General Reserves

Under existing BSP regulations, a general provision for loan losses shall also be set up as follows: (i) five percent (5.0%) of the outstanding balance of unclassified restructured loans less the outstanding balance of restructured loans which are considered non-risk under existing laws and regulations, provided that for certain borrowers adversely affected by recent super typhoons, and whose loans were restructured or rescheduled under the debt relief program for them not later than December 31, 2011, they shall be treated as regular loans and subject to the general loan loss provision of one percent (1.0%); and (ii) one percent (1.0%) of the outstanding balance of unclassified loans other than restructured loans less loans which are considered non-risk under existing laws and regulations.

Restrictions on Branch Openings

Section 20 of the General Banking Law provides that universal and commercial banks may open branches within or outside the Philippines upon prior approval of the BSP. The same provision of law allows banks, with prior approval from the Monetary Board, to use any or all of their branches as outlets for the presentation and/or sale of financial products of their allied undertakings or investment house units. In line with this, the MORB, as amended by BSP Circular No. 728, issued June 23, 2011, provides, various minimum theoretical capital requirements for the establishment of branches of universal and commercial banks. Depending on the location of the branch, the minimum amount of theoretical capital ranges from ₱15.0 million for branches of universal/commercial banks to be located in the fourth to sixth class municipalities to ₱50.0 million for the branches to be located in Metro Manila, subject to corresponding increases implemented on a staggered basis over a three (3)-year period. A bank must first comply with this minimum theoretical capital requirement in order to be given authority to establish more branches.

Pursuant to BSP Circular No. 624, issued October 13, 2008, and BSP Circular No. 505, issued December 22, 2005, banks shall be allowed to establish branches in the Philippines, except in the cities of Makati, Mandaluyong, Manila, Paranaque, Pasay, Pasig, and Quezon, and the municipality of San Juan ("restricted areas") Metro Manila. BSP Circular No. 728, issued June 23, 2011, lifted the restriction on the establishment of branches in "restricted areas" under a two (2)-phased liberalization approach. Under phase 1, private domestically incorporated universal and thrift banks with a limited branch network in the "restricted areas" have been given until June 30, 2014 to apply for and establish branches in those areas. Under phase 2, all banks, except rural and cooperative banks, can apply for and establish branches in the "restricted areas" starting July 1, 2014. However, branches of microfinance-orientated banks, microfinance-orientated branches of regular banks and branches that will cater primarily to the credit needs of BMBEs duly registered under Republic Act No. 9178 may be established anywhere upon the fulfillment of certain conditions.

Anti-Money Laundering Law

The Anti-Money Laundering Act, or Republic Act No. 9160, was passed on September 29, 2001 and was later amended on March 23, 2003, under Republic Act No. 9194. It was further amended on February 15, 2013 by Republic Act No. 10365. Under the law's provisions, as amended, (i) certain financial intermediaries including banks, non-banks, offshore banking units, quasi-banks, trust entities, non-stock savings and loan associations, foreign exchange dealers, pawnshops, money changers, remittance and transfer companies, and all other institutions including their subsidiaries and affiliates supervised and/or regulated by the BSP, (ii) insurance companies and/or institutions regulated by the Insurance Commission and (iii) securities brokers, dealers, salesmen, associated persons of brokers and dealers, investment banks, mutual funds, foreign exchange corporations, and certain other entities regulated by the SEC, (iv) certain jewelry dealers, (v) certain company service providers such as those which provide, as a business, the service of acting as a formation agent of juridical persons, acting as a director or corporate secretary of a company, a partner of a partnership, or a similar position in relation to other juridical persons, and (vi) persons who provide management of certain services such as management of money, securities, assets, savings accounts, contributions for management of companies, etc. are required to submit a "covered" transaction report involving a single transaction in cash or other equivalent monetary instruments in excess of ₱500,000.00 within one (1) Banking Day.

These institutions are also required to submit a "suspicious" transaction report within ten (10) working days if there is a reasonable ground to believe that any amounts processed are the proceeds of money laundering activities.

BSP regulations also require all universal and commercial banks in the Philippines to have an electronic money laundering transaction monitoring system in place. Each system will be required to detect and bring to the relevant institution's attention all transactions and/or accounts that either qualify as "covered transactions" or "suspicious transactions".

These transactions are reported to the AMLC, which body is created under the law, within ten (10) Banking Days from the date of occurrence thereof. The Court of Appeals, upon application by the AMLC, has the authority to order any accounts which it suspects are being used for money laundering to be frozen.

Institutions that are subject to the Anti-Money Laundering Act are also required to establish and record the identities of their clients based on official documents. In addition, all records of transactions are required to be maintained and stored for five (5) years from the date of a transaction. Records of closed accounts must also be kept for five (5) years after their closure.

PROCEDURE

The following summary is qualified in its entirety by, and should be read in conjunction with, the more detailed information found elsewhere in this Preliminary Offering Circular, the Terms and Conditions included herein, and the related Agreements regarding the offer, maintenance, trade and settlement of the LTNCDs. Prospective LTNCD Holders should read this entire Preliminary Offering Circular, the Terms and Conditions, and the related Agreements fully and carefully. In case of any inconsistency between this summary and the more detailed information in this Preliminary Offering Circular, then the more detailed portions and/or Terms and Conditions, and/or the Agreements, as the case may be, shall at all times prevail.

Offering Procedures

Pursuant to the Market Maker Agreement, the Registry and Paying Agency Agreement, and the Arrangement Agreement (the "Agreements") entered into by the Bank with the relevant counterparties, and pursuant to an approval by the BSP dated August 15, 2013 and subject to the terms and conditions of the Master Certificate, as well as Section X233.9 of the MORB, BSP Circular No. 304 and BSP Circular No. 428, as may be amended from time to time, the LTNCDs are being issued by the Bank with (a) HSBC as Sole Lead Arranger, Selling Agent and Market Maker; (b) the Bank as Selling Agent; (c) Multinational Investment Bancorporation as Selling Agent and Market Maker; and (d) Deutsche Bank AG, Manila Branch through its Direct Securities Services Department as Registrar and Paying Agent.

The following is a summary of the procedures to be adopted among the parties and the prospective LTNCD Holders and is qualified in its entirety by, and should be read in conjunction with, the more detailed information found elsewhere in this Preliminary Offering Circular and the Agreements.

The Offer Period

During the relevant Offer Period, the Bank, through the Sole Lead Arranger and Selling Agents, shall solicit subscriptions to the LTNCDs from Eligible LTNCD Holders. Prospective LTNCD Holders may purchase the LTNCDs during the Offer Period by submitting fully and duly accomplished Applications to Purchase the LTNCDs (the "ATPs"), in quadruplicate, together with all the required attachments and the corresponding payments to the Selling Agents or the Limited Selling Agent, as the case may be, from whom such application was obtained no later than 3:00 p.m. of the last day of the Offer Period, or such other date as may be determined by the Bank and the Sole Lead Arranger. ATPs received after said date or time or without the required attachments will be rejected. Only ATPs which are accompanied by payments in cleared funds or covered by acceptable payment instructions and covering the entire application money shall be accepted by the Selling Agents. The Selling Agents shall receive such funds and shall hold it until the end of the Offer Period.

1) For Applicants who are individuals:

    a. A clear copy of at least one (1) valid photo-bearing identification document issued by an official authority in accordance with BSP Circular No. 608 (2008) as may be amended from time to time, and documents as may be required by the Registrar and/or Selling Agent concerned;

    b. Two (2) fully executed signature cards in the form attached to the ATP; and

c. For aliens residing in the Philippines or non-residents engaged in trade or business in the Philippines, consularized proof of tax domicile issued by the relevant tax authority of the Applicant.

2) For corporate and institutional Applicants:

a. SEC-certified or Corporate Secretary-certified true copy of the SEC Certificate of Registration, Articles of Incorporation and By-Laws or such other relevant and equivalent organizational or charter documents;

b. Original or Corporate Secretary-certified true copy of the duly notarized certificate confirming the resolution of the Board of Directors and/or committees or bodies authorizing the purchase of the LTNCDs and specifying the authorized signatories;

c. Two (2) fully executed signature cards duly authenticated by the Corporate Secretary with respect to corporate and institutional investors, in the form attached to the ATP;

d. If claiming tax-exempt status, the (i) certified true copy of the original tax exemption certificate, ruling or opinion issued by the BIR, certified true copy of the current and valid/revalidated tax exemption certificate, ruling or opinion issued by the BIR, (ii) original duly notarized undertaking, in the prescribed form, declaring and warranting its tax exempt status, undertaking to immediately notify the Issuer and the Registrar and Paying Agent of any suspension or revocation of its tax exempt status and agreeing to indemnify and hold the Issuer and the Registrar and Paying Agent free and harmless against any claims, actions, suits, and liabilities resulting from or incidental to the non-withholding of the required tax; and (iii) such other documentary requirements as may be required by the Issuer or Selling Agent, or Registrar and Paying Agent as proof of the Applicant's tax-exempt status; and

e. Such other documentary requirements as may be required by the Registrar as proof of the Applicant's tax-exempt status.

The Investor must also be compliant with the Foreign Account Tax Compliance Act (FATCA) and hereby truly and faithfully executes the ATP Rider for FATCA.

The Selling Agents, as the case may be, may require the submission of other documents for purposes of confirming matters in conformity with relevant regulations or policies.

Allocation and Issue of the LTNCDs

Applications to Purchase the LTNCDs shall be subject to the availability of the LTNCDs and acceptance by the Bank. The Sole Lead Arranger, in consultation with the Bank, reserve the right to accept, reject, scale down, or reallocate any Application.

In the event that payment supporting any Application is returned by the drawee bank for any reason whatsoever, the Application shall be automatically cancelled and any prior acceptance of the Application shall be deemed revoked. If any Application is rejected or accepted in part only, the application money or the appropriate portion thereof will be returned without interest by the relevant Selling Agent or the Limited Selling Agent, as the case may be. On the Issue Date, the Selling Agents or the Limited Selling Agent, as the case may be, shall, on behalf of the Bank, accept the relevant ATPs. The acceptance of the ATP shall *ipso facto* convert such ATP into a purchase agreement between the Bank and the relevant prospective LTNCD Holder.

Upon confirmation by the Bank of acceptance of the relevant Applications and the respective amount of LTNCDs, the Selling Agents or the Limited Selling Agent, as the case may be, shall issue copies of the relevant purchase advice (the "Purchase Advice") to successful prospective LTNCD Holders confirming the acceptances of their offers to purchase the LTNCDs and consequent ownership thereof and stating the pertinent details including the amount accepted, with copies furnished to the Registrar.

The Registrar shall rely solely on the Consolidated Sales Report transmitted by the Selling Agents or the Limited Selling Agent, as the case may be, in its preparation of the Registry Book and the issuance of the Registry Confirmation for each LTNCD Holder without any document deficiency as identified by the Registrar. The Registrar shall mail the Registry Confirmations directly to the LTNCD Holders via courier at their mailing addresses as indicated in their respective ATPs, in accordance with the terms of the Registry and Paying Agency Agreement.

Transactions in the Secondary Market

All secondary trading of the LTNCDs shall be coursed through a Market Maker, subject to the payment by the LTNCD Holder of fees to the Market Maker and payment of fees to the Registrar. Any transfer between investors of different tax status with respect to the Issue shall only be effective on an Interest Payment Date. No transfers will be effected during the period between the Record Date and an Interest Payment Date or Principal Payment Date, inclusive. Once the system of the Registrar can process the transfer of a Certificate that will result in a change in the taxability or non-taxability of the interest income due thereon in between Interest Payment Dates, then such transfers can be done at any time.

No person may require the transfer of any LTNCD to be registered by the Registrar in the Registry during the Closed Period. The Registrar shall recognize and treat only those LTNCD Holders registered as such in the Registry immediately prior to the start of the Closed Period as the owners of the corresponding LTNCDs for any relevant or allocation purpose.

The Registrar shall register any transfer of the LTNCDs upon receipt from the Market Makers of the following documents in form and substance acceptable to it:

- The Transfer Instruction Letter;
- The transferor LTNCD Holder's original copy of the Registry Confirmation;
- The transferor LTNCD Holder's original copy of the Purchase Advice;
- The relevant Purchase Advice of the transferee LTNCD Holder (with the information provided therein duly set forth in typewritten form);
- Proof of the qualified tax-exempt status of the transferee LTNCD Holder, if applicable, and the covering Affidavit of Undertaking;
- The original duly endorsed signature cards of the transferee LTNCD Holder and such other original or certified true copies of other documents submitted by the transferee LTNCD Holder in support of the transfer or assignment of the LTNCDs in its favor;
- The appropriate secretary's certificate attesting to the board resolutions authorizing the transfers and acceptances as well as designating the authorized signatories, together with

specimen signature cards duly signed by the parties, and duly authenticated by each party's corporate secretary; and

- Such other documents that may be required by the Registrar.

Transfers of the LTNCDs made in violation of the restrictions on transfer under the Terms and Conditions shall be null and void and shall not be registered by the Registrar.

Payment of Interest and Principal

The Paying Agent shall exert all efforts to pay or cause to be paid on behalf of the Bank by 2:00 p.m. via Real Time Gross Settlement (RTGS)/ Electronic Peso Clearing & Settlement (EPCS) System the amount necessary to discharge in full the total amounts due for payment under the LTNCDs, net of taxes and fees (if any) to the Bank, the Authorized Representative, or the settlement bank designated as such in the ATPs or Purchase Advice which shall credit such payment to the LTNCD Holder's account, as indicated in the ATPs or Purchase Advice, provided, the Bank remits the amount necessary to discharge in full the total amounts due for payment under the LTNCDs to the Paying Agent no later than 10:00 a.m. on any Payment Date.

Schedule of Registry Fees

The Registrar shall be entitled to charge the LTNCD Holders and/or their counterparties such fees as the Registrar shall prescribe in connection with the services that the Registrar shall perform. The Registry will charge the following fees to the LTNCD Holders:

Fees charged for primary market transactions:

- A maintenance fee (services necessary to perform registry function which shall be netted out of the interest payment) of 2.5 basis points per annum of the face value of the LTNCD Holders' total holdings, subject to a minimum of ₱500.00 per year.

Fees charged for secondary market transactions:

- ₱80.00 transfer fee (for both the transferor and transferee LTNCD Holders).
- ₱80.00 account opening fee for each new transferee investor.
- Handling fees may also be charged by the Market Maker.
- The transferee LTNCD Holder shall shoulder the account maintenance fee traditionally charged on each interest payment date.

Other Fees

- ₱80.00 will be charged for each statement requested outside of the quarterly statements of account released.
- Replacement Registry Confirmations may likewise be issued, subject to the fulfillment of certain terms and conditions, for ₱80.00.
- A fee of ₱80.00 for each bank certification.
- A fee of ₱80.00 for non-trade transactions.

In the event that the Registrar is prohibited by law or regulation to charge the LTNCD Holders and/or their counterparties such fees in connection with its services, the Bank and the Registrar shall agree on such other arrangements in order for the Registrar to be fully compensated for the services it performs pursuant to the Registry and Paying Agency Agreement executed between them.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

FINANCIAL STATEMENTS

UNION BANK OF THE PHILIPPINES AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
JUNE 30, 2013
(With Comparative Figures for December 31, 2012)
(Amounts in Thousands of Philippine Pesos)

	June 30, 2013 (Unaudited)	December 31, 2012 (Audited)
RESOURCES		
CASH AND OTHER CASH ITEMS	**P 3,836,220**	P 4,242,361
DUE FROM BANGKO SENTRAL NG PILIPINAS	**91,927,446**	27,450,311
DUE FROM OTHER BANKS	**2,919,257**	2,999,339
INTERBANK LOANS RECEIVABLE	**13,062,712**	5,503,496
TRADING AND INVESTMENT SECURITIES	**92,819,594**	88,955,753
LOANS AND OTHER RECEIVABLES - Net	**99,751,288**	119,716,589
BANK PREMISES, FURNITURE, FIXTURES AND EQUIPMENT - Net	**3,308,144**	3,105,790
ASSETS HELD FOR SALE - Net	**504,670**	397,459
INVESTMENT PROPERTIES	**12,047,262**	11,555,076
GOODWILL	**11,258,251**	7,886,898
OTHER RESOURCES - Net	**9,205,529**	7,931,914
TOTAL RESOURCES	**P 340,640,373**	P 279,744,986
LIABILITIES AND CAPITAL FUNDS		
DEPOSIT LIABILITIES	**259,546,092**	189,841,357
BILLS PAYABLE	**15,208,030**	18,541,267
NOTES PAYABLE	**3,750,000**	3,750,000
OTHER LIABILITIES	**17,102,609**	19,765,119
Total Liabilities	**295,606,731**	231,897,743
CAPITAL FUNDS		
Capital funds attributable to the Parent Company's stockholders		
Common stock	**6,414,224**	6,414,224
Additional paid-in capital	**5,819,861**	5,819,861
Surplus free	**37,602,249**	33,656,926
Surplus reserves	**149,596**	149,596
Net unrealized fair value gains (losses) on available-for-sale financial assets	**(4,964,665)**	1,806,636
Total capital funds attributable to the Parent Company's stockholders	**45,021,265**	47,847,243
Non-controlling interests	**12,377**	-
Total Capital Funds	**45,033,642**	47,847,243
TOTAL LIABILITIES AND CAPITAL FUNDS	**P 340,640,373**	P 279,744,986

UNION BANK OF THE PHILIPPINES AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE SIX MONTHS ENDED JUNE 30, 2013 AND 2012
(Amounts in Thousands of Philippine Pesos, Except Per Share Data)
(Unaudited)

	2013	2012
INTEREST INCOME ON		
Loans and other receivables	P 4,060,384	P 3,480,290
Trading and investment securities	1,811,607	2,081,399
Cash and cash equivalents	501,157	102,522
Interbank loans receivable	9,681	14,777
	6,382,829	5,678,988
INTEREST EXPENSE ON		
Deposit liabilities	1,973,367	1,838,274
Bills payable and other liabilities	346,122	171,513
	2,319,489	2,009,787
NET INTEREST INCOME	4,063,340	3,669,201
IMPAIRMENT LOSSES	369,626	260,148
NET INTEREST INCOME AFTER IMPAIRMENT LOSSES	3,693,714	3,409,053
OTHER INCOME	8,710,132	5,569,419
OTHER EXPENSES	(5,730,848)	(4,672,604)
PROFIT BEFORE TAX	6,672,998	4,305,868
TAX EXPENSE	481,243	238,610
NET PROFIT	P 6,191,755	P 4,067,258
Profit for the period attributable to the:		
Parent Company's stockholders	P 6,190,301	P 4,067,258
Non-controlling interests	1,454	-
	P 6,191,755	P 4,067,258
BASIC/DILUTED EARNINGS PER SHARE	P 19.31	P 12.68

UNION BANK OF THE PHILIPPINES AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE SIX MONTHS ENDED JUNE 30, 2013 AND 2012
(Amounts in Thousands of Philippine Pesos, Except Per Share Data)
(Unaudited)

	2013	2012
NET PROFIT FOR THE PERIOD	**P 6,191,755**	P 4,067,258
OTHER COMPREHENSIVE LOSS		
Net unrealized fair value losses on available-for-sale financial assets	**(6,771,301)**	(1,336,358)
Transfer of unrealized fair value losses to statements of income for the impairment of available-for-sale financial assets	**-**	(257,413)
Amortization of unrealized loss on reclassified investments	**-**	(52,982)
	(6,771,301)	(1,646,753)
TOTAL COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD	**(P 579,546)**	P 2,420,505

UNION BANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF CHANGES IN CAPITAL FUNDS
FOR THE SIX MONTHS ENDED JUNE 30, 2013 AND 2012
(Amounts in Thousands of Philippine Pesos)
(Unaudited)

	Common Stock	Additional Paid-in Capital	Surplus Free	Surplus Reserves	Net Unrealized Fair Value Gains (Losses) on Available-for-sale Financial Assets	Non- controlling Interests	Total Capital Funds
Balance at January 1, 2013	P 6,414,224	P 5,819,861	P 33,656,926	P 149,596	P 1,806,636	-	P 47,847,243
Cash dividends	-	-	(2,244,978)	-	-	-	(2,244,978)
Total comprehensive income (loss) for the period	-	-	6,190,301	-	(6,771,301)	1,454	(579,546)
Acquisition of new subsidiary with non-controlling interests	-	-	-	-	-	10,923	10,923
Balance at June 30, 2013	**P 6,414,224**	**P 5,819,861**	**P 37,602,249**	**P 149,596**	**(P 4,964,665)**	**P 12,377**	**P 45,033,642**
Balance at January 1, 2012	P 6,414,224	P 5,819,861	P 28,009,506	P 134,173	P 2,459,517	-	P 42,837,281
Cash dividends	-	-	(1,924,267)	-	-	-	(1,924,267)
Total comprehensive income (loss) for the period	-	-	4,067,258	-	(1,646,753)	-	2,420,505
Balance at June 30, 2012	P 6,414,224	P 5,819,861	P 30,152,497	P 134,173	P 812,764	-	P 43,333,519

See Notes to Interim Consolidated Financial Information.

UNION BANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2013 AND 2012
(Amounts in Thousands of Philippine Pesos)
(Unaudited)

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before tax	P 6,672,998	P 4,305,868
Adjustments for:		
Impairment losses	369,626	260,148
Dividend income	(344,279)	(224,208)
Depreciation and amortization	225,428	174,884
Loss (gain) on sale and exchange of properties	(181,094)	59,378
Operating profit before working capital changes	6,742,679	4,576,070
Decrease (increase) in financial assets at fair value through profit or loss	76,516	(540,948)
Decrease in loans and other receivables	19,597,169	17,141,951
Increase in assets held for sale	(107,211)	(55,218)
Decrease (increase) in investment properties	(311,092)	813,860
Increase in goodwill	(3,371,353)	-
Decrease (increase) in other resources	(1,285,341)	1,881,561
Increase (decrease) in deposit liabilities	69,704,735	(37,839,889)
Decrease in other liabilities	(2,874,189)	(421,832)
Cash generated from (used in) operations	88,171,913	(14,444,445)
Dividends received	342,785	330,603
Cash paid for income taxes	(269,564)	(261,570)
Net Cash From (Used in) Operating Activities	88,245,134	(14,375,412)
CASH FLOWS FROM INVESTING ACTIVITIES		
Net acquisitions of bank premises, furniture, fixtures and equipment	(384,347)	(285,151)
Increase in available-for-sale financial assets	(10,711,658)	(1,587,651)
Net Cash Used in Investing Activities	(11,096,005)	(1,872,802)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net availments (payments) of bills payable	(3,333,237)	7,635,557
Dividends paid	(2,244,978)	(1,924,267)
Net Cash From (Used in) Financing Activities	(5,578,215)	5,711,290
EFFECTS OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(20,786)	320,972
NET DECREASE IN CASH AND CASH EQUIVALENTS ***(Carried Forward)***	P 71,550,128	(P 10,215,952)

NET DECREASE IN CASH AND CASH EQUIVALENTS ***(Brought Forward)***	**P 71,550,128**	(P 10,215,952)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD		
Cash and other cash items	**4,242,361**	3,686,931
Due from Bangko Sentral ng Pilipinas	**27,450,311**	28,771,881
Due from other banks	**2,999,339**	3,213,740
Interbank loans receivable	**5,503,496**	12,989,144
	40,195,507	48,661,696
CASH AND CASH EQUIVALENTS AT END OF PERIOD		
Cash and other cash items	**3,836,220**	3,217,182
Due from Bangko Sentral ng Pilipinas	**91,927,446**	28,670,394
Due from other banks	**2,919,257**	3,765,777
Interbank loans receivable	**13,062,712**	2,792,391
	P 111,745,635	P 38,445,744

Punongbayan & Araullo

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Report of Independent Auditors

19th and 20th Floors, Tower 1
The Enterprise Center
6766 Ayala Avenue
1200 Makati City
Philippines

T +63 2 886 5511
F +63 2 886 5506
www.punongbayan-araullo.com

The Board of Directors and Stockholders
UnionBank of the Philippines
UnionBank Plaza, Meralco Avenue
Corner Onyx Street and Sapphire Road
Ortigas Center, Pasig City

Report on the Financial Statements

We have audited the accompanying financial statements of UnionBank of the Philippines and subsidiaries (the Group) and of UnionBank of the Philippines (the Parent Company), which comprise the statements of financial position of the Group as at December 31, 2012, 2011 and 2010, and of the Parent Company as at December 31, 2012 and 2011, and the statements of income, statements of comprehensive income, statements of changes in capital funds and statements of cash flows for each of the three years in the period ended December 31, 2012, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the financial reporting standards in the Philippines for banks as described in Note 2 to the financial statements, 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Philippine Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of UnionBank of the Philippines and subsidiaries as at December 31, 2012, 2011 and 2010, and of UnionBank of the Philippines as at December 31, 2012 and 2011, and their financial performance and their cash flows for each of the three years in the period ended December 31, 2012, in accordance with the financial reporting standards in the Philippines for banks as described in Note 2 to the financial statements.

Report on Other Legal and Regulatory Requirements

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information for the year ended December 31, 2012 required by the Bureau of Internal Revenue as disclosed in Note 35 to the financial statements is presented for purposes of additional analysis and is not a required part of the basic financial statements prepared in accordance with the financial reporting standards in the Philippines for banks. Such supplementary information is the responsibility of management. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

PUNONGBAYAN & ARAULLO

By: Leonardo D. Cuaresma, Jr.
Partner

CPA Reg. No. 0058647
TIN 109-227-862
PTR No. 3671448, January 2, 2013, Makati City
SEC Group A Accreditation
Partner - No. 0007-AR-3 (until Jan. 18, 2015)
Firm - No. 0002-FR-3 (until Jan. 18, 2015)
BIR AN 08-002511-7-2011 (until Sept. 21, 2014)
Firm's BOA/PRC Cert. of Reg. No. 0002 (until Dec. 31, 2015)

March 22, 2013

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2012, 2011 AND 2010
(Amounts in Thousands of Philippine Pesos)

		GROUP			PARENT	
	Notes	2012	2011 (As Restated - See Note 2)	2010 (As Restated - See Note 2)	2012	2011
RESOURCES						
CASH AND OTHER CASH ITEMS	7	P 4,242,361	P 3,686,931	P 4,177,961	P 4,242,324	P 3,686,914
DUE FROM BANGKO SENTRAL NG PILIPINAS	7	27,450,311	28,771,881	42,524,011	27,450,311	28,771,881
DUE FROM OTHER BANKS	8	2,999,339	3,213,740	1,760,146	2,999,198	3,213,599
INTERBANK LOANS RECEIVABLE	9	5,503,496	12,989,144	7,470,463	5,503,496	12,989,144
TRADING AND INVESTMENT SECURITIES						
At fair value through profit or loss	10	397,477	270,870	5,997,330	397,128	270,115
Available-for-sale financial assets - net	11	88,558,276	89,743,516	33,812,760	88,523,808	89,714,285
Held-to-maturity investments - net	12	-	-	35,665,162	-	-
LOANS AND OTHER RECEIVABLES - Net	13	119,716,589	105,011,206	95,031,665	119,639,210	104,931,023
INVESTMENTS IN SUBSIDIARIES	14	-	-	-	636,486	636,486
BANK PREMISES, FURNITURE, FIXTURES AND EQUIPMENT - Net	15	3,105,790	2,769,566	2,862,610	3,104,437	2,767,764
ASSETS HELD FOR SALE - Net	17	397,459	198,085	137,455	397,459	198,085
INVESTMENT PROPERTIES	16	11,555,076	12,166,969	12,382,162	11,290,988	11,896,168
GOODWILL	2	7,886,898	7,886,898	7,886,898	7,886,898	7,886,898
OTHER RESOURCES - Net	18	7,931,914	5,920,135	4,074,697	4,034,516	3,462,863
TOTAL RESOURCES		P 279,744,986	P 272,628,941	P 253,783,320	P 276,106,259	P 270,425,225

Forward

	Notes	GROUP 2012	GROUP 2011 (As Restated - See Note 2)	GROUP 2010 (As Restated - See Note 2)	PARENT 2012	PARENT 2011
LIABILITIES AND CAPITAL FUNDS						
DEPOSIT LIABILITIES	20					
Demand		P 62,811,727	P 114,752,297	P 109,468,172	P 62,881,671	P 114,868,781
Savings		23,868,712	22,521,897	25,208,414	23,978,728	22,521,906
Time		103,160,918	69,379,150	58,642,943	103,160,918	69,379,150
Total Deposit Liabilities		189,841,357	206,653,344	193,319,529	190,021,317	206,769,837
BILLS PAYABLE	21	18,541,267	5,619,244	7,396,288	18,540,767	5,618,744
NOTES PAYABLE	22	3,750,000	3,750,000	5,037,100	3,750,000	3,750,000
OTHER LIABILITIES	23	19,765,119	13,767,314	12,045,053	16,406,159	11,699,242
Total Liabilities		231,897,743	229,789,902	217,797,970	228,718,243	227,837,823
CAPITAL FUNDS	24					
Common stock		6,414,224	6,414,224	6,414,224	6,414,224	6,414,224
Additional paid-in capital		5,819,861	5,819,861	5,819,861	5,819,861	5,819,861
Surplus free		33,656,926	28,011,264	23,033,433	33,217,786	27,688,954
Surplus reserves		149,596	134,173	120,162	149,596	134,173
Net unrealized fair value gains on available-for-sale financial assets		1,806,636	2,459,517	597,670	1,786,549	2,530,190
Total Capital Funds		47,847,243	42,839,039	35,985,350	47,388,016	42,587,402
TOTAL LIABILITIES AND CAPITAL FUNDS		P 279,744,986	P 272,628,941	P 253,783,320	P 276,106,259	P 270,425,225

See Notes to Financial Statements.

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(Amounts in Thousands of Philippine Pesos, Except Per Share Data)

		GROUP			PARENT		
	Notes	2012	2011	2010	2012	2011	2010
INTEREST INCOME ON							
Loans and other receivables	13	P 6,984,054	P 6,875,612	P 6,374,534	P 6,981,994	P 6,873,499	P 6,372,350
Trading and investment securities	10, 11, 12	3,745,205	4,011,124	4,362,174	3,745,205	4,011,124	4,362,174
Cash and cash equivalents	7, 8	113,765	831,583	1,023,010	112,660	831,582	1,027,305
Interbank loans receivable	9	24,843	32,113	53,336	24,843	32,113	53,336
		10,867,867	11,750,432	11,813,054	10,864,702	11,748,318	11,815,165
INTEREST EXPENSE ON							
Deposit liabilities	20	3,182,903	4,349,436	4,289,676	3,187,665	4,350,817	4,294,935
Bills payable and other liabilities	21, 22, 23	373,322	417,819	449,136	373,322	417,819	449,136
		3,556,225	4,767,255	4,738,812	3,560,987	4,768,636	4,744,071
NET INTEREST INCOME		7,311,642	6,983,177	7,074,242	7,303,715	6,979,682	7,071,094
IMPAIRMENT LOSSES	19	1,559,839	1,549,552	524,464	1,559,839	1,549,552	524,464
NET INTEREST INCOME AFTER IMPAIRMENT LOSSES		5,751,803	5,433,625	6,549,778	5,743,876	5,430,130	6,546,630
OTHER INCOME							
Trading gain - net	10, 11, 12, 13	6,472,823	5,401,470	2,851,911	6,472,823	5,401,470	2,851,911
Premium revenues	2	1,243,013	1,387,319	281,491	-	-	-
Service charges, fees and commissions	25	861,632	846,584	682,146	854,360	840,291	681,324
Miscellaneous	26	2,253,389	1,922,628	2,319,298	1,859,066	1,606,432	2,164,519
		10,830,857	9,558,001	6,134,846	9,186,249	7,848,193	5,697,754

Forward

	Notes	GROUP 2012	GROUP 2011	GROUP 2010	PARENT 2012	PARENT 2011	PARENT 2010
OTHER EXPENSES							
Salaries and employee benefits	27	**3,304,063**	2,958,592	2,451,746	**3,279,371**	2,941,835	2,437,504
Trust fund due	2	**1,168,864**	1,304,079	262,274	-	-	-
Taxes and licenses	16, 28, 35	**998,167**	830,275	796,092	**992,985**	823,664	791,992
Occupancy	33	**553,723**	545,506	509,566	**552,500**	545,531	510,087
Depreciation and amortization	15, 18	**351,487**	357,765	373,025	**350,893**	357,140	371,650
Miscellaneous	26	**2,292,964**	2,185,502	2,105,465	**1,960,561**	1,993,278	2,059,652
		8,669,268	8,181,719	6,498,168	**7,136,310**	6,661,448	6,170,885
PROFIT BEFORE TAX		**7,913,392**	6,809,907	6,186,456	**7,793,815**	6,616,875	6,073,499
TAX EXPENSE	28	**328,040**	214,509	833,205	**325,293**	211,381	830,154
NET PROFIT		**P 7,585,352**	P 6,595,398	P 5,353,251	**P 7,468,522**	P 6,405,494	P 5,243,345
BASIC/DILUTED EARNINGS PER SHARE	31	**P 11.83**	P 10.28	P 8.35	**P 11.64**	P 9.99	P 8.17

See Notes to Financial Statements.

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(Amounts in Thousands of Philippine Pesos)

	Note	GROUP 2012	GROUP 2011	GROUP 2010	PARENT 2012	PARENT 2011	PARENT 2010
NET PROFIT FOR THE YEAR		P **7,585,352**	P 6,595,398	P 5,353,251	P **7,468,522**	P 6,405,494	P 5,243,345
OTHER COMPREHENSIVE INCOME (LOSS)	11						
Net unrealized fair value gains (losses) on available-for-sale financial assets		(**652,881**)	1,842,575	752,037	(**743,641**)	1,845,084	763,734
Transfer of unrealized fair value losses to statements of income for the impairment of available-for-sale financial assets		-	15,151	-	-	15,151	-
Amortization of unrealized loss on reclassified investments		-	4,121	10,841	-	4,121	10,841
		(**652,881**)	1,861,847	762,878	(**743,641**)	1,864,356	774,575
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		P **6,932,471**	P 8,457,245	P 6,116,129	P **6,724,881**	P 8,269,850	P 6,017,920

See Notes to Financial Statements.

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF CHANGES IN CAPITAL FUNDS
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(Amounts in Thousands of Philippine Pesos)

GROUP

	Notes	Common Stock	Additional Paid-in Capital	Surplus Free	Surplus Reserves	Net Unrealized Fair Value Gains (Losses) on Available-for-sale Financial Assets	Total Capital Funds
Balance at January 1, 2012		P 6,414,224	P 5,819,861	P 28,011,264	P 134,173	P 2,459,517	P 42,839,039
Cash dividends	24	-	-	(1,924,267)	-	-	(1,924,267)
Total comprehensive income (loss) for the year		-	-	7,585,352	-	(652,881)	6,932,471
Appropriation for trust business	29	-	-	(15,423)	15,423	-	-
Balance at December 31, 2012		**P 6,414,224**	**P 5,819,861**	**P 33,656,926**	**P 149,596**	**P 1,806,636**	**P 47,847,243**
Balance at January 1, 2011		P 6,414,224	P 5,819,861	P 23,033,433	P 120,162	P 597,670	P 35,985,350
Cash dividends	24	-	-	(1,603,556)	-	-	(1,603,556)
Total comprehensive income for the year		-	-	6,595,398	-	1,861,847	8,457,245
Appropriation for trust business	29	-	-	(14,011)	14,011	-	-
Balance at December 31, 2011		P 6,414,224	P 5,819,861	P 28,011,264	P 134,173	P 2,459,517	P 42,839,039
Balance at January 1, 2010		P 6,414,224	P 5,819,861	P 19,101,825	P 109,648	(P 165,208)	P 31,280,350
Cash dividends	24	-	-	(1,411,129)	-	-	(1,411,129)
Total comprehensive income for the year		-	-	5,353,251	-	762,878	6,116,129
Appropriation for trust business	29	-	-	(10,514)	10,514	-	-
Balance at December 31, 2010		P 6,414,224	P 5,819,861	P 23,033,433	P 120,162	P 597,670	P 35,985,350

See Notes to Financial Statements.

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF CHANGES IN CAPITAL FUNDS
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(Amounts in Thousands of Philippine Pesos)

PARENT

	Notes	Common Stock	Additional Paid-in Capital	Surplus Free	Surplus Reserves	Net Unrealized Fair Value Gains (Losses) on Available-for-sale Financial Assets	Total Capital Funds
Balance at January 1, 2012		P 6,414,224	P 5,819,861	P 27,688,954	P 134,173	P 2,530,190	P 42,587,402
Cash dividends	24	-	-	(1,924,267)	-	-	(1,924,267)
Total comprehensive income (loss) for the year		-	-	7,468,522	-	(743,641)	6,724,881
Appropriation for trust business	29	-	-	(15,423)	15,423	-	-
Balance at December 31, 2012		**P 6,414,224**	**P 5,819,861**	**P 33,217,786**	**P 149,596**	**P 1,786,549**	**P 47,388,016**
Balance at January 1, 2011		P 6,414,224	P 5,819,861	P 22,901,027	P 120,162	P 665,834	P 35,921,108
Cash dividends	24	-	-	(1,603,556)	-	-	(1,603,556)
Total comprehensive income for the year		-	-	6,405,494	-	1,864,356	8,269,850
Appropriation for trust business	29	-	-	(14,011)	14,011	-	-
Balance at December 31, 2011		P 6,414,224	P 5,819,861	P 27,688,954	P 134,173	P 2,530,190	P 42,587,402
Balance at January 1, 2010		P 6,414,224	P 5,819,861	P 19,079,325	P 109,648	(P 108,741)	P 31,314,317
Cash dividends	24	-	-	(1,411,129)	-	-	(1,411,129)
Total comprehensive income for the year		-	-	5,243,345	-	774,575	6,017,920
Appropriation for trust business	29	-	-	(10,514)	10,514	-	-
Balance at December 31, 2010		P 6,414,224	P 5,819,861	P 22,901,027	P 120,162	P 665,834	P 35,921,108

See Notes to Financial Statements.

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(Amounts in Thousands of Philippine Pesos)

	Notes	GROUP 2012	GROUP 2011	GROUP 2010	PARENT 2012	PARENT 2011	PARENT 2010
CASH FLOWS FROM OPERATING ACTIVITIES							
Profit before tax		P 7,913,392	P 6,809,907	P 6,186,456	P 7,793,815	P 6,616,875	P 6,073,499
Adjustments for:							
Impairment losses	19	1,559,839	1,549,552	524,464	1,559,839	1,549,552	524,464
Dividend income	26	(522,880)	(496,662)	(463,388)	(520,737)	(491,792)	(458,842)
Fair value gains on investment properties	16, 26	(379,873)	(44,476)	(118,737)	(379,873)	(44,476)	(118,737)
Depreciation and amortization	15, 18	351,487	357,765	373,025	350,893	357,140	371,650
Gain on sale and exchange of properties	16, 26	(156,231)	(161,172)	(26,815)	(156,231)	(161,172)	(26,815)
Gain on disposal of held-to-maturity investments	12	-	(671,690)	-	-	(671,690)	-
Operating profit before working capital changes		8,765,734	7,343,224	6,475,005	8,647,706	7,154,437	6,365,219
Decrease (increase) in financial assets at fair value through profit or loss		(126,607)	5,726,460	(5,169,125)	(127,013)	5,726,495	(5,169,047)
Decrease (increase) in loans and other receivables		(15,212,558)	(11,196,236)	5,418,901	(15,222,075)	(11,171,277)	5,414,120
Increase in assets held for sale		(199,374)	(60,630)	(30,358)	(199,374)	(60,630)	(30,358)
Decrease (increase) in investment properties		(313,649)	(85,260)	104,610	(313,649)	(87,287)	97,897
Decrease (increase) in other resources		(2,197,331)	(1,467,761)	(169,668)	(383,993)	159,568	610,611
Increase (decrease) in deposit liabilities		(16,811,987)	13,333,815	(1,188,848)	(16,748,520)	13,189,888	(1,669,160)
Increase (decrease) in other liabilities		6,277,525	2,043,370	(723,063)	4,616,172	730,140	(900,973)
Cash generated from (used in) operations		(19,818,247)	15,636,982	4,717,454	(19,730,746)	15,641,334	4,718,309
Dividends received		509,204	441,544	394,006	507,061	436,674	389,460
Cash paid for income taxes	28	(607,760)	(623,915)	(592,208)	(607,760)	(623,656)	(591,678)
Net Cash From (Used in) Operating Activities		(19,916,803)	15,454,611	4,519,252	(19,831,445)	15,454,352	4,516,091
CASH FLOWS FROM INVESTING ACTIVITIES							
Acquisitions of bank premises, furniture, fixtures and equipment	15	(710,750)	(483,191)	(321,222)	(710,605)	(483,069)	(317,935)
Decrease (increase) in available-for-sale financial assets	11	532,359	(23,588,983)	(494,101)	446,836	(23,588,981)	(494,102)
Proceeds from sale of bank premises, furniture, fixtures and equipment		428,173	157,452	12	428,173	157,452	12
Net disposals (acquisitions) of held-to-maturity investments	12	-	5,490,261	(12,879,755)	-	5,490,261	(12,879,755)
Net maturities of held-to-maturity investments	12	-	-	1,000,075	-	-	1,000,075
Net Cash Used in Investing Activities		249,782	(18,424,461)	(12,694,991)	164,404	(18,424,337)	(12,691,705)
CASH FLOWS FROM FINANCING ACTIVITIES							
Net availments (payments) of bills payable	21	12,922,023	(1,777,044)	6,340,951	12,922,023	(1,776,911)	6,340,818
Dividends paid	24	(1,924,267)	(1,603,556)	(1,411,129)	(1,924,267)	(1,603,556)	(1,411,129)
Net payments of notes payable	22	-	(1,287,100)	-	-	(1,287,100)	-
Net Cash From (Used in) Financing Activities		10,997,756	(4,667,700)	4,929,822	10,997,756	(4,667,567)	4,929,689
EFFECTS OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS		203,076	366,665	1,097,943	203,076	366,665	1,097,943
NET DECREASE IN CASH AND CASH EQUIVALENTS *(Carried Forward)*		(P 8,466,189)	(P 7,270,885)	(P 2,147,974)	(P 8,466,209)	(P 7,270,887)	(P 2,147,982)

	Notes	GROUP 2012	GROUP 2011	GROUP 2010	PARENT 2012	PARENT 2011	PARENT 2010
NET DECREASE IN CASH AND CASH EQUIVALENTS *(Brought Forward)*		(P 8,466,189)	(P 7,270,885)	(P 2,147,974)	(P 8,466,209)	(P 7,270,887)	(P 2,147,982)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR							
Cash and other cash items	7	3,686,931	4,177,961	4,023,958	3,686,914	4,177,944	4,023,950
Due from Bangko Sentral ng Pilipinas	7	28,771,881	42,524,011	20,850,017	28,771,881	42,524,011	20,850,017
Due from other banks	8	3,213,740	1,760,146	2,730,786	3,213,599	1,760,007	2,730,646
Interbank loans receivable	9	12,989,144	7,470,463	30,475,794	12,989,144	7,470,463	30,475,794
		48,661,696	55,932,581	58,080,555	48,661,538	55,932,425	58,080,407
CASH AND CASH EQUIVALENTS AT END OF YEAR							
Cash and other cash items	7	4,242,361	3,686,931	4,177,961	4,242,324	3,686,914	4,177,944
Due from Bangko Sentral ng Pilipinas	7	27,450,311	28,771,881	42,524,011	27,450,311	28,771,881	42,524,011
Due from other banks	8	2,999,339	3,213,740	1,760,146	2,999,198	3,213,599	1,760,007
Interbank loans receivable	9	5,503,496	12,989,144	7,470,463	5,503,496	12,989,144	7,470,463
		P 40,195,507	P 48,661,696	P 55,932,581	P 40,195,329	P 48,661,538	P 55,932,425

Supplemental Information on Noncash Operating and Investing Activities

1. Additions to investment properties in settlement of loans and receivable amounted to P586,070 in 2012, P496,998 in 2011 and P384,165 in 2010 in the Group and Parent Company financial statements (see Note 16).

2. In 2011, the Bank disposed of more than an insignificant amount of its held-to-maturity investments amounting to P5,716,283. Consequently, the remaining held-to-maturity investments portfolio amounting to P30,479,926 were reclassified to available-for-sale financial assets (see Notes 11 and 12).

3. In December 2010, the Group participated in a bond exchange program by the Bureau of Treasury wherein certain investments designated at fair value through profit or loss, available-for-sale, and held-to-maturity with carrying amounts of P1,109,829, P278,987, and P1,479,429, respectively, were exchanged for new investments with longer terms and higher yield rates with fair values of P1,083,022, and P295,052, and P1,466,252, respectively. The investments previously designated as fair value through profit or loss and available-for-sale were exchanged for investments designated as available-for-sale while the investments previously classified as held-to-maturity were also exchanged for held-to-maturity investments (see Notes 10, 11, and 12). The investments under the bond exchange program were all substantially disposed of in 2011.

4. In 2012 and 2011, certain investment properties with carrying values of P422,658 and P228,362, respectively, were reclassified to Bank Premises, Furnitures, Fixtures and Equipment (see Note 16).

See Notes to Financial Statements.

(Amounts in Thousands of Philippine Pesos, Except Par Value, Per Share Data, Exchange Rates and as Indicated)

1. CORPORATE INFORMATION

1.1 Incorporation and Operations

UnionBank of the Philippines (the Bank, UnionBank or the Parent Company) was incorporated in the Philippines on August 16, 1968 and operates as a universal bank through its universal banking license acquired in July 1992.

The Bank provides expanded commercial banking products and services such as loans and deposits, cash management, retail banking, foreign exchange, capital markets, corporate and consumer finance, investment management and trust banking. As of December 31, 2012, the Bank has 186 branches and 206 on-site and 26 off-site automated teller machines (ATMs), located nationwide.

The Bank's common shares are listed in the Philippine Stock Exchange (PSE). The Bank is effectively 43.27% owned by Aboitiz Equity Ventures, Inc. (AEVI), a company incorporated and domiciled in the Philippines. AEVI is the holding and management company of the Aboitiz Group of Companies.

The Bank's subsidiaries (all incorporated in the Philippines), effective percentage of ownership and the nature of the subsidiaries' businesses follow:

Subsidiary	Effective Percentage of Ownership	Nature of Business
Union Properties, Inc. (UPI)	100%	Real estate administration
First Union Direct Corporation (FUDC)*	100%	Financial products marketing
First Union Plans, Inc. (FUPI)*	100%	Pre-need
UBP Insurance Brokers, Inc. (UBPIBI)	100%	Insurance brokerage
UBP Securities, Inc. (UBPSI)	100%	Securities brokerage
UnionBank Currency Brokers Corporation (UCBC)	100%	Foreign currency brokerage
UnionDataCorp (UDC)	100%	Data processing
Interventure Capital Corporation (IVCC)	60%	Venture capital

* *Wholly-owned subsidiaries of UPI.*

Other relevant information about the subsidiaries' nature of business and their status of operations are discussed in the sections that follow:

(a) UPI was incorporated and registered with the Securities and Exchange Commission (SEC) on December 23, 1993. It is presently engaged in the administration and management of the Parent Company's premises and other properties such as buildings, condominium units and other real estate, wholly or partially owned by the Group. Pursuant to the action of the Board of Directors (BOD) of UPI approving the amendment of its Articles of Incorporation on May 13, 2004, the primary purpose of UPI was changed from a real estate developer to a real estate administrator. The SEC approved such amendment on December 13, 2004. Through its wholly-owned subsidiaries, FUPI and FUDC, UPI is also engaged in the sale of pre-need plans and marketing of financial products.

(b) UBPIBI was organized to engage in the insurance brokerage business. It was incorporated and registered with the SEC on February 27, 1992. In 1995, the BOD of UBPIBI approved the cessation of its operations.

(c) UBPSI was incorporated and registered with the SEC on March 2, 1993. It was organized to engage in the business of buying, selling or dealing in stocks and other securities. In January 1995, as approved by UBPSI's stockholders and BOD, UBPSI sold its stock exchange seat in the PSE to an affiliate of the Parent Company. Accordingly, UBPSI ceased its stock brokerage activities and has settled and liquidated its customers' positions.

(d) UCBC was registered in the SEC on June 14, 1994. It was organized to engage in the foreign currency brokerage business. On March 23, 2001, the BOD of UCBC approved the cessation of its business operations effective on April 16, 2001. Since then, UCBC's activities were significantly limited to the settlement of its liabilities.

(e) UDC was registered with the SEC on September 8, 1998. It was organized to handle the centralized branch accounting services as well as the processing of credit card application forms of the Parent Company and the entire backroom operations of FUPI. On July 1, 2003, the BOD of UDC approved the cessation of its business operations effective on August 30, 2003. The services previously handled by UDC are presently under the Centralized Processing Service unit of the Parent Company.

(f) IVCC was incorporated and registered with the SEC on October 16, 1980. It was organized to develop, promote, aid and assist financially any small or medium scale enterprises and to purchase, receive, take or grant, hold, convey, sell, lease, pledge, mortgage and otherwise deal with such real and personal property, including securities and bonds of other corporations as the transaction of the lawful business of the corporation may reasonably and necessarily require, subject to the limitations prescribed by law and the constitution. IVCC has ceased operations since 1992.

The Parent Company is presently assessing the business prospects and environment as a basis in formulating future plans for UBPIBI, UBPSI, UCBC, UDC and IVCC. Accordingly, such dormant companies are maintained as shell companies. The total assets, liabilities and capital funds of these subsidiaries amounted to P5,590, P5,540 and P50, respectively, as of December 31, 2012, and P5,537, P4,836 and P701, respectively, as of December 31, 2011.

The Bank's registered address, which is also its principal place of business, is at UnionBank Plaza, Meralco Avenue corner Onyx Street and Sapphire Road, Ortigas Center, Pasig City. AEVI's registered address is located at Aboitiz Corporate Center, Gov. Manuel A. Cuenco Avenue, Cebu City.

1.2 Approval of Financial Statements

The consolidated financial statements of UnionBank of the Philippines and Subsidiaries (the Group) and the financial statements of UnionBank of the Philippines for the year ended December 31, 2012 (including the comparatives for the years ended December 31, 2011 and 2010) were authorized for issue by the Bank's BOD on March 22, 2013.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies that have been used in the preparation of these financial statements are summarized below. The policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of Preparation of Financial Statements

(a) Statement of Compliance with Financial Reporting Standards in the Philippines for Banks

The consolidated financial statements of the Group and the financial statements of the Bank have been prepared in accordance with Financial Reporting Standards in the Philippines (FRSP) for banks. FRSP for banks and Philippine Financial Reporting Standards (PFRS) are the same, except for the exemption from the tainting provision of Philippine Accounting Standard (PAS) 39, *Financial Instruments: Recognition and Measurement*, as allowed by Bangko Sentral ng Pilipinas (BSP) and the SEC.

The following reconciliations and explanatory information thereto describe the difference in the 2010 statement of financial position between FRSP for banks and PFRS had the Bank's held-to-maturity (HTM) portfolio became tainted. In 2012 and 2011, there is no difference between FRSP for banks and PFRS since the Bank only had transactions in 2010 in which the relief from the tainting provision under PAS 39 granted by the BSP and the SEC was applied (see also Note 12).

	Group	Parent
Capital funds under FRSP for banks	P 35,985,350	P 35,921,108
Adjustment on net unrealized fair value gain had the Bank's entire HTM portfolio been tainted	3,190,792	3,190,792
Capital funds under PFRS	P 39,176,142	P 39,111,900

Differences in the measurement of items in the statement of financial position as of December 31, 2010 are summarized below:

	FRSP for banks	**Difference**	**PFRS**
Group			
Changes in resources:			
Available-for-sale (AFS) financial assets	P 33,812,760	P 38,855,954	P 72,668,714
HTM investments	35,665,162	(35,665,162)	-
	P 69,477,922		P 72,668,714
Total adjustments to capital funds		P 3,190,792	
Parent Company			
Changes in resources:			
AFS financial assets	P 33,781,022	P 38,855,854	P 72,636,876
HTM investments	35,665,162	(35,665,162)	-
	P 69,446,184		P 72,636,876
Total adjustments to capital funds		P 3,190,692	

PFRS are adopted by the Financial Reporting Standards Council (FRSC) from the pronouncements issued by the International Accounting Standards Board (IASB).

The financial statements have been prepared using the measurement bases specified by PFRS for each type of resource, liability, income and expense. The measurement bases are more fully described in the accounting policies that follow.

(b) Presentation of Financial Statements

The financial statements are presented in accordance with PAS 1, *Presentation of Financial Statements*. The Group presents all items of income and expenses in two statements: a statement of income and a statement of comprehensive income.

Two comparative periods are presented for the statement of financial position when the Group applies an accounting policy retrospectively, makes a retrospective restatement of items in its financial statements, or reclassifies items in the financial statements. In 2012, the Group restated its 2011 and 2010 consolidated financial statements to appropriately recognize the trust fund assets of FUPI (see Note 18). Accordingly, two comparative periods are presented for the Group's statement of financial position. In this connection, the Group early adopted PAS 1 (Amendment) which no longer requires the related notes on the opening consolidated statement of financial position to be presented [see Note 2.2(c)].

The restatement has no effect on the financial statements of the Parent Company. Thus, two comparative periods were not presented for the Parent Company.

(c) Functional and Presentation Currency

These financial statements are presented in Philippine pesos, the Parent Company's functional and presentation currency, and all values represent absolute amounts except when otherwise indicated (see also Note 2.19).

Items included in the financial statements of the Group are measured using functional currency of the Parent Company, the currency of the primary economic environment in which the Group operates.

2.2 Adoption of New and Amended PFRS

(a) Effective in 2012 that are Relevant to the Group

In 2012, the Group adopted the following amendments to PFRS that are relevant to the Group and effective for financial statements for the annual period beginning on or after July 1, 2011 or January 1, 2012:

PFRS 7 (Amendment)	:	Financial Instruments: Disclosures – Transfers of Financial Assets
PAS 12 (Amendment)	:	Income Taxes – Deferred Taxes: Recovery of Underlying Assets

Discussed below are relevant information about these amended standards.

(i) PFRS 7 (Amendment), *Financial Instruments: Disclosures – Transfers of Financial Assets*. The amendment requires additional disclosures that will allow users of financial statements to understand the relationship between transferred financial assets that are not derecognized in their entirety and the associated liabilities; and, to evaluate the nature of, and risk associated with any continuing involvement of the reporting entity in financial assets that are derecognized in their entirety. The Group did not transfer any financial asset involving this type of arrangement; hence, the amendment did not result in any significant change in the Group's disclosures in its financial statements.

(ii) PAS 12 (Amendment), *Income Taxes – Deferred Taxes: Recovery of Underlying Assets*. The amendment provides an exception to the existing principle in PAS 12 that recovery of the carrying amount of investment property measured at fair value under PAS 40, *Investment Property*, will be or normally be through sale. The amendment introduces a rebuttable presumption that the measurement of a deferred tax liability or asset on an investment property measured at fair value should reflect the tax consequence of recovering the carrying amount entirely through sale. The presumption is rebutted for depreciable investment property (e.g., building) measured at fair value that is held with an objective to consume substantially the economic benefits embodied in the asset over time, rather than through sale. As a result of the amendment, Standing Interpretations Committee (SIC) 21 *Income Taxes – Recovery of Revalued Non-Depreciable Assets*, is accordingly withdrawn and is incorporated under PAS 12. The amendment has no significant impact on the Group's financial statements as the Group's investment properties which are measured at fair value are taxable with the same rate regardless of whether these assets will be sold or used in operations.

(b) Effective in 2012 that is not Relevant to the Group

PFRS 1, *First-time Adoption of PFRS*, was amended to provide relief for first-time adopters of PFRS from having to reconstruct transactions that occurred before the date of transition to PFRS and to provide guidance for entities emerging from severe hyperinflation either to resume presenting PFRS financial statements or to present PFRS financial statements for the first time. The amendment became effective for annual periods beginning on or after July 1, 2011 but is not relevant to the Group's financial statements.

(c) *Early Adoption of PAS 1 (Amendment)*

In the preparation of the 2012 financial statements, the Group adopted early the amendment made to PAS 1, issued by the FRSC as part of the Annual Improvements to PFRS 2009-2011 Cycle, which will be effective for the annual period beginning on or after January 1, 2013. The amendment clarifies that when an entity applies an accounting policy retrospectively or makes a retrospective restatement or reclassification of items in its financial statements that has a material effect on the information in the statement of financial position at the beginning of the preceding period (i.e., opening statement of financial position), it shall present a third statement of financial position as at the beginning of that preceding period. Other than disclosures of certain specified information as provided in Note 18, the related notes to the opening statement of financial position are no longer required to be presented.

(d) *Effective Subsequent to 2012 but not Adopted Early*

There are new PFRS and amendments, annual improvements and interpretations to existing standards that are effective for periods subsequent to 2012. Management has initially determined the following pronouncements, which the Group will apply in accordance with their transitional provisions, to be relevant to its financial statements:

(i) PAS 1 (Amendment), *Financial Statements Presentation – Presentation of Items of Other Comprehensive Income* (effective from July 1, 2012). The amendment requires an entity to group items presented in other comprehensive income into those that, in accordance with other PFRSs: (a) will not be reclassified subsequently to profit or loss; and (b) will be reclassified subsequently to profit or loss when specific conditions are met. The Group's management expects that this will not affect the presentation of items in other comprehensive income, since all of the Group's other comprehensive income, which include unrealized fair value gains and losses on AFS financial assets, can be reclassified to profit or loss when specified conditions are met.

(ii) PAS 19 (Revised), *Employee Benefits* (effective from January 1, 2013). The revision made a number of changes as part of the improvements throughout the standard. The main changes relate to defined benefit plans as follows:

- eliminates the corridor approach under the existing guidance of PAS 19 and requires an entity to recognize all actuarial gains and losses arising in the reporting period;

- streamlines the presentation of changes in plan assets and liabilities resulting in the disaggregation of changes into three main components of service costs, net interest on net defined benefit obligation or asset, and remeasurement; and,

- enhances disclosure requirements, including information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans.

Currently, the Group is using the corridor approach and its unrecognized actuarial loss as of December 31, 2012 amounted to P715,547 (see Note 27.2) which will be retrospectively recognized in 2013 as loss in other comprehensive income. If the information in the recent actuarial valuation will be used in 2013 to effect the retrospective application, the estimated impact to the consolidated total resources and consolidated total capital funds would be a decrease of P685,962 and P715,547, respectively, as of December 31, 2012 and P563,857 and P598,493, respectively, as of December 31, 2011, while to the consolidated net profit and consolidated other comprehensive income (loss) would be an increase (decrease) of P23,367 and P117,054 in 2012, and P23,314 and (P30,369) in 2011.

(iii) Consolidation Standards

The Group is currently reviewing the impact on its financial statements of the following consolidation standards which will be effective from January 1, 2013:

- PFRS 10, *Consolidated Financial Statements*. This standard builds on existing principles of consolidation by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements. The standard also provides additional guidance to assist in determining control where this is difficult to assess.

- PFRS 12, *Disclosure of Interest in Other Entities*. This standard integrates and makes consistent the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and unconsolidated structured entities. This also introduces new disclosure requirements about the risks to which an entity is exposed from its involvement with structured entities.

- PAS 27 (Amendment), *Separate Financial Statements*. This revised standard now covers the requirements pertaining solely to separate financial statements after the relevant discussions on control and consolidated financial statements have been transferred and included in PFRS 10. No new major changes relating to separate financial statements have been introduced as a result of the revision.

- PAS 28 (Amendment), *Investments in Associate and Joint Venture*. This revised standard includes the requirements for joint ventures, as well as associates, to be accounted for using equity method following the issuance of PFRS 11, *Joint Arrangement*.

Subsequent to the issuance of the foregoing consolidation standards, the IASB made some changes to the transitional provisions in International Financial Reporting Standard (IFRS) 10, IFRS 11 and IFRS 12, which were also adopted by the FRSC. The guidance confirms that an entity is not required to apply PFRS 10 retrospectively in certain circumstances and clarifies the requirements to present adjusted comparatives. The guidance also made changes to PFRS 10 and PFRS 12 which provide similar relief from the presentation or adjustment of comparative information for periods prior to the immediately preceding period. Further, it provides relief by removing the requirement to present comparatives for disclosures relating to unconsolidated structured entities for any period before the first annual period for which PFRS 12 is applied.

(iv) PFRS 7 (Amendment), *Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities* (effective from January 1, 2013). The amendment requires qualitative and quantitative disclosures relating to gross and net amounts of recognized financial instruments that are set-off in accordance with PAS 32, *Financial Instruments: Presentation.* The amendment also requires disclosure of information about recognized financial instruments subject to enforceable master netting arrangements or similar agreements, even if they are not set-off in the statement of financial position, including those which do not meet some or all of the offsetting criteria under PAS 32, and amounts related to a financial collateral. These disclosures will allow financial statement users to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with recognized financial assets and financial liabilities on the entity's financial position. The Group has initially assessed that the adoption of the amendment will not have a significant impact on its financial statements since there are no significant items of financial assets and liabilities that are offset.

(v) PFRS 13, *Fair Value Measurement* (effective from January 1, 2013). This standard aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across PFRS. The requirements do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards. Management is in the process of reviewing its valuation methodologies for conformity with the new requirements and has yet to assess the impact of the new standard on the Group's financial statements.

(vi) PAS 32 (Amendment), *Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities* (effective from January 1, 2014). The amendment provides guidance to address inconsistencies in applying the criteria for offsetting financial assets and financial liabilities. It clarifies that a right of set-off is required to be legally enforceable, in the normal course of business, in the event of default and in the event of insolvency or bankruptcy of the entity and all of the counterparties. The amendment also clarifies the principle behind net settlement and includes an example of a gross settlement system with characteristics that would satisfy the criterion for net settlement. The Group does not expect this amendment to have a significant impact on its financial statements.

(vii) PFRS 9, *Financial Instruments: Classification and Measurement* (effective from January 1, 2015). This is the first part of a new standard on financial instruments that will replace PAS 39 in its entirety. This chapter covers the classification and measurement of financial assets and financial liabilities and it deals with two measurement categories for financial assets: amortized cost and fair value. All equity instruments will be measured at fair value while debt instruments will be measured at amortized cost only if the entity is holding it to collect contractual cash flows which represent payment of principal and interest. The accounting for embedded derivatives in host contracts that are financial assets is simplified by removing the requirement to consider whether or not they are closely related, and as such, the entity shall apply measurement to the entire hybrid contract, depending on whether the contract is at fair value or amortized cost.

For liabilities, the standard retains most of the PAS 39 requirements which include amortized cost accounting for most financial liabilities, with bifurcation of embedded derivatives. The main change is that, in case where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than in profit or loss, unless this creates an accounting mismatch.

To date, other chapters of PFRS 9 dealing with impairment methodology and hedge accounting are still being completed.

Further, in November 2011, the IASB tentatively decided to consider making limited modifications to IFRS 9's financial asset classification model to address certain application issues.

The Group does not expect to implement and adopt PFRS 9 until its effective date or until all chapters of this new standard have been published. In addition, management is currently assessing the impact of PFRS 9 on the financial statements of the Group and it plans to conduct a comprehensive study of the potential impact of this standard prior to its mandatory adoption date to assess the impact of all changes.

(viii) 2009-2011 Annual Improvements to PFRS. Annual improvements to PFRS (2009-2011 Cycle) made minor amendments to a number of PFRS, which are effective for annual period beginning on or after January 1, 2013. Among those improvements, the following amendments are relevant to the Group but management does not expect a material impact on the Group's financial statements:

(a) PAS 16 (Amendment), *Property, Plant and Equipment – Classification of Servicing Equipment*. The amendment addresses a perceived inconsistency in the classification requirements for servicing equipment which resulted in classifying servicing equipment as part of inventory when it is used for more than one period. It clarifies that items such as spare parts, stand-by equipment and servicing equipment shall be recognized as property, plant and equipment when they meet the definition of property, plant and equipment, otherwise, these are classified as inventory.

(b) PAS 32 (Amendment), *Financial Instruments – Presentation – Tax Effect of Distributions to Holders of Equity Instruments* was identified to be relevant to the Group's financial statements but management does not expect a material impact on the Group's financial statements. The amendment clarifies that the consequences of income tax relating to distributions to holders of an equity instrument and to transaction costs of an equity transaction shall be accounted for in accordance with PAS 12, *Income Taxes*. Accordingly, income tax relating to distributions to holders of an equity instrument is recognized in profit or loss while income tax related to the transaction costs of an equity transaction is recognized in equity.

2.3 Basis of Consolidated and Separate Financial Statements

The Group obtains and exercises control through voting rights. The Group's financial statements comprise the accounts of the Bank and its subsidiaries, as enumerated in Note 1.1 and as disclosed under Note 14, after the elimination of material intercompany transactions. All intercompany balances and transactions with subsidiaries, including income, expenses and dividends, are eliminated in full. Unrealized profits and losses from intercompany transactions that are recognized in the separate financial statements are also eliminated in full. Intercompany losses that indicate impairment are recognized in the Group's financial statements.

The financial statements of subsidiaries are prepared for the same reporting period as the Bank, using consistent accounting principles.

The Group's and Parent Company's investments in special purpose companies (SPCs), as described in Note 14, are recognized in the financial statements through the Investment Properties account instead of equity investments. Individually identifiable assets of these SPCs (land and building) acquired by the Group are classified as investment properties and not as investments in the shares of stocks of the SPCs. These properties therefore are measured at fair value (see Note 2.9).

In the Bank's separate financial statements, the investments in subsidiaries (see Note 14) are carried at cost, less any impairment in value.

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date the Bank obtains control until such time that such control ceases.

The acquisition method is applied to account for acquired subsidiaries. This requires recognizing and measuring the identifiable assets acquired, the liabilities assumed and any noncontrolling-interest in the acquiree. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred and the equity interests issued by the Group, if any. The consideration transferred also includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred and subsequent change in the fair value of contingent consideration is recognized directly in profit or loss.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognizes any noncontrolling- interest in the acquiree, either at fair value or at the noncontrolling-interest's proportionate share of the recognized amounts of acquiree's identifiable net assets.

The excess of the consideration transferred, the amount of any noncontrolling-interest in the acquiree and the acquisition-date fair value of any existing equity interest in the acquiree over the acquisition-date fair value of identifiable net assets acquired is recognized as goodwill. If the consideration transferred is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognized directly as gain in profit or loss (see Note 2.4).

2.4 Business Combinations

Business acquisitions are accounted for using the acquisition method of accounting.

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Subsequent to initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested annually for impairment and is carried at cost less accumulated losses.

Negative goodwill which is the excess of the Group's interest in the net fair value of net identifiable assets acquired over acquisition cost is charged directly to profit.

For the purpose of impairment testing, goodwill is allocated to cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose. The cash-generating units or groups of cash-generating units are identified according to operating segment.

Gains and losses on the disposal of an interest in a subsidiary include the carrying amount of goodwill relating to it.

If the business combination is achieved in stages, the acquirer is required to remeasure its previously held equity interest in the acquired at its acquisition-date fair value and recognize the resulting gain or loss, if any, in the profit or loss or other comprehensive income, as appropriate.

Any contingent consideration to be transferred by the Group is recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent that is deemed to be an asset or liability is recognized in accordance with PAS 37, *Provisions, Contingent Liabilities and Contingent Assets,* either in profit or loss or as a charge to other comprehensive income. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

2.5 Financial Assets

Financial assets are recognized when the Group becomes a party to the contractual terms of the financial instrument. Financial assets other than those designated and effective as hedging instruments are classified into the following categories: financial assets at fair value through profit or loss (FVTPL), loans and receivables, HTM investments and AFS financial assets. Financial assets are assigned to the different categories by management on initial recognition, depending on the purpose for which the investments were acquired.

Regular purchases and sales of financial assets are recognized on their settlement date. All financial assets that are not classified as at FVTPL are initially recognized at fair value, plus any directly attributable transaction costs. Financial assets carried at FVTPL are initially recorded at fair value and transaction costs related to it are recognized in profit or loss.

A more detailed description of the four categories of financial assets follow:

(a) Financial Assets at FVTPL

This category includes financial assets that are either classified as held for trading or that meets certain conditions and are designated by the Group to be carried at FVTPL upon initial recognition. All derivatives fall into this category, except for those designated and effective as hedging instruments.

Subsequent to initial recognition, the financial assets included in this category are measured at fair value with changes in fair value recognized in profit or loss. Financial assets (except derivatives and financial assets originally designated as financial assets at FVTPL) may be subsequently reclassified out of FVTPL category if they are no longer held for the purpose of being sold or repurchased in the near term, effective July 1, 2008:

(i) only in rare circumstances and if there is a change in intention (i.e., the financial asset is no longer held for the purpose of selling or repurchasing it in the near future); and

(ii) if the financial asset would have met the definition of loans receivables and if the financial asset had not been required to be classified as held-for-trading at initial recognition and the entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity.

(b) *Loans and Receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to the debtor with no intention of trading the receivables. Included in this category are those arising from direct loans to customers, interbank loans, sales contract receivables, and all receivables from customers and other banks.

Securities Purchased Under Reverse Repurchase Agreements (SPURRA) wherein the Group enters into short-term purchases of securities under reverse repurchase agreements of substantially identical securities with the BSP, are also included in this category. The difference between the sale and repurchase price is recognized as interest and accrued over the life of the agreements using the effective interest method.

Loans and receivables are subsequently measured at amortized cost using the effective interest method, less impairment losses, if any. Any change in their fair value is recognized in profit or loss, except for reclassified financial assets under PAS 39 and PFRS 7 (Amendments). Increases in estimates of future cash receipts from financial assets that have been reclassified in accordance with PAS 39 and PFRS 7 (Amendments) shall be recognized as an adjustment to the effective interest rate from the date of the change in estimate.

Impairment losses is the estimated amount of losses in the Group's loan portfolio, based on the evaluation of the estimated future cash flows discounted at the loan's original effective interest rates or the last repricing rate for loans issued at variable rates (see Note 2.20). It is established through an allowance account which is charged to expense. Loans and receivables are written off against the allowance for impairment when management believes that the collectibility of the principal is unlikely, subject to BSP regulations.

(c) *HTM Investments*

This category includes non-derivative financial assets with fixed or determinable payments and a fixed date of maturity that the Group has the positive intention and ability to hold to maturity. Investments intended to be held for an undefined period are not included in this classification.

HTM investments are subsequently measured at amortized cost using the effective interest method. In addition, if there is objective evidence that the investment has been impaired, the financial asset is measured at the present value of estimated cash flows (see Note 2.20). Any changes to the carrying amount of the investment due to impairment are recognized in profit or loss.

Should the Group sell other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS financial assets, except as may be allowed by the BSP and SEC. Moreover, the tainting provision will not apply if the sales or reclassifications of HTM investments are: (i) so close to maturity or the financial resources' call date that changes in the market rate of interest would not have a significant effect on its fair value; (ii) occur after the Group has collected substantially all of the financial assets' original principal through scheduled payments or prepayments; or, (iii) are attributable to an isolated event that is beyond the control of the Group, is non-recurring and could have not been reasonably anticipated by the Group.

In December 2010, the Group participated in a bond exchange program by the Bureau of Treasury wherein certain HTM investments were exchanged for HTM investments with longer terms and higher yield rates. The investments given up in the exchange constitute more than an insignificant portion of the total HTM portfolio before the exchange. Hence, for PFRS reporting, the entire HTM portfolio of the Bank would have been considered tainted. However, the BSP and the SEC granted relief from the tainting provision of PAS 39 to all participants in the exchange program (see Note 12).

(d) *AFS Financial Assets*

This category includes non-derivative financial assets that are either designated to this category or do not qualify for inclusion in any of the other categories of financial assets.

All financial assets within this category are subsequently measured at fair value, unless otherwise disclosed. Gains and losses from changes in fair value are recognized in other comprehensive income, net of any income tax effects, and are reported as part of the Net Unrealized Fair Value Gains (Losses) on AFS Financial Assets account in equity. When the financial asset is disposed of or is determined to be impaired, the cumulative fair value gains or losses recognized in other comprehensive income is reclassified from equity to profit or loss and is presented as reclassification adjustment within other comprehensive income.

Reversal of impairment losses are recognized in other comprehensive income, except for financial assets that are debt securities which are recognized in profit or loss only if the reversal can be objectively related to an event occurring after the impairment loss was recognized.

For investments that are actively traded in organized financial markets, fair value is determined by reference to exchange-quoted market bid prices at the close of business on the reporting period. For investments where there is no quoted market price, fair value is determined by reference to the current market value of another instrument which is substantially the same or is calculated based on the expected cash flows of the underlying net asset base of the investment.

A financial asset is considered as being traded in an active market if quoted prices or market values are readily and periodically available from stock or debt markets, exchanges, dealers, brokers, industry groups, pricing service entities or regulatory agencies. In such cases, those prices or values represent actual and regularly occurring market transactions on an arm's length basis. Otherwise, the market is regarded as being inactive. Indications that a market is inactive are when there are few recent transactions or when market participants have not engaged in transactions for at least one year.

Non-compounding interest, dividend income and other cash flows resulting from holding financial assets are recognized in profit or loss when earned, regardless of how the related carrying amount of financial assets is measured.

The financial assets are derecognized when the contractual rights to receive cash flows from the financial instruments expire or when all substantial risks and rewards of ownership have been transferred.

2.6 Derivative Financial Instruments

The Group is a counterparty to derivatives contracts, such as options, currency forwards and swaps, interest rate swap and futures contracts. These contracts are entered into as a means of reducing or managing the Group's foreign exchange and interest rate exposures as well as those of its customers.

Derivatives are initially recognized at fair value on the date on which the derivative contract is entered into and are subsequently measured at their fair values. Fair values are obtained from quoted market prices in active markets, including recent market transactions. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument. When such evidence exists, the Group recognizes a gain or loss at initial recognition.

For more complex instruments, the Group uses proprietary models, which usually are developed from recognized valuation models. Some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions. When entering into a transaction, the financial instrument is recognized initially at the transaction price, which is the best indicator of fair value, although the value obtained from the valuation model may differ from the transaction price. This initial difference in fair value indicated by valuation techniques is recognized in income depending upon the individual facts and circumstances of each transaction and not later than when the market data becomes observable.

The value produced by a model or other valuation technique is adjusted to allow for a number of factors as appropriate, because valuation techniques cannot appropriately reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments carried at fair value on the statement of financial position.

Certain derivatives embedded in other financial instruments, such as the call or put option in a bond and credit default swap in a credit linked note, are considered as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are bifurcated from the host contracts and are measured at fair value with changes in fair value recognized in profit or loss.

Changes in the fair value of derivatives are recognized in profit or loss.

2.7 Assets Held for Sale

Assets held for sale include real and other properties acquired (ROPA) through repossession or foreclosure that the Group intends to sell within one year from the date of classification as held for sale.

Assets classified as held for sale are measured at the lower of their carrying amounts, immediately prior to their classification as held for sale, and their fair value less costs to sell. Assets classified as held for sale are not subject to depreciation or amortization. The profit or loss arising from the sale of assets held for sale is included in the Other Income account in the statement of income.

2.8 Bank Premises, Furniture, Fixtures and Equipment

Bank premises, furniture, fixtures and equipment are carried at acquisition cost less accumulated depreciation and amortization, and any impairment in value.

The cost of an asset comprises its purchase price and directly attributable costs of bringing the asset to working condition for its intended use. Expenditures for additions, major improvements and renewals are capitalized; expenditures for repairs and maintenance are charged to expense as incurred.

Depreciation is computed on a straight-line basis over the estimated useful lives of the depreciable assets as follows:

Buildings	25 – 50 years
Furniture, fixtures and equipment	5 – 10 years

Leasehold rights and improvements are amortized over the term of the lease or the estimated useful lives of the improvements of five to ten years, whichever is shorter.

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 (see Note 2.21).

The residual values and estimated useful lives of bank premises, furniture, fixtures and equipment are reviewed, and adjusted if appropriate, at the end of each reporting period.

An item of bank premises, furniture, fixtures and equipment, including the related accumulated depreciation, amortization and impairment losses, 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.

2.9 Investment Properties

Investment properties are measured initially at acquisition cost which comprise its purchase price and directly attributable cost incurred. These include parcels of land and buildings and related improvements acquired by the Bank from defaulting borrowers not held for sale in the next 12 months. Subsequently, investment properties are stated at fair value, as determined by independent appraisal companies accredited by the BSP. The carrying amounts recognized in the statement of financial position reflect the prevailing market conditions at the reporting date.

Investment properties of the Group under construction or development, if the fair value of these properties cannot be reliably measured, are measured at cost until construction or development is complete. At completion, these properties are measured at fair value.

Any gain or loss resulting from either a change in the fair value or the sale of an investment property is immediately recognized in profit or loss as Fair value gains (losses) on investment properties under Other Income account in the statement of income.

Investment properties are derecognized upon disposal or when permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss on the retirement or disposal of an investment property is recognized in profit or loss in the year of retirement or disposal.

Direct operating expenses related to investment properties, such as repairs and maintenance, and real estate taxes are normally charged against current operations in the period in which these costs are incurred.

2.10 Intangible Assets

Goodwill represents the excess of the acquisition cost over the fair value of the former International Exchange Bank's (iBank) identifiable net assets on its merger with the Bank on April 30, 2006. Goodwill is classified as intangible asset with indefinite useful life, and thus, not subject to amortization but would require an annual test for impairment. Goodwill is subsequently carried at cost less accumulated impairment losses.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. Goodwill sometimes cannot be allocated on a non-arbitrary basis to individual cash-generating units, but only to groups of cash-generating units. As a result, the lowest level within the Parent Company at which goodwill is monitored for internal management purposes sometimes comprises a number of cash-generating units. The Group's cash-generating unit represents the branches and segments identified as coming from the former iBank.

Intangible assets include acquired computer software used in administration which is accounted for under the cost model. The cost of the asset is the amount of cash or cash equivalents paid or the fair value of the other considerations given up to acquire an asset at the time of its acquisition or production.

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and install the specific software. These costs are amortized on a straight-line basis over the expected useful lives of five to ten years. Costs associated with maintaining computer software are expensed as incurred. Intangible assets are subject to impairment testing as described in Note 2.21.

2.11 Prepayments and Other Resources

Prepayments and other resources pertain to other resources controlled by the Group as a result of past events. These are recognized in the financial statements when it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured reliably.

2.12 Financial Liabilities

Financial liabilities include deposit liabilities, bills payable, notes payable, and other liabilities (except tax-related payables and pre-need reserves).

Financial liabilities are recognized when the Group becomes a party to the contractual agreements of the instrument. All interest-related charges incurred on a financial liability are recognized as an expense in profit or loss.

Deposit liabilities are recorded or stated at amounts in which they are to be paid, which approximate fair value.

Bills payable and notes payable are recognized initially at fair value, which is the issue proceeds (fair value of consideration received), net of direct issue costs. Bills payable and notes payable are subsequently stated at amortized cost; any difference between the proceeds, net of transaction costs and the redemption value is recognized in profit or loss over the period of the borrowings using the effective interest method.

Derivative liabilities, which are included as part of Other Liabilities, are recognized initially and subsequently measured at fair value with changes in fair value recognized in profit or loss.

Other liabilities are recognized initially at their fair value and subsequently measured at amortized cost, using effective interest method for maturities beyond one year, less settlement payments.

Dividend distributions to shareholders are recognized as financial liabilities when the dividends are approved by the BSP.

Financial liabilities are derecognized in the statement of financial position only when the obligations are extinguished either through discharge, cancellation or expiration.

2.13 Offsetting Financial Instruments

Financial assets and liabilities are offset and the resulting net amount is reported in the statement of financial position 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.

2.14 Provisions and Contingencies

Provisions are recognized when present obligations will probably lead to an outflow of economic resources and they can be estimated reliably even if the timing or amount of the outflow may still be uncertain. A present obligation arises from the presence of a legal or constructive obligation that has resulted from past events.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the end of the reporting period, including the risks and uncertainties associated with the present obligation. Any reimbursement expected to be received in the course of settlement of the present obligation is recognized, if virtually certain as a separate asset, at an amount not exceeding the balance of the related provision. 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. In addition, long-term provisions are discounted to their present values using a pretax rate that reflects market assessment and the risks specific to the obligation, where time value of money is material. The increase in the provision due to passage of time is recognized as interest expense. Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimate.

In those cases where the possible outflow of economic resource as a result of present obligations is considered improbable or remote, or the amount to be provided for cannot be measured reliably, no liability is recognized in the financial statements. Similarly, possible inflows of economic benefits that do not yet meet the recognition criteria of an asset are considered contingent assets, hence, are not recognized in the financial statements. On the other hand, any reimbursement that the Group can be virtually certain to collect from a third party with respect to the obligation is recognized as a separate asset not exceeding the amount of the related provision.

2.15 Pre-Need Reserves and Insurance Premium Reserves

(a) Pre-need Reserves

In the Group consolidated financial statements, pre-need reserves (PNR), presented as part of Other Liabilities in the statements of financial position, are recognized for all pre-need benefits guaranteed and payable by FUPI as defined in the pre-need pension plan contracts.

PNR for pension plans are determined using the requirements on provisioning of PAS 37 and the specific method of computation required by the Insurance Commission (IC) as described below.

The amount recognized as a provision to cover the PNR is the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The risks and uncertainties that inevitably surround many events and circumstances were taken into account in reaching the best estimate of a provision.

PNR is computed based on the following considerations:

(i) On Currently-Being-Paid Plans

- Provision for termination values are computed based on the surrender rate experience.

- Provision for the portion of currently-being-paid plans that will reach full payment are computed based on full payment experience. It is equivalent to the present value of future maturity benefits reduced by the present value of future trust fund contributions required per product model discounted at the approved hurdle rate per product model of FUPI.

(ii) On Lapsed Plans within the Allowable Reinstatement Period

- Provision for termination values are computed based on reinstatement experience.

(iii) On Fully Paid Plans

- For plans due for payment within the next five years, the reserve is computed based on the present value of future maturity benefits discounted at the attainable rate, as determined and certified by FUPI's trustee using industry best practices and principles.

- For plans not yet due for payment within the next five years, the reserve is based on the present value of future maturity benefits discounted at the approved hurdle rate per product model.

(iv) Future events that may affect the foregoing amounts are reflected in the amount of the provision for PNR where there is sufficient objective evidence that they will occur.

(v) The rates of surrender, cancellation, reinstatement, utilization and inflation, when applied, represent the actual experience of FUPI in the last three years, or the industry, in the absence of a reliable experience.

(vi) The probability of pre-termination on surrender of fully paid plans, are considered in determining the PNR of fully paid plans. A pre-termination experience on fully paid plans of 5% and below are considered insignificant. In such cases, derecognition of liability shall be recorded at pre-termination date.

The computation of the foregoing assumptions is validated by the IC accredited actuary of FUPI.

Any excess in the amount of the trust fund as a result of the revised reserving requirement shall neither be released from the fund nor be credited/set off to future required contributions.

(b) *Insurance Premium Reserves*

Insurance premium reserves for life, pension and educational plans represents FUPI's actuarially-determined liability in accordance with PAS 37 to guarantee the benefits provided in the plan in consideration of the insurance premium funds assigned for this purpose as determined and certified by the IC accredited actuary.

2.16 Capital Funds

Common stock represents the nominal value of shares that have been issued.

Additional paid-in capital includes any premiums received on the issuance of common stock. Any transaction costs associated with the issuance of shares are deducted from additional paid-in capital, net of any related income tax benefits.

Surplus free includes all current and prior period results as reported in the statement of income and which are available and not restricted for use by the Group.

Surplus reserves pertains to a portion of the Group's income from trust operations set-up on a yearly basis in compliance with BSP regulations. The surplus set-up is equal to 10% of the net profit accruing from the trust business until the surplus shall amount to 20% of authorized capital stock. The reserve shall not be paid out as dividends, but losses accruing in the course of the trust business may be charged against this account.

Net unrealized fair value gains (losses) on AFS financial assets pertain to cumulative mark-to-market valuation of AFS financial assets.

2.17 Revenue and Cost Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Expenses are recognized in profit or loss upon utilization of the assets or services or at the date these are incurred. All finance costs are reported on an accrual basis. Specific recognition criteria of income and expenses described below must also be met before income or expense is recognized.

(a) *Interest* – Interest income and expenses are recognized in profit or loss for all instruments measured at amortized cost using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and points 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 impairment, interest income is recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(b) *Trading gain (loss)* – Trading gain (loss) is recognized when the ownership of the securities is transferred to the buyer (at an amount equal to the excess of the selling price over the carrying amount of securities) and as a result of the mark-to-market valuation of outstanding securities classified as FVTPL at year-end.

(c) *Premium revenues* – Premiums from sale of pre-need plans are recognized as earned when collected inclusive of advance premium payments. When premiums are recognized as income, the related cost of contracts is computed and recognized, with the result that the benefits and expenses are matched with such revenue.

(d) *Service charges, fees and commissions* – Service charges, fees and commissions are generally recognized when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognized as an adjustment to the effective interest rate on the loan. If the commitment expires without draw down by the Bank, the commitment fees are recognized as other income. Loan commitment fees earned as services are provided, are recognized as other income on a time proportion basis over the commitment period.

(e) *Miscellaneous* income includes the following accounts:

(i) *Gain (loss) from sale of assets* – Profit or loss from assets sold or exchanged is recognized when the risk and rewards to the assets is transferred to the buyer or when the collectibility of the entire sales price is reasonably assured.

(ii) *Dividend* – Dividend income is recognized when the Group's right to receive payment is established.

(iii) *Rental* – Rental income arising from leased properties is accounted for on a straight-line basis over the lease terms on ongoing leases.

(iv) *Commissions earned on credit cards* – Commissions earned on credit cards are taken up as income upon receipt from member establishments of charges arising from credit availments by credit cardholders. These commissions are computed based on certain agreed rates and are deducted from amounts remittable to member establishments. Purchases by the credit cardholders, collectible on installment basis, are recorded at the cost of the items purchased plus certain percentage of cost. Income is recognized on every term of installment billed to the cardholders and computed using the effective interest method.

2.18 Leases

The Group accounts for its leases as follows:

(a) *Group as Lessee*

Leases, which do not transfer to the Group substantially all the risks and benefits of ownership of the asset, are classified as operating leases. Operating lease payments are recognized as expense in profit or loss on a straight-line basis over the lease term. Associated costs, such as repairs, maintenance and insurance, are expensed as incurred.

(b) *Group as Lessor*

Leases which do not transfer to the lessee substantially all the risks and benefits of ownership of the asset are classified as operating leases. Lease income from operating leases is recognized as income in profit or loss on a straight-line basis over the lease term.

The Group determines whether an arrangement is, or contains a lease based on the substance of the arrangement. It makes an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

2.19 Foreign Currency Transactions and Translations

The accounting records of the Group are maintained in Philippine pesos except for the Foreign Currency Deposit Unit (FCDU) which are maintained in United States (US) dollars. Foreign currency transactions during the period are translated into the functional currency at exchange rates which approximate those prevailing on transaction dates.

For financial reporting purposes, the accounts of the FCDU are translated into their equivalents in Philippine pesos based on the Philippine Dealing System closing rates (PDSCR) prevailing at the end of the period (for resources and liabilities) and at the average PDSCR for the period (for income and expenses).

Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in profit or loss.

2.20 Impairment of Financial Assets

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is 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 has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about certain loss events, including, among others: (i) significant financial difficulty of the issuer or debtor; (ii) a breach of contract, such as a default or delinquency in interest or principal payments; (iii) it is probable that the borrower will enter bankruptcy or other financial reorganization; (iv) the disappearance of an active market for that financial asset because of financial difficulties; or, (v) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group.

(a) Assets Carried at Amortized Cost

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group 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 to be recognized are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables or HTM investments carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in profit or loss.

If a loan or HTM investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. When practicable, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose 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 Group's or BSP'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 and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in future cash flows for groups of assets should reflect and be consistent with changes in related observable data from period to period. The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it may be written off, subject to BSP guidelines, against the related allowance for loan impairment. Such loans are written off after all the necessary procedures including approval from the BOD and the BSP, if necessary under existing regulations, have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the impairment loss in profit or loss.

If, in a subsequent period the amount of the impairment loss decrease 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 profit or loss.

(b) Assets Carried at Fair Value with Changes Recognized in Other Comprehensive Income

In the case of investments classified as AFS financial assets, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for AFS financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss – is removed from other comprehensive income and recognized in profit or loss. Impairment losses recognized in profit or loss on equity instruments are not reversed through profit or loss.

If, in a subsequent period, the fair value of a debt instrument classified as AFS increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed through profit or loss.

(c) Assets Carried at Cost

The Group assesses at the end of each reporting period whether there is objective evidence that any of the unquoted equity securities and derivative assets linked to and required to be settled in such unquoted equity instruments, which are carried at cost, may be impaired. The amount of impairment loss is the difference between the carrying amount of the equity security and the present value of the estimated future cash flows discounted at the current market rate of return of a similar asset. Impairment losses on assets carried at cost cannot be reversed. Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews restructured loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loans' original effective interest rate. The difference between the recorded sale of the original loan and the present value of the restructured cash flows, discounted at the original effective interest rate, is recognized as part of Impairment Losses in the statement of income.

2.21 Impairment of Non-financial Assets

The Group's intangible assets (consisting of goodwill and computer software recorded as part of Other Resources), bank premises, furniture, fixtures and equipment, assets held for sale, and the Bank's investments in subsidiaries are subject to impairment testing. Intangible assets with an indefinite useful life, such as goodwill, are tested for impairment at least annually. All other individual assets or cash-generating units are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

For purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). As a result, some assets are tested individually for impairment and some are tested at cash-generating unit level.

An impairment loss is recognized for the amount by which the asset or cash-generating unit's carrying amount exceeds its recoverable amount which is the higher of fair value, reflecting market conditions, less costs to sell and value in use. In determining value in use, management estimates the expected future cash flows from each cash-generating unit and determines the suitable interest rate in order to calculate the present value of those cash flows. Discount factors are determined individually for each cash-generating unit and reflect management's assessment of respective risk profiles, such as market and asset-specific risk factors.

All assets are subsequently reassessed for indications that an impairment loss previously recognized may no longer exist and the carrying amount of the asset is adjusted to the recoverable amount resulting in the reversal of the impairment loss.

2.22 Employee Benefits

Retirement benefits are provided to employees through a defined benefit plan, as well as a defined contribution plan.

(a) Post-employment Defined Benefit Plan

A defined benefit plan is a post-employment plan that defines an amount of post-employment benefit that an employee will receive on retirement, and is dependent on factors such as age, years of service and salary. The legal obligation for any benefits from this kind of post-employment plan remains with the Group, even if plan assets for funding the defined benefit plan have been acquired. Plan assets may include assets specifically designated to a long-term benefit fund. The Group's post-employment defined benefit plan covers all regular full-time employees. The pension plan is tax-qualified, noncontributory and administered by a trustee.

The liability recognized in the statement of financial position for post-employment defined benefit plans is the present value of the defined benefit obligation (DBO) at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognized actuarial gains or losses and past service costs. The DBO is calculated annually by independent actuaries using the projected unit credit method. The present value of the DBO is determined by discounting the estimated future cash outflows using interest rates of zero coupon government bonds as published by Philippine Dealing and Exchange Corporation, that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related post-employment liability.

Actuarial gains and losses are not recognized as an expense unless the total unrecognized gain or loss exceeds 10% of the greater of the obligation and related plan assets. The amount exceeding this 10% corridor is charged or credited to profit or loss over the employees' expected average remaining working lives. Actuarial gains and losses within the 10% corridor are disclosed separately. Past-service costs are recognized immediately in profit or loss, unless the changes to the retirement plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortized on a straight-line basis over the vesting period.

(b) Defined Benefit Contribution Plan

The Group pays fixed mandatory contributions to the Social Security System. The Group has no legal or constructive obligations to pay further contributions after payment of the fixed contribution. The contributions recognized in respect of defined contribution plans are expensed as they fall due. Liabilities and assets may be recognized if underpayment or prepayment has occurred.

(c) Separation Benefits

Separation benefits are payable when employment is terminated due to resignation or redundancy by the Group before the normal retirement date. The Group recognizes termination benefits when it is demonstrably committed to either: (i) terminating the employment of current employees due to resignation; or (ii) providing termination benefits as a result of a redundancy. Any benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

(d) Profit-Sharing and Bonus Plans

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

(e) Compensated Absences

Compensated absences are recognized for the number of paid leave days (including holiday entitlement) remaining at the end of the reporting date. They are included in the Accrued taxes and other expenses under the Other Liabilities account in the statements of financial position at the undiscounted amount that the Group expects to pay as a result of the unused entitlement.

2.23 Income Taxes

Tax expense recognized in profit or loss comprises the sum of deferred tax and current tax not recognized in other comprehensive income or directly in capital funds, if any.

Current tax assets or liabilities comprise those claims from, or obligations to, fiscal authorities relating to the current or prior reporting period, that are uncollected or unpaid at the reporting period. They are calculated using the tax rates and tax laws applicable to the fiscal periods to which they relate, based on the taxable profit for the year. All changes to current tax assets or liabilities are recognized as a component of tax expense in profit or loss.

Deferred tax is accounted for using the liability method on all temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Under the liability method, with certain exceptions, deferred tax liabilities are recognized for all taxable temporary differences and deferred tax assets are recognized for all deductible temporary differences and the carryforward of unused tax losses and unused tax credits to the extent that it is probable that taxable profit will be available against which the deferred tax assets can be utilized. Unrecognized deferred tax assets are reassessed at the end of each reporting period and are recognized to the extent that it has become probable that future taxable profit will be available to allow such deferred tax assets to be recovered.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the end of the reporting period.

Most changes in deferred tax assets or liabilities are recognized as a component of tax expense in profit or loss. Only changes in deferred tax assets or liabilities that relate to items recognized in other comprehensive income or directly in capital funds are recognized in other comprehensive income or directly in capital funds.

2.24 Related Party Relationships and Transactions

Related party transactions are transfers of resources, services or obligations between the Group and their related parties, regardless whether a price is charged.

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. These parties include: (a) individuals owning, directly or indirectly through one or more intermediaries, control or are controlled by, or under common control with the Bank; (b) associates; (c) individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank and close members of the family of any such individual; and, (d) the Group's retirement plan.

In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely on the legal form.

2.25 Earnings Per Share

Basic earnings per share are determined by dividing the net income for the year attributable to common shareholders by the weighted average number of common shares outstanding during the year, after retroactive effect to any stock dividends declared in the current year.

Diluted earnings per common share are also computed by dividing net income by the weighted average number of common shares subscribed and outstanding at the end of the reporting period. However, net income attributable to common shares and the weighted average number of common shares subscribed and outstanding are adjusted to reflect the effects of any potentially dilutive preferred shares, stock options and warrants. As of December 31, 2012, 2011 and 2010, the Group has no outstanding potentially dilutive securities, hence, the basic earnings per share is equal to diluted earnings per share.

2.26 Trust Activities

The Group commonly acts as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and the related income arising thereon are excluded from these financial statements, as they are not resources of the Group.

2.27 Segment Reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Group's chief operating decision-maker. The chief operating decision-maker is responsible for allocating resources and assessing performance of the operating segments.

In identifying its operating segments, management generally follows the Group's products and services as disclosed in Note 6, which represent the main products and services provided by the Group.

Each of these operating segments is managed separately as each of these services require different technologies and other resources as well as marketing approaches. All inter-segment transfers are carried out at arm's length prices.

The measurement policies the Group uses for segment reporting under PFRS 8, *Operating Segments,* are the same as those used in its financial statements, except that the following are not included in arriving at the operating profit of the operating segments, if any:

- expenses relating to share-based payments;
- research costs relating to new business activities; and,
- revenue, costs and fair value gains from investment properties.

In addition, corporate assets which are not directly attributable to the business activities of any operating segment are not allocated to a particular segment.

There have been no changes from prior periods in the measurement methods used to determine reported segment profit or loss.

The Group's operations are organized according to the nature of the products and services provided. Financial information on business segments is presented in Note 6.

2.28 Events After the End of the Reporting Period

Any post-year-end event that provides additional information about the Group's position at the statement of financial position date (adjusting event) is reflected in the financial statements. Post-year-end events that are not adjusting events, if any, are disclosed when material to the financial statements.

3. SUMMARY OF ACCOUNTING JUDGMENTS AND ESTIMATES

The Group's financial statements prepared in accordance with FRSP for banks require management to make judgments and estimates that affect the amounts reported in the financial statements and related notes. Judgments and estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results may ultimately differ from these estimates.

3.1 Critical Management Judgments in Applying Accounting Policies

In the process of applying the Group's accounting policies, management has made the following judgments, apart from those involving estimation, which have the most significant effect on the amounts recognized in the financial statements:

(a) Determining Functional and Presentation Currency

The Group has determined that its functional and presentation currency is the Philippine peso, which is the currency of the primary environment in which the Group operates.

(b) Tainting of HTM Investments

Except for the exemption from the tainting provision of PAS 39 as allowed by the BSP and the SEC in 2010 as disclosed in Note 2.1, the Group follows the guidance of PAS 39 in classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as HTM investments. This classification requires significant judgment. In making this judgment, the Group evaluates its intention and ability to hold such investments up to maturity. If the Group fails to keep these investments to maturity other than for specific circumstances as allowed under the standards, it will be required to reclassify the whole class as AFS financial assets. In such a case, the investments would, therefore, be measured at fair value, not at amortized cost. In 2011, the Bank disposed of more than an insignificant amount of its HTM investments. Accordingly, the rest of the HTM portfolio was reclassified to AFS financial assets in accordance with PAS 39 (see Notes 11 and 12).

(c) Evaluating Impairment of AFS Financial Assets

The determination when an investment is other-than-temporarily impaired requires significant judgment. In making this judgment, the Group 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 of and near-term business outlook for the investee, including factors such as industry and sector performance, changes in technology and operational and financing cash flows. The Group and Parent Company recognized impairment losses on AFS financial assets in profit or loss amounting to P15,151 in 2011 and nil in 2012 and 2010. Future changes in those information and circumstance might significantly affect the carrying amount of the assets.

(d) Distinction Between Investment Properties and Owner-occupied Properties

The Group determines whether a property qualifies as an investment property. In making its judgment, the Group considers whether the property generated cash flows largely independent of the other assets held by an entity. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rental or for capital appreciation and another portion that is held for use in the production and supply of goods and services or for administrative purposes. If these portions can be sold separately (or leased out separately under finance lease), the Group accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes.

Judgment is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Group considers each property separately in making its judgment.

(e) Distinction Between Operating and Finance Leases

The Group has entered into various lease agreements as either a lessor or lessee. Critical judgment was exercised by management to distinguish each lease agreement as either an operating or finance lease by looking at the transfer or retention of significant risk and rewards of ownership of the properties covered by the agreements. Failure to make the right judgment will result in either overstatement or understatement of resources and liabilities.

(f) Classification of Acquired Properties and Fair Value Determination of Assets Held for Sale and Investment Properties

The Group classifies its acquired properties as Bank Premises, Furniture, Fixtures and Equipment if used in operations, as Assets Held for sale if the Group expects that the properties will be recovered through sale within one year from the date of classification rather than use, as Investment Properties if the Group intends to hold the properties for capital appreciation or as Financial Assets in accordance with PAS 39. At initial recognition, the Group determines the fair value of acquired properties based on valuations performed by independent appraisal companies accredited by the BSP. The appraised value is determined based on the current economic and market conditions as well as the physical condition of the property.

(g) Recognition of Provisions and Contingencies

Judgment is exercised by management to distinguish between provisions and contingencies. Policies on recognition and disclosures of provisions and of contingencies are discussed in Notes 2.14 and 2.15 and relevant disclosures are presented in Note 33.

3.2 Key Sources of Estimation Uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

(a) Estimating Impairment Losses on Other Financial Assets (Loans and Other Receivables and HTM Investments)

The Group reviews its loan and other receivables and HTM investments portfolios to assess impairment at least on an annual basis. In determining whether an impairment loss should be recorded in profit or loss, the Group makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from the portfolio before the decrease can be identified with an individual item in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers or issuers 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 assets with credit risk characteristics and 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.

Impairment losses recognized by the Group and Parent Company on its loans and other receivables are discussed in Notes 13 and 19.

(b) Fair Value Measurement of Financial Assets and Liabilities

Management applies valuation techniques to determine the fair value of financial instruments where active market quotes are not available. This requires management to develop estimates and assumptions based on market inputs, using observable data that market participants would use in pricing the instrument.

Where such data is not observable, management uses its best estimate. Estimated fair values of financial instruments may vary from the actual prices that would be achieved in an arm's length transaction at the reporting date.

In accordance with this PFRS 7, *Financial Instruments: Disclosures*, financial assets and liabilities measured at fair value in the statement of financial position are categorized in accordance with the fair value hierarchy. This hierarchy groups financial assets and liabilities into three levels based on the significance of inputs used in measuring the fair value of the financial assets and liabilities. The fair value hierarchy has the following levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;

- Level 2: inputs other than quoted prices included within Level 1 that are observable for the resource or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level within which the financial asset or liability is classified is determined based on the lowest level of significant input to the fair value measurement. The financial assets and liabilities measured at fair value in the statements of financial position as of December 31, 2012 and 2011 are grouped into the fair value hierarchy as presented in the following table (amounts in millions of Philippine pesos).

Group

	Notes	December 31, 2012			
		Level 1	**Level 2**	**Level 3**	**Total**
Resources					
Financial assets at FVTPL	10				
Derivative assets		P -	P 304	P 39	P 343
Debt securities		54	-	-	54
		54	304	39	397
AFS financial assets	11				
Government bonds		30,390	-	-	30,390
Other debt securities					
Fixed rate treasury notes		31,074	-	-	31,074
Private bonds and commercial papers		18,531	-	-	18,531
Equity securities		8,563	-	-	8,563
		88,558	-	-	88,558
		P 88,612	**P 304**	**P 39**	**P 88,955**
Liabilities					
Derivatives with negative fair values	10	**P 1,048**	**P -**	**P -**	**P 1,048**

	Notes	December 31, 2011			
		Level 1	Level 2	Level 3	Total
Resources					
Financial assets at FVTPL	10				
Derivative assets		P -	P 225	P -	P 225
Debt securities		45	-	-	45
Equity securities		1	-	-	1
		46	225	-	271
AFS financial assets	11				
Government bonds		34,270	-	-	34,270
Other debt securities					
Fixed rate treasury notes		28,938	-	-	28,938
Private bonds and commercial papers		20,872	-	-	20,872
Equity securities		5,568	-	-	5,568
		89,648	-	-	89,648
		P 89,694	P 225	P -	P 89,919
Liabilities					
Derivatives with negative fair values	10	P -	P 159	P -	P 159

Parent

	Notes	December 31, 2012 Level 1	Level 2	Level 3	Total
Resources					
Financial assets at FVTPL	10				
Derivative assets		P -	P 304	P 39	P 343
Debt securities		54	-	-	54
		54	304	39	397
AFS financial assets	11				
Government bonds		30,390	-	-	30,390
Other debt securities					
Fixed rate treasury notes		31,074	-	-	31,074
Private bonds and commercial papers		18,531	-	-	18,531
Equity securities		8,529	-	-	8,529
		88,524	-	-	88,524
		P 88,578	**P 304**	**P 39**	**P 88,921**
Liabilities					
Derivatives with negative fair values	10	**P 1,048**	**P -**	**P -**	**P 1,048**

	Notes	December 31, 2011 Level 1	Level 2	Level 3	Total
Resources					
Financial assets at FVTPL	10				
Derivative assets		P -	P 225	P -	P 225
Debt securities		45	-	-	45
		45	225	-	270
AFS financial assets	11				
Government bonds		34,270	-	-	34,270
Other debt securities					
Fixed rate treasury notes		28,938	-	-	28,938
Private bonds and commercial papers		20,872	-	-	20,872
Equity securities		5,539	-	-	5,539
		89,619	-	-	89,619
		P 89,664	P 225	P -	P 89,889
Liabilities					
Derivatives with negative fair values	10	P -	P 159	P -	P 159

There were no transfers between other levels of hierarchy, except in 2012, when certain unquoted equity securities classified as AFS financial assets with cost amounting to P94,427 as of December 31, 2011 and previously not reflected in the 2011 fair value hierarchy measurement were already included in the 2012 hierarchy using Level 1 measurement. The fair value of such investments amounted to P109,047 as of the date of measurement. Also, in 2011, San Miguel Corporation Series I Preferred Shares became listed. Consequently, transfer between levels of hierarchy from Level 2 to Level 1 amounting to P3,580 was made in 2011. There were no gains or losses recognized in profit or loss for Level 3 instruments.

Unquoted equity securities consist of preferred shares and common shares of various unlisted local companies.

The following table summarizes the carrying amounts and fair values of those financial resources and liabilities not presented in the statement of financial position at their fair values:

	2012			
	Group		Parent	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets				
Cash and other cash items	P 4,242,361	P 4,242,361	P 4,242,324	P 4,242,324
Due from BSP	27,450,311	27,450,311	27,450,311	27,450,311
Due from other banks	2,999,339	2,999,339	2,999,198	2,999,198
Interbank loans receivable	5,503,496	5,503,496	5,503,496	5,503,496
Loans and other receivables	119,716,589	119,673,853	119,639,210	119,596,474
Financial Liabilities				
Deposit liabilities	189,841,357	189,841,357	190,021,317	190,021,317
Bills payable	18,541,267	18,541,267	18,540,767	18,540,767
Notes payable	3,750,000	3,935,750	3,750,000	3,935,750
Manager's checks	5,067,041	5,067,041	5,067,041	5,067,041
Accrued interest payable	310,199	310,199	310,101	310,101
Domestic bills purchased – contra	2,975,895	2,975,895	2,975,895	2,975,895
Due to Treasurer of the Philippines	3,071,036	3,071,036	3,071,036	3,071,036
Accounts payable	1,374,027	1,374,027	1,373,146	1,373,146
Payment orders payable	193,315	193,315	193,315	193,315

	2011			
	Group		Parent	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets				
Cash and other cash items	P 3,686,931	P 3,686,931	P 3,686,914	P 3,686,914
Due from BSP	28,771,881	28,771,881	28,771,881	28,771,881
Due from other banks	3,213,740	3,213,740	3,213,599	3,213,599
Interbank loans receivable	12,989,144	12,989,144	12,989,144	12,989,144
Loans and other receivables	105,011,206	104,709,437	104,931,023	104,629,254
Financial Liabilities				
Deposit liabilities	206,653,344	206,653,344	206,769,837	206,769,837
Bills payable	5,619,244	5,619,244	5,618,744	5,618,744
Notes payable	3,750,000	4,229,962	3,750,000	4,229,962
Manager's checks	3,460,884	3,460,884	3,460,884	3,460,884
Accrued interest payable	431,381	431,381	431,282	431,282
Domestic bills purchased – contra	3,031,209	3,031,209	3,031,209	3,031,209
Due to Treasurer of the Philippines	1,038,123	1,038,123	1,038,123	1,038,123
Accounts payable	1,217,155	1,217,155	1,215,352	1,215,352
Payment orders payable	56,454	56,454	56,454	56,454

(i) Due from BSP and Other Banks

Due from BSP pertains to deposits made by the Group to BSP for clearing and reserve requirements. Due from other banks include interbank placements and items in the course of collection. The fair value of floating rate placements and overnight deposits is their carrying amount. 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, which for short term deposits approximates the nominal value.

(ii) AFS Financial Assets

The fair value of AFS financial assets is determined by direct reference to published price quoted in an active market for traded securities. On the other hand, unquoted AFS financial assets are carried at cost because the fair value cannot be reliably determined either by reference to similar financial instruments or through valuation technique.

(iii) HTM Investments

Fair value for HTM investments is based on market prices. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics or through valuation techniques using discounted cash flow analysis.

(iv) Loans and Other Receivables

Loans and other receivables are net of provisions for impairment. The estimated fair value of loans and receivables represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

(v) Deposits and Borrowings

The estimated fair value of demand deposits with no stated maturity, which includes noninterest-bearing deposits, is the amount repayable on demand. The estimated fair value of long-term fixed interest-bearing deposits and other borrowings without quoted market price is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

(c) Determining Fair Value of Derivatives

The fair values of derivative financial instruments that are not quoted in an active market are determined through valuation techniques using the net present value computation.

Valuation techniques are used to determine fair values which are validated and periodically reviewed. To the extent practicable, models use observable data, however, areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions could affect reported fair value of financial instruments. The Group uses judgment to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

(d) Estimating Useful Lives of Bank Premises, Furniture, Fixtures and Equipment and Computer Software

The Group estimates the useful lives of bank premises, furniture, fixtures and equipment and computer software based on the period over which the assets are expected to be available for use. The estimated useful lives of bank premises, furniture, fixtures and equipment and computer software are reviewed periodically and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limits on the use of the assets. In addition, estimation of the useful lives of bank premises, furniture, fixtures and equipment and computer software is based on collective assessment of industry practice, internal technical evaluation and experience with similar assets. The carrying amounts of bank premises, furniture, fixtures and equipment and computer software are presented in Notes 15 and 18, respectively. Based on management's assessment as at December 31, 2012 and 2011, there is no change in estimated useful lives of those assets during those years. Actual results, however, may vary due to changes in estimates brought about by changes in factors mentioned above.

(e) Determining Fair Value of Investment Properties

The fair value of investment properties is determined based on valuations performed by independent appraisal companies accredited by the BSP at the end of each reporting period. The fair value is determined by reference to market-based evidence, which is the amount for which the assets could be exchanged between a knowledgeable willing buyer and seller in an arm's length transaction as at the valuation date. Such amount is influenced by different factors including the location and specific characteristics of the property (e.g., size, features, and capacity), quantity of comparable properties available in the market, and economic condition and behavior of the buying parties. The amounts of revaluation and fair value gains recognized on certain land, buildings and land improvements are disclosed in Note 16.

(f) Evaluating Realizable Amount of Deferred Tax Assets

The Group reviews its deferred tax assets at the end of each reporting period and reduces the carrying amount to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. The carrying value of deferred tax assets as of those dates is disclosed in Note 28. The Group does not recognize any deferred tax assets on net operating loss carryover (NOLCO) and minimum corporate income tax (MCIT) since management believes that the deferred tax assets on these differences may not be fully utilized in the future.

(g) Estimating Impairment of Non-financial Assets

PFRS requires that an impairment review be performed when certain impairment indicators are present. The Group's policy on estimating the impairment of non-financial assets is discussed in detail in Note 2.21. Though management believes that the assumptions used in the estimation of fair values reflected in the financial statements are appropriate and reasonable, significant changes in these assumptions may materially affect the assessment of recoverable values and any resulting impairment loss could have a material adverse effect on the results of operations.

No impairment losses on non-financial assets were recognized by the Group in 2012, 2011 and 2010.

(h) Valuation of Post-employment and Other Benefits

The determination of the Group's obligation and cost of pension and other post-employment benefits is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions include, among others, discount rates, expected return on plan assets and expected rates of salary increase. In accordance with PFRS, actual results that differ from the assumptions, subject to the 10% corridor test, are accumulated and amortized over future periods and therefore, generally affect the recognized expense and recorded obligation in such future periods. While the Group believes that the assumptions were reasonable and appropriate, significant differences between actual experiences and assumptions may materially affect the cost of employee benefits and related obligations.

The historical rate of return on plan assets was based on the average historical premium of fund assets. The assumed discount rates were determined using the market yields on Philippine government bonds with terms consistent with the expected benefit payout as of the end of each reporting period.

The amounts of retirement benefit obligation and expense and an analysis of the movements in the estimated present value of retirement benefit obligation are presented in Note 27.2.

The Group also estimates other employee benefit obligations and expenses, including the cost of paid leaves based on historical leave availments of employees, subject to Parent Company policies. These estimates may vary depending on future changes in salaries and actual experiences during the year.

4. RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group is exposed to a range of potential risks arising from its business activities. It enters into financial instruments contracts, which consist of financial assets at FVTPL, AFS financial assets, HTM investments, loans and receivables, interbank loans receivable, and financial liabilities such as deposits, bills and acceptances payable and notes payable to finance the Group's operations. The Group also enters into derivative transactions such as interest rate swaps and forward currency contracts to manage the interest rate and currency risks arising from its operations.

The Group's goal in risk management is to ensure that it identifies, understands, measures and monitors the various risks that arise from its business activities, such as credit risk, liquidity risk, market risk, interest rate risk, foreign exchange risk, operational risk, prepayment risk, and legal and regulatory risk.

4.1 Risk Management Structure

The BOD is primarily responsible for approving the risk parameters, credit policies and the overall risk capacity of the Parent Company. Board committees have been established by the BOD to oversee the increasingly varied risk management activities of the Parent Company with the active participation of senior management.

(a) The Executive Committee (EXCOM), composed of seven members of the BOD, exercises certain functions as delegated by the BOD including, among others, the approval of credit proposals, asset recovery and ROPA sales within its delegated limits.

(b) The Risk Management Committee (RMC), composed of seven members of the BOD, is responsible for the development and oversight of the Parent Company's risk management program. It assists the BOD in overseeing all matters relating to risk management including providing a comprehensive and bank-wide oversight of all risks and the management of such risks, formulating and reviewing all of the Parent Company's material risk policies, strategies and procedures. Among its specific duties are to identify and evaluate exposures, develop risk management strategies, implement risk management plans and review such plans as necessary. It also provides oversight, direction, and guidance to the other committees including the Market Risk Committee (MRC) and the Operations Risk Management Committee (ORMC).

(c) The MRC, composed of five members of the BOD, sets policies and standards for market risk identification, analysis and management. The MRC also monitors the sensitivity of the Group's financial condition to the effects of market volatility and adverse price changes on the Group's portfolio of financial instrument and oversees the Group's liquidity position through the Asset and Liability Committee (ALCO).

(d) The ORMC, composed of three members of the BOD and two members from Senior Management, reviews various operations risk policies and practices.

(e) The Audit Committee is a committee of the BOD that is composed of five members, most with accounting, auditing, or related financial management expertise or experience. The skills, qualifications, and experience of the committee members are appropriate for them to perform their duties as laid down by the Board. Two of these five members are independent directors, including the Chairman.

The Audit Committee serves as principal agent of the BOD in ensuring independence of the Bank's external auditors and the internal audit function, the integrity of management, and the adequacy of disclosures and reporting to stockholders. It also oversees the Bank's financial reporting process on behalf of the BOD. It assists the BOD in fulfilling its fiduciary responsibilities as to accounting policies, reporting practices and the sufficiency of auditing relative thereto, and regulatory compliance.

To effectively perform these functions, the Audit Committee has a good understanding of the Parent Company's business including the following: Parent Company's structure, business, controls, and the types of transactions or other financial reporting matters applicable to the Parent Company. The Audit Committee also has a good understanding of the Parent Company's internal controls to determine whether these controls are adequate, functioning as designed, and operating effectively. It also considers the potential effects of emerging business risks and their impact on the Parent Company's financial position and results of operations.

Among the responsibilities of the Audit Committee are:

(i) *Oversight of the financial reporting process.* The Audit Committee ensures that the Parent Company has a high-quality reporting process that provides transparent, consistent and comparable financial statements. In this regard, the Audit Committee works closely with management especially the Office of the Controller, the Internal Audit Division (IAD), as well as the external auditors, to effectively monitor the financial reporting process and the existence of significant financial reporting issues and concerns.

(ii) *Oversight of the audit process.* The Audit Committee is knowledgeable on the audit function and the audit process. The Audit Committee maintains supportive, trusting and inquisitive relationships with both internal and external auditors to enhance its effectiveness.

In the performance of these functions, the Audit Committee is supported by the IAD. The IAD Head derives authority from and is directly accountable to the Audit Committee. However, administratively, the IAD Head reports to the President of the Bank.

The IAD is entirely independent from all the other organizational units of the Bank, as well as from the personnel and work that are to be audited. It operates under the direct control of the Audit Committee and is given an appropriate standing within the Bank to be free from bias and interference. The IAD is free to report its findings and appraisals internally at its own initiative to the Audit Committee.

The IAD is authorized by the Audit Committee to have unrestricted access to all functions, records, property, and personnel of the Bank subject to existing mandate and applicable laws. This includes the authority to allocate resources, set audit frequencies, select subjects, determine scope of work, and apply the techniques required to accomplish the audit engagement objectives.

The IAD is also authorized to obtain the necessary assistance from personnel within the Bank units where they perform audits, as well as other specialized services within or outside the Bank.

At least once a month, the Audit Committee meets to discuss the results of the assurance and consulting engagements and case investigations by IAD. The results of these meetings are regularly reported by the Audit Committee Chairman to the BOD in its monthly meetings.

In response to the increasing role of internal audit under Basel II, the IAD undertook a special project to acquire the right skill set and approach to fulfill its role to conduct an independent review of the Bank's Internal Capital Adequacy Assessment Process (ICAAP) document and its underlying processes and procedures.

(f) The Corporate Governance Committee (CGC) is primarily responsible for helping the BOD fulfill its corporate governance responsibilities. It advocates and assists the BOD in adopting and implementing sound principles and practices of good corporate governance.

The CGC recommends corporate governance policies to the BOD based on the regulations of the BSP, SEC, the PSE and other regulatory bodies, as well as internationally recognized industry best practices. It serves as the primary resource for the BOD to study and evaluate the BOD's and its Committees' structure, policies and practices with the objective of raising the bar for the Bank's corporate governance.

CGC's specific duties include, among others, making recommendations to the BOD regarding continuing education of directors and overseeing the periodic performance evaluation of the BOD, its Committees and senior management.

The CGC consists of seven members of the Board, two of whom are independent directors, including its chairman, and one belonging to the Bank's senior management. It has two sub-committees, namely, the Nominations Sub-Committee and the Compensation and Remuneration Sub-Committee.

The Nominations Sub-Committee is comprised of six voting members of the BOD, one of whom is an independent director, and one non-voting member in the person of the Human Resources Director. The Nominations Sub-Committee is responsible for reviewing the qualifications of and screening candidates for the BOD, key officers of the Bank and nominees for independent directors. It oversees the implementation of programs for identifying, retaining and developing critical officers and the succession plan for various units in the organization.

The Compensation and Remuneration Sub-Committee is composed of five members of the BOD, one of whom is an independent director. It is responsible for overseeing implementation of the programs for salaries and benefits of directors and senior management. It monitors adequacy, effectiveness and consistency of compensation program vis-à-vis corporate philosophy and strategy.

The Bank's Compliance and Corporate Governance Office (CCGO) assists the CGC in fulfilling its functions by apprising the same of pertinent regulations and other issuances relating to corporate governance and continuously giving updates thereon. In addition, the CCGO keeps the CGC abreast of governance issues being brought about among private organizations and individuals advocating good governance practices. It then makes recommendations to the CGC based on such governance issues and practices applicable and relevant to the Bank.

The Parent Company's Risk Management Units (RMUs) are responsible for identifying, assessing, monitoring and managing the credit risk, market risk, liquidity risk and operational risk of the Group in accordance with well-defined policies and procedures. In coordination with the respective business units, they are also responsible for risk policy development, risk analysis, implementation of risk methodologies and risk reporting to senior management and the various committees of the Parent Company.

The RMU's portfolio management function involves the review of the Parent Company's loan portfolio, including the portfolio risks associated with particular industry sectors, regions, loan size and maturity, and the development of a strategy for the Parent Company to achieve its desired portfolio mix and risk profile.

4.2 Credit Risk

Credit risk is the risk of loss resulting from the failure of a borrower or counterparty to honor its financial or contractual obligation to the Parent Company. The risk may arise from lending, trade finance, treasury, investments, derivatives and other activities undertaken by the Parent Company. Credit risk is managed through strategies, policies and limits that are approved by the BOD. Further, the Parent Company has a well-structured and standardized credit approval process and credit scoring system for each of its business and/or product segments.

The RMU undertakes several functions with respect to credit risk management. The RMU independently performs credit risk assessment, evaluation and review for its retail, commercial and corporate financial products to ensure consistency in the Parent Company's risk assessment process. It also ensures that the Parent Company's credit policies and procedures are adequate and are constantly updated to meet the changing demands of the business. The RMU is also responsible for developing procedures to streamline and expedite the processing of credit applications.

The RMU reviews the Parent Company's loan portfolio quality in line with the Parent Company's policy of avoiding significant concentrations of exposure to specific industries or groups of borrowers. Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features. Concentrations indicate the relative sensitivity of the Parent Company's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Parent Company's policies and procedures include guidelines for maintaining a diversified portfolio (e.g. concentration limits). Identified concentrations of credit risks are controlled and managed accordingly. The RMU also monitors compliance to the BSP's limit on exposure to any single person or group of connected persons to an amount not exceeding 25% of the Parent Company's adjusted capital accounts.

4.2.1 Corporate Loans

Corporate lending activities are undertaken by the Bank's Corporate Banking Center. The customer accounts under this group belong to the top tier corporations, conglomerates and large multinational companies. The Bank undertakes a comprehensive procedure for the credit evaluation and risk assessment of large corporate borrowers based on its Internal Credit Risk Rating System. The rating system assesses risks on a three-dimensional level: Borrower Risk, Facility Risk and Security Risk. It also has established concentration limits depending on the Borrower Risk Rating and overall credit quality.

Borrower risk is evaluated by considering (i) quantitative factors, such as profitability, liquidity, capital adequacy and sales growth; (ii) qualitative factors, such as management skills and management integrity; and (iii) industry risk. Industry risk is assessed by considering certain industry characteristics, such as its importance to the economy, growth outlook, cyclicality, industry structure and relevant government policies.

Based on foregoing factors, each borrower is assigned a Borrower Risk Rating (BRR), a 10-grade scoring system that ranges from AAA to D, with AAA to A as High Grade, BBB to B as Standard Grade and CCC and lower as Substandard grade. Borrowers with high grade BRRs are considered to have very strong credits where the Parent Company may be comfortable in granting clean short-term facilities. Borrowers with standard BRRs are similarly acceptable credits but may require collateral to mitigate the credit risk. On the other hand, borrowers with sub-standard BRRs are deemed to be high risk and thus may be required by the Bank to pledge high grade collateral or other forms of credit enhancements.

Below is a summary as of December 31, 2012 and 2011 of the Bank's corporate loans (gross of the related allowance for impairment) with their respective credit scores:

	Credit Score	Description	Amount 2012	Amount 2011
High grade	AAA	Highest quality	**P -**	P -
	AA	High quality	**1,000,000**	873,731
	A	Satisfactory quality	**13,257,602**	9,247,218
Standard grade	BBB	Average	**11,137,688**	11,031,889
	BB	Fair	**1,339,147**	1,113,093
	B	Low	**127,775**	100,217
		Non-rated	**492,546**	103,067
Substandard grade	CCC and below	Substandard	**465,552**	615,352
			P 27,820,310	P 23,084,567

The description of each credit score is explained further as follows:

Highest Quality - These borrowers have a high degree of stability, substance and diversity. They are expected to remain of high quality in virtually all economic conditions and have access to substantial amount of funds through the public markets at any time.

High Quality - These borrowers have a comfortable degree of stability, substance and diversity. They have access to substantial amount of funds through the public market under normal conditions. These are normally the quality multinationals or local corporations which are well capitalized.

Satisfactory Quality - These borrowers have strong cash flows and acceptable degree of stability and substance under normal market conditions. However, they may be susceptible to cyclical changes or concentrations of business risk may be present.

Average - These borrowers have adequate cash flows to meet its commitments and can withstand normal business cycles. However, any prolonged unfavorable economic period would create deterioration beyond acceptable levels as clear risk elements exist reflecting volatility of earnings and performance.

Fair - These borrowers have adequate cash flows to meet its commitments but faces on-going uncertainties and exposure to adverse business, financial or economic conditions.

Low - Although these borrowers currently have adequate cash flows to meet their commitments, their performance have already been weakened and any continuation of adverse business, financial or economic conditions or further downturns are already expected to impair their capacity or willingness to meet their financial commitments.

Substandard - These borrowers have inadequate cash flows and are exposed to a real risk of non-payment of principal. The probability of default increases as the credit score goes down to CCC and lower.

In addition to the BRR, the Bank assigns a loan exposure rating (LER), a 100-point system which is comprised of a Facility Tenor Rating (FTR) and a Security Risk Rating (SRR). The FTR measures the maturity risk based on the length of loan exposure, while the SRR measures the quality of the collateral and risk of its potential deterioration over the term of the loan. The FTR and the SRR, each a 100-point scoring system, are given equal weight in determining the LER.

Once the BRR and the LER have been determined, the credit limit to a borrower is determined under the Risk Asset Acceptance Criteria (RAAC) which is a range of acceptable combinations of the BRR and the LER. For example, under the RAAC, a borrower with a high BRR will have a broader range of acceptable LERs.

The credit rating for each borrower is reviewed annually or earlier if the borrower has a higher risk profile or when there are extraordinary or adverse developments affecting the borrower, the industry and/or the Philippine economy. Any major change in the credit scoring system, the RAAC range and/or the risk-adjusted pricing system is presented to and approved by the RMC.

4.2.2 Commercial Loans

The Parent Company's commercial banking activities are undertaken by its Commercial Banking Center (ComBank). These consist of banking products and services rendered to customers which are entities that are predominantly small and medium scale enterprises (SMEs). These products and services are similar to those provided to large corporate customers, with the predominance of trade finance-related products and services.

ComBank uses a separate 10-grade credit scoring system for commercial accounts, comprised of: an Obligor Risk Rating (ORR), a Facility Risk Adjustment (FRA) and a Final Risk Rating (FRR). An Estimated Cash Risk Position is indicated to determine the secured and unsecured portion of the obligation relative to collateral.

The ORR is an assessment of the creditworthiness of the borrower (or guarantor) without considering the type or amount of the facility, or its security arrangements. It is an indicator of the probability that a borrower cannot meet its credit obligations in the foreseen manner. In determining the ORR, the focus lies on the outlook of the borrower. Although the borrower's financial condition is evaluated on the basis of the historical financial statements, this is primarily to determine any trend in the company's financial position going forward, and how it will impact the company's future solvency or debt-service capabilities.

Based on above factors, each borrower is assigned an ORR that ranges from 1 to 10, with 1 to 3 as High Grade, 4 to 6 as Standard Grade and 7 and lower as Substandard Grade. Borrowers with high grade ORRs are usually granted clean short-term loan facilities. Borrowers with standard ORRs may be required by the Bank to give collateral to enhance their credit rating. On the other hand, borrowers with substandard ORRs are deemed to be high risk, thus, may be required by the Bank to pledge high grade collateral.

Below is a summary as of December 31, 2012 and 2011 of the Bank's commercial loans (gross of related allowance for impairment) with their respective credit scores:

	Credit Score	Description	Amount 2012	Amount 2011
High grade	1	Substantially risk-free	**P 22,000**	P 2,416,406
	2	Minimal risk	**2,638,463**	3,887,983
	3	Moderate risk	**8,464,761**	8,266,844
Standard grade	4	Average risk	**5,407,532**	5,490,434
	5	Above average risk	**3,524,979**	3,593,944
	6	High risk	**1,016,069**	1,799,656
	7	Non-rated	**617,821**	742,535
Substandard grade	Below 7	Past due and C rated	**602,337**	174,465
			P 22,293,962	P 26,372,267

Substantially Risk-free - These borrowers have high degree of stability, substance and diversity. They are expected to remain of high quality in virtually all economic conditions and have access to substantial amount of funds through the public markets at any time.

Minimal Risk - These borrowers have strong market and financial position with history of successful performance. The overall debt service capacity as measured by cash flow to total debt service, as well as their ability to meet their financial commitments, is very strong.

Modest Risk - These borrowers have strong cash flows and acceptable degree of stability and substance under normal market conditions. However, they may be susceptible to cyclical changes or concentrations of business risk may be present.

Average Risk - These borrowers have adequate cash flows to meet its commitments and can withstand normal business cycles. However, any prolonged unfavorable economic period would create deterioration beyond acceptable levels as clear risk elements exists reflecting volatility of earnings and performance.

Above Average Risk - These borrowers have adequate cash flows to meet its commitments but faces on-going uncertainties and exposure to adverse business, financial or economic conditions.

High Risk - Although these borrowers currently have adequate cash flows to meet their commitments, their performance have already been weakened and any continuation of adverse business, financial or economic conditions or further downturns are already expected to impair their capacity or willingness to meet their financial commitments.

Substandard - These borrowers represent inadequacy of cash flows and real risk of non-payment of principal. The probability of default increases as credit rating goes down from 7.

Basically independent from influence of any transactional factors, the ORR is combined with the FRA to allow a more precise depiction of risk. The FRA takes into account the conduct or handling of the borrower's loan and depository accounts. The combination of the ORR and the FRA results in a borrower risk rating which may be combined with other relevant factors not considered initially in the credit scoring system to determine the FRR.

4.2.3 Retail Financial Products

The consumer loan portfolio of the Bank is composed of three main product groups, namely: credit cards, auto and residential mortgage loans. Each of these product groups has their own credit risk guidelines and risk assessment system. Although each loan application is examined through an individual credit evaluation process (combined manual and automated process), the consumer loans are managed on a portfolio basis with respect to defaults as well as accept, reject and review standards.

For the Bank's credit card business, the main risk assessment tool is the applications scoring model which has been revised and fine-tuned through the years using the Bank's own credit experience in the credit card business. The current applications scoring model uses nine variables which have been identified as likely predictors of credit behavior of credit card applicants.

The Bank has categorized the scorecard into three levels: Outright accept, Review band and Outright reject. The Outright Accept category refers to applicants that are within the risk profile acceptable to the Bank and their applications are automatically approved, provided that all information in the application are verified to be accurate based on a validation system presently in place. The Outright Reject category refers to applicants that are below the minimum risk profile acceptable to the Parent Company and their applications are automatically rejected. Applications that fall within the Review Band are borderline cases which are routed for approval by a risk officer, who has the authority to individually accept or reject such applications based on the predetermined review parameters. The Parent Company utilizes statistical modeling in updating its application score cards.

4.2.4 Exposure to Credit Risk

Maximum exposure to credit risk without taking into account any collateral held or other credit enhancements for on-books financial assets and off-books items are shown below:

	Group		Parent	
	2012	2011	**2012**	2011
Credit risk exposures relating to on-books items:				
Due from BSP	**P 27,450,311**	P 28,771,881	**P 27,450,311**	P 28,771,881
Due from other banks	**2,999,339**	3,213,740	**2,999,198**	3,213,599
Interbank loans receivable	**5,503,496**	12,989,144	**5,503,496**	12,989,144
	35,953,146	44,974,765	**35,953,005**	44,974,624
Financial assets at FVTPL				
Derivative assets	**343,229**	225,238	**343,229**	225,238
Debt securities	**53,899**	44,877	**53,899**	44,877
	397,128	270,115	**397,128**	270,115
AFS financial assets				
Government bonds	**30,389,526**	34,270,091	**30,389,526**	34,270,091
Fixed rate treasury notes	**31,074,146**	28,938,441	**31,074,146**	28,938,441
Private bonds and commercial papers	**18,531,308**	20,872,257	**18,531,308**	20,872,257
	79,994,980	84,080,789	**79,994,980**	84,080,789
Loans and receivables				
Receivables from customers				
Commercial	**24,351,524**	28,164,692	**24,351,524**	28,164,692
Corporate	**27,828,584**	22,519,045	**27,828,584**	22,519,045
Consumer	**24,139,907**	21,575,949	**24,139,907**	21,575,949
Bills purchased	**3,038,652**	3,105,128	**3,038,652**	3,105,128
Accrued interest receivable (AIR)	**480,035**	459,641	**480,035**	459,641
Others	**998,879**	743,391	**998,879**	743,391
SPURRA	**35,300,000**	25,200,000	**35,300,000**	25,200,000
Unquoted debt securities classified as loans (UDSCL)	**-**	22,752	**-**	22,752
AIR – other receivables	**1,007,168**	1,532,958	**1,007,168**	1,532,958
Sales contract receivables	**2,025,018**	1,137,258	**2,025,018**	1,137,258
Accounts receivable	**531,517**	530,772	**469,443**	470,209
Installment contracts receivable	**15,305**	19,620	**-**	-
	119,716,589	105,011,206	**119,639,210**	104,931,023
Subtotal (carried forward)	**P 236,061,843**	P 234,336,875	**P 235,984,323**	P 234,256,551

	Group		Parent	
	2012	2011	**2012**	2011
Subtotal (brought forward)	**P 236,061,843**	P 234,336,875	**P 235,984,323**	P 234,256,551
Credit risk exposures relating to off-books items:				
Financial guarantees (see Note 33.2)	**3,546,253**	3,144,618	**3,546,253**	3,144,618
Loan commitments and other credit-related liabilities	**12,802,792**	10,935,011	**12,802,792**	10,935,011
	16,349,045	14,079,629	**16,349,045**	14,079,629
	P 252,410,888	P 248,416,504	**P 252,333,368**	P 248,336,180

4.2.5 Concentrations of Credit Risk

An analysis of concentrations of credit risk for loans and other receivables and investment securities (grossed up for any allowance for impairment losses and unearned discounts) of the Group and the Parent Company by industry and by geographic location as of December 31, 2012 and 2011 is shown below:

Group

	2012			
	Loans and Other Receivables			
	Amount	%	Investment Securities	Total
Concentration by industry				
Manufacturing	P 7,868,846	6.00	P 103,156	P 7,972,002
Real estate, renting and other related activities	27,161,683	20.72	8,110,809	35,272,492
Financial intermediation	49,564,478	37.80*	52,906,715	102,471,193
Community, social and personal activities	18,106,902	13.81	-	18,106,902
Wholesale and retail trade	9,879,210	7.54	18	9,879,228
Transportation, storage and communication	6,468,849	4.93	1,687,170	8,156,019
Electricity, gas and water	6,801,981	5.19	15,734,252	22,536,233
Private households	2,084,942	1.59	-	2,084,942
Hotel and restaurants	987,084	0.75	1,973,138	2,960,222
Others	2,194,348	1.67	123,150	2,317,498
	P 131,118,323	**100.00**	**P 80,638,408**	**P 211,756,731**

* Current BSP regulations limit the concentration to an industry to 30%. Concentration to financial intermediation industry as of December 31, 2012 of P49,564,478 includes reverse repurchase agreements with the BSP of P35,300,000, pertaining to overnight lending which matured immediately after December 31, 2012. Hence, excluding the reverse repurchase agreement account, the concentration ratio to financial intermediation is reduced to 14.89%.

	2012			
	Loans and Other Receivables		**Investment**	
	Amount	**%**	**Securities**	**Total**
Concentration by location				
Philippines	P 130,914,958	99.84	P 66,462,876	P 197,377,834
Other Asia	182,013	0.14	13,226,110	13,408,123
Europe	14,058	0.01	130,106	144,164
United States	7,294	0.01	819,316	826,610
	P 131,118,323	**100.00**	**P 80,638,408**	**P 211,756,731**

	2011			
	Loans and Other Receivables		Investment	
	Amount	%	Securities	Total
Concentration by industry				
Manufacturing	P 8,948,233	7.79	P 211,488	P 9,159,721
Real estate, renting and other related activities	21,363,018	18.59	8,392,128	29,755,146
Financial intermediation	40,039,161	34.84*	52,864,476	92,903,637
Community, social and personal activities	17,038,307	14.82	-	17,038,307
Wholesale and retail trade	9,474,407	8.24	765	9,475,172
Transportation, storage and communication	7,356,072	6.40	1,949,606	9,305,678
Electricity, gas and water	6,865,037	5.97	19,303,739	26,168,776
Private households	1,627,998	1.42	-	1,627,998
Hotel and restaurants	432,068	0.38	1,760,184	2,192,252
Others	1,780,834	1.55	131,558	1,912,392
	P 114,925,135	100.00	P 84,613,944	P 199,539,079

* Current BSP regulations limit the concentration to an industry to 30%. Concentration to financial intermediation industry as of December 31, 2011 of P40,039,161 includes reverse repurchase agreements with the BSP of P25,200,000, pertaining to overnight lending which matured immediately after December 31, 2011. Hence, excluding the reverse repurchase agreement account, the concentration ratio to financial intermediation is reduced to 16.54%.

	2011			
	Loans and Other Receivables		Investment	
	Amount	%	Securities	Total
Concentration by location				
Philippines	P 114,665,515	99.77	P 68,387,483	P 183,052,998
Other Asia	215,308	0.19	15,361,440	15,576,748
Europe	36,519	0.03	141,916	178,435
United States	7,793	0.01	723,105	730,898
	P 114,925,135	100.00	P 84,613,944	P 199,539,079

Parent

	2012			
	Loans and Other Receivables		Investment Securities	Total
	Amount	%		
Concentration by industry				
Manufacturing	P 7,868,846	6.01	P 103,156	P 7,972,002
Real estate, renting and other related activities	27,113,447	20.69	8,110,809	35,224,256
Financial intermediation	49,564,053	37.82*	52,906,715	102,470,768
Community, social and personal activities	18,106,902	13.82	-	18,106,902
Wholesale and retail trade	9,879,210	7.54	18	9,879,228
Transportation, storage and communication	6,468,849	4.94	1,687,170	8,156,019
Electricity, gas and water	6,801,981	5.19	15,734,252	22,536,233
Private households	2,084,942	1.59	-	2,084,942
Hotel and restaurants	987,084	0.75	1,973,138	2,960,222
Others	2,162,428	1.65	123,150	2,285,578
	P 131,037,742	100.00	P 80,638,408	P 211,676,150

* Current BSP regulations limit the concentration to an industry to 30%. Concentration to financial intermediation industry as of December 31, 2012 of P49,564,053 includes reverse repurchase agreements with the BSP of P35,300,000, pertaining to overnight lending which matured immediately after December 31, 2012. Hence, excluding the reverse repurchase agreement account, the concentration ratio to financial intermediation is reduced to 14.90%.

	2012			
	Loans and Other Receivables		Investment Securities	Total
	Amount	%		
Concentration by location				
Philippines	P 130,834,377	99.84	P 66,462,876	P 197,297,253
Other Asia	182,013	0.14	13,226,110	13,408,123
Europe	14,058	0.01	130,106	144,164
United States	7,294	0.01	819,316	826,610
	P 131,037,742	100.00	P 80,638,408	P 211,676,150

	2011			
	Loans and Other Receivables		Investment	
	Amount	%	Securities	Total
Concentration by industry				
Manufacturing	P 8,948,233	7.79	P 211,488	P 9,159,721
Real estate, renting and other related activities	21,283,125	18.53	8,392,128	29,675,253
Financial intermediation	40,037,259	34.86*	52,864,476	92,901,735
Community, social and personal activities	17,038,307	14.84	-	17,038,307
Wholesale and retail trade	9,474,407	8.25	765	9,475,172
Transportation, storage and communication	7,356,072	6.40	1,949,606	9,305,678
Electricity, gas and water	6,865,037	5.98	19,303,739	26,168,776
Private households	1,627,998	1.42	-	1,627,998
Hotel and restaurants	432,068	0.38	1,760,184	2,192,252
Others	1,779,343	1.55	131,558	1,910,901
	P 114,841,849	100.00	P 84,613,944	P 199,455,793

* Current BSP regulations limit the concentration to an industry to 30%. Concentration to financial intermediation industry as of December 31, 2011 of P40,037,259 includes reverse repurchase agreements with the BSP of P25,200,000, pertaining to overnight lending which matured immediately after December 31, 2011. Hence, excluding the reverse repurchase agreement account, the concentration ratio to financial intermediation is reduced to 16.55%.

	2011			
	Loans and Other Receivables		Investment	
	Amount	%	Securities	Total
Concentration by location				
Philippines	P 114,582,229	99.77	P 68,387,483	P 182,969,712
Other Asia	215,308	0.19	15,361,440	15,576,748
Europe	36,519	0.03	141,916	178,435
United States	7,793	0.01	723,105	730,898
	P 114,841,849	100.00	P 84,613,944	P 199,455,793

4.2.6 Credit Quality of Financial Assets

The credit quality of loans and other receivables as well as investment securities are summarized below.

Group

	2012		
	Loans and Other Receivables	**Investment Securities**	**Total**
Neither past due nor impaired	P 112,229,731	P 80,392,108	P 192,621,839
Past due but not impaired	1,562,996	-	1,562,996
Impaired	17,185,847	246,300	17,432,147
	130,978,574	80,638,408	211,616,982
Allowance for impairment	(11,261,985)	(246,300)	(11,508,285)
	P 119,716,589	**P 80,392,108**	**P 200,108,697**

	2011		
	Loans and Other Receivables	Investment Securities	Total
Neither past due nor impaired	P 100,785,601	P 84,350,904	P 185,136,505
Past due but not impaired	887,000	-	887,000
Impaired	13,080,754	263,040	13,343,794
	114,753,355	84,613,944	199,367,299
Allowance for impairment	(9,742,149)	(263,040)	(10,005,189)
	P 105,011,206	P 84,350,904	P 189,362,110

Parent

	2012		
	Loans and Other Receivables	**Investment Securities**	**Total**
Neither past due nor impaired	P 112,180,029	P 80,392,108	P 192,572,137
Past due but not impaired	1,535,319	-	1,535,319
Impaired	17,182,645	246,300	17,428,945
	130,897,993	80,638,408	211,536,401
Allowance for impairment	(11,258,783)	(246,300)	(11,505,083)
	P 119,639,210	**P 80,392,108**	**P 200,031,318**

	2011		
	Loans and Other Receivables	Investment Securities	Total
Neither past due nor impaired	P 100,757,794	P 84,350,904	P 185,108,698
Past due but not impaired	834,624	-	834,624
Impaired	13,077,651	263,040	13,340,691
	114,670,069	84,613,944	199,284,013
Allowance for impairment	(9,739,046)	(263,040)	(10,002,086)
	P 104,931,023	P 84,350,904	P 189,281,927

The table below shows the credit quality per class of financial assets that are neither past due nor impaired, based on the Bank's rating system:

Group

	2012			
	High Grade	**Standard Grade**	**Substandard Grade**	**Total**
Due from BSP	P 27,450,311	P -	P -	P 27,450,311
Due from other banks	2,720,159	279,180	-	2,999,339
Interbank loans receivable	5,503,496		-	5,503,496
	35,673,966	279,180	-	35,953,146
Financial assets at FVTPL				
Government debt securities	62,114	53,899	-	116,013
Private debt securities	149,318	131,797	-	281,115
	211,432	185,696	-	397,128
AFS financial assets				
Government debt securities (including fixed rate treasury notes)	41,368,095	20,095,577	-	61,463,672
Private debt securities	177,586	18,353,722	-	18,531,308
	41,545,681	38,449,299	-	79,994,980
Loans and other receivables				
Receivables from customers				
Corporate	14,257,602	11,337,351	145,000	25,739,953
Commercial	9,770,216	12,770,247	-	22,540,463
Consumer	-	21,233,009	-	21,233,009
Bills purchased	-	3,038,652	-	3,038,652
Accrued interest receivable	-	1,483,603	-	1,483,603
Others	-	1,018,841	-	1,018,841
SPURRA	35,300,000	-	-	35,300,000
UDSCL	-	-	-	-
AIR – other receivables	-	-	-	-
Accounts receivable	-	178,149	-	178,149
Sales contract receivable	-	1,697,061	-	1,697,061
	59,327,818	52,756,913	145,000	112,229,731
	P 136,758,897	**P 91,671,088**	**P 145,000**	**P 228,574,985**

	2011			
	High Grade	Standard Grade	Substandard Grade	Total
Due from BSP	P 28,771,881	P -	P -	P 28,771,881
Due from other banks	3,068,244	145,496	-	3,213,740
Interbank loans receivable	12,989,144	-	-	12,989,144
	44,829,269	145,496	-	44,974,765
Financial assets at FVTPL				
Government debt securities	43,835	44,877	-	88,712
Private debt securities	70,807	110,596	-	181,403
	114,642	155,473	-	270,115
AFS financial assets				
Government debt securities (including fixed rate treasury notes)	40,941,557	22,266,975	-	63,208,532
Private debt securities	169,614	20,702,643	-	20,872,257
	41,111,171	42,969,618	-	84,080,789
Loans and other receivables				
Receivables from customers				
Corporate	10,120,949	10,790,983	-	20,911,932
Commercial	13,858,798	12,019,077	-	25,877,875
Consumer	-	21,886,871	-	21,886,871
Bills purchased	-	3,105,128	-	3,105,128
Accrued interest receivable	-	451,058	-	451,058
Others		755,100	-	755,100
SPURRA	25,200,000	-	-	25,200,000
UDSCL	-	22,752	-	22,752
AIR – other receivables	-	1,532,958	-	1,532,958
Accounts receivable	-	106,341	-	106,341
Sales contract receivable	-	935,586	-	935,586
	49,179,747	51,605,854	-	100,785,601
	P 135,234,829	P 94,876,441	P -	P 230,111,270

Parent

	2012			
	High Grade	**Standard Grade**	**Substandard Grade**	**Total**
Due from BSP	P 27,450,311	P -	P -	P 27,450,311
Due from other banks	2,720,159	279,039	-	2,999,198
Interbank loans receivable	5,503,496	-	-	5,503,496
Subtotal (carried forward)	P 35,673,966	P 279,039	P -	P 35,953,005

	2012			
	High Grade	Standard Grade	Substandard Grade	Total
Subtotal (brought forward)	P 35,673,966	P 279,039	P -	P 35,953,005
Financial assets at FVTPL				
Government debt securities	62,114	53,899	-	116,013
Private debt securities	149,318	131,797	-	281,115
	211,432	185,696	-	397,128
AFS financial assets				
Government debt securities (including fixed rate treasury notes)	41,368,095	20,095,577	-	61,463,672
Private debt securities	177,586	18,353,722	-	18,531,308
	41,545,681	38,449,299	-	79,994,980
Loans and other receivables				
Receivables from customers				
Corporate	14,257,602	11,337,351	145,000	25,739,953
Commercial	9,770,216	12,770,247	-	22,540,463
Consumer	-	21,233,009	-	21,233,009
Bills purchased	-	3,038,652	-	3,038,652
Accrued interest receivable	-	1,483,603	-	1,483,603
Others	-	1,018,841	-	1,018,841
SPURRA	35,300,000	-	-	35,300,000
UDSCL	-	-	-	-
AIR – other receivables	-	-	-	-
Accounts receivable	-	128,447	-	128,447
Sales contract receivable	-	1,697,061	-	1,697,061
	59,327,818	52,707,211	145,000	112,180,029
	P 136,758,897	**P 91,621,245**	**P 145,000**	**P 228,525,142**

	2011			
	High Grade	Standard Grade	Substandard Grade	Total
Due from BSP	P 28,771,881	P -	P -	P 28,771,881
Due from other banks	3,068,244	145,355	-	3,213,599
Interbank loans receivable	12,989,144	-	-	12,989,144
	P 44,829,269	P 145,355	P -	P 44,974,624
Financial assets at FVTPL				
Government debt securities	43,835	44,877	-	88,712
Private debt securities	70,807	110,596	-	181,403
	114,642	155,473	-	270,115
AFS financial assets				
Government debt securities (including fixed rate treasury notes)	40,941,557	22,266,975	-	63,208,532
Private debt securities	169,614	20,702,643	-	20,872,257
	41,111,171	42,969,618	-	84,080,789
Subtotal (carried forward)	P 86,055,082	P 43,270,446	P -	P 129,325,528

	2011 High Grade	Standard Grade	Substandard Grade	Total
Subtotal (brought forward)	P 86,055,082	P 43,270,446	P -	P 129,325,528
Loans and other receivables				
Receivables from customers				
Corporate	10,120,949	10,790,983	-	20,911,932
Commercial	13,858,798	12,019,077	-	25,877,875
Consumer	-	21,886,871	-	21,886,871
Bills purchased	-	3,105,128	-	3,105,128
Accrued interest receivable	-	451,058	-	451,058
Others	-	755,100	-	755,100
SPURRA	25,200,000	-	-	25,200,000
UDSCL	-	22,752	-	22,752
AIR – other receivables	-	1,532,958	-	1,532,958
Accounts receivable	-	95,785	-	95,785
Sales contract receivable	-	918,335	-	918,335
	49,179,747	51,578,047	-	100,757,794
	P 135,234,829	P 94,848,493	P -	P 230,083,322

The table below shows the aging analysis of past due but not impaired financial assets per class of the Group:

	2012 Less than 30 days	**31 to 90 days**	**91 to 180 days**	**More than 180 days**	**Total**
Loans					
Commercial	P 7,664	P -	P -	P -	P 7,664
Consumer	420,087	398,647	-	-	818,734
Corporate	-	-	-	19,104	19,104
Accrued interest receivable	1,217	2,382	-	-	3,599
Others	23,934	116,238	-	-	140,172
	452,902	517,267	-	19,104	989,273
Sales contracts receivable	126,789	136,218	36,985	27,965	327,957
	P 579,691	**P 653,485**	**P 36,985**	**P 47,069**	**P 1,317,230**

	2012 61 to 180 days	**181 to 360 days**	**361 days and over**	**Total**
Other receivables – Accounts receivable	**P 170,070**	**P 27,953**	**P 47,743**	**P 245,766**

	2011				
	Less than 30 days	31 to 90 days	91 to 180 days	More than 180 days	Total
Loans					
Commercial	P 93,748	P 92,160	P -	P -	P 185,908
Consumer	-	84,582	-	-	84,582
Corporate	38	58,668	-	19,045	77,751
Accrued interest receivable	4,696	3,887	-	-	8,583
	98,482	239,297	-	19,045	356,824
Sales contracts receivable	142,024	41,796	17,912	17,191	218,923
	P 240,506	P 281,093	P 17,912	P 36,236	P 575,747

	2011			
	61 to 180 days	181 to 360 days	361 days and over	Total
Other receivables:				
Accounts receivable	P 180,800	P 71,311	P 56,773	P 308,884
Installment contracts receivable	405	1,964	-	2,369
	P 181,205	P 73,275	P 56,773	P 311,253

No separate parent company aging analysis of past due but not impaired financial assets was presented due to insignificant difference between the consolidated and parent company accounts.

4.2.7 Collateral Held As Security and Other Credit Enhancements

The Group holds collateral against loans and other receivables from customers in order to mitigate risk. The collateral may be in the form of mortgage over real estate property, chattels, inventory, cash, securities and/or guarantees. The Bank regularly monitors and updates the fair value of the collateral depending on the type of credit exposure. Estimates of the fair value of collateral are considered in the review and assessment of the adequacy of allowance for credit losses. In general, the Bank does not require collateral for loans and advances to other banks, except when securities are held as part of reverse repurchase agreements.

An estimate of the fair value of collateral and other security enhancements held by the Group against loans and other receivables as of December 31, 2012 and 2011 is shown below:

		2012		2011
Against individually impaired				
Property	**P**	**2,260,916**	P	2,102,002
Others		**22,472,217**		3,508,881
		24,733,133		5,610,883
Against collectively impaired				
Property		**4,543,602**		529,888
Deposits		**517**		-
Others		**2,043,178**		707,373
		6,587,297		1,237,261
Against past due but not impaired				
Property		**1,489,968**		601,593
Deposits		**6,671**		13,390
Others		**178,176**		7,077
		1,674,815		622,060
Against neither past due nor impaired				
Property		**33,882,659**		33,887,628
Deposits		**884,183**		288,011
Others		**15,878,350**		13,796,289
		50,645,192		47,971,928
	P	**83,640,437**	P	55,442,132

4.3 Liquidity Risk

Liquidity risk is the risk that there are insufficient funds available to adequately meet the credit demands of the Group's customers and repay deposits on maturity. The ALCO and the Treasurer of the Group ensure that sufficient liquid assets are available to meet short-term funding and regulatory requirements. Liquidity is monitored by the Group on a daily basis and under stressed situations. A contingency plan is formulated to set out the amount and the sources of funds (such as unused credit facilities) that are available to the Group and the circumstances under which the Group may use such funds.

The Group also manages its liquidity risks through the use of a Maximum Cumulative Outflow (MCO) limit which regulates the outflow of cash on a cumulative basis and on a tenor basis. To maintain sufficient liquidity in foreign currencies, the Group has also set an MCO limit for certain designated foreign currencies. The MCO limits are endorsed by the MRC and approved by the BOD.

The table below shows the maturity profile of the financial liabilities based on contractual undiscounted cash flows (amounts in millions of Philippine pesos):

Group

	2012						
	On demand	**Up to 1 month**	**1 to 3 months**	**3 to 6 months**	**6 to 12 months**	**Beyond 1 year**	**Total**
Non-derivative liabilities							
Deposit liabilities							
Demand	P 62,812	P -	P -	P -	P -	P -	P 62,812
Savings	23,869	-	-	-	-	-	23,869
Time	-	75,552	23,072	3,621	1,159	212	103,616
	86,681	75,552	23,072	3,621	1,159	212	190,297
Bills payable	20	18,342	30	7	21	137	18,557
Notes payable	-	69	-	69	138	4,303	4,579
Manager's checks	5,067	-	-	-	-	-	5,067
Accrued interest payable	-	310	-	-	-	-	310
Accrued other payables	-	222	-	-	-	3,524	3,746
Other liabilities	15	10,531	-	8		88	10,642
	91,783	105,026	23,102	3,705	1,318	8,264	233,198
Derivative liabilities							
Outflow	-	13,934	12,998	4,894	1,470	-	33,296
Inflow	-	(13,606)	(12,521)	(4,702)	(1,419)	-	(32,248)
	-	328	477	192	51	-	1,048
Total liabilities	**P 91,783**	**P 105,354**	**P 23,579**	**P 3,897**	**P 1,369**	**P 8,264**	**P 234,246**

	2011						
	On demand	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Beyond 1 year	Total
Non-derivative liabilities							
Deposit liabilities							
Demand	P 114,752	P -	P -	P -	P -	P -	P 114,752
Savings (as restated)	22,522	-	-	-	-	-	22,522
Time	2	49,397	17,734	1,488	877	202	69,700
	137,276	49,397	17,734	1,488	877	202	206,974
Bills payable	20	3,891	1,550	11	1	161	5,634
Notes payable	-	69	-	69	138	4,303	4,579
Manager's checks	3,461	-	-	-	-	-	3,461
Accrued interest payable	-	431	-	-	-	-	431
Accrued other payables	-	210	-	-	-	2,136	2,346
Other liabilities	45	7,396	3	8	-	77	7,529
	140,802	61,394	19,287	1,576	1,016	6,879	230,954
Derivative liabilities							
Outflow	-	6,791	10,033	1,071	-	-	17,895
Inflow	-	(6,724)	(9,963)	(1,049)	-	-	(17,736)
	-	67	70	22	-	-	159
Total liabilities	P 140,802	P 61,461	P 19,357	P 1,598	P 1,016	P 6,879	P 231,113

Parent

	2012						
	On demand	**Up to 1 month**	**1 to 3 months**	**3 to 6 months**	**6 to 12 months**	**Beyond 1 year**	**Total**
Non-derivative liabilities							
Deposit liabilities							
Demand	P 62,882	P -	P -	P -	P -	P -	P 62,882
Savings	23,979	-	-	-	-	-	23,979
Time	-	75,552	23,072	3,621	1,159	212	103,616
	86,861	75,552	23,072	3,621	1,159	212	190,477
Bills payable	19	18,342	30	7	21	137	18,556
Notes payable	-	69	-	69	138	4,303	4,579
Manager's checks	5,067	-	-				5,067
Accrued interest payable	-	310	-	-	-	-	310
Accrued other payables	-	222	-	-	-	-	222
Other liabilities	15	10,696	-	8		88	10,807
	91,962	105,191	23,102	3,705	1,318	4,740	230,018
Derivative liabilities							
Outflow	-	13,934	12,998	4,894	1,470	-	33,296
Inflow	-	(13,606)	(12,521)	(4,702)	(1,419)	-	(32,248)
	-	328	477	192	51	-	1,048
Total liabilities	**P 91,962**	**P 105,519**	**P 23,579**	**P 3,897**	**P 1,369**	**P 4,740**	**P 231,066**

	2011						
	On demand	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Beyond 1 year	Total
Non-derivative liabilities							
Deposit liabilities							
Demand	P 114,869	P -	P -	P -	P -	P -	P 114,869
Savings	22,522	-	-	-	-	-	22,522
Time	2	49,397	17,734	1,488	877	202	69,700
	137,393	49,397	17,734	1,488	877	202	207,091
Bills payable	19	3,891	1,550	11	1	161	5,633
Notes payable	-	69	-	69	138	4,303	4,579
Manager's checks	3,461	-	-	-	-	-	3,461
Accrued interest payable	-	431	-	-	-	-	431
Accrued other payables	-	207	-	-	-	-	207
Other liabilities	45	7,467	3	8	-	77	7,600
	140,918	61,462	19,287	1,576	1,016	4,743	229,002
Derivative liabilities							
Outflow	-	6,791	10,033	1,071	-	-	17,895
Inflow	-	(6,724)	(9,963)	(1,049)	-	-	(17,736)
	-	67	70	22	-	-	159
Total liabilities	P 140,918	P 61,529	P 19,357	P 1,598	P 1,016	P 4,743	P 229,161

Following is the contractual maturity per type of derivative liabilities for both the Group and Parent Company in 2012 and 2011:

	On demand	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Beyond 1 year	Total
2012							
Foreign currency forwards	**P -**	**P 328**	**P 477**	**P 192**	**P 51**	**P -**	**P 1,048**

	On demand	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Beyond 1 year	Total
2011							
Foreign currency forwards	P -	P 67	P 70	P 22	P -	P -	P 159

4.4 Market Risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rate, foreign exchange rates and equity prices. The Group classifies exposures to market risk into either trading book or banking book. The market risk for the trading portfolio is managed and monitored based on a Value-at-Risk (VaR) methodology. Meanwhile, the market risk for the non-trading positions are managed and monitored using other sensitivity analyses.

The Group applies a VaR methodology to assess the market risk of positions held and to estimate the potential economic loss based upon a number of parameters and assumptions for various changes in market conditions. VaR is a method used in measuring financial risk by estimating the potential negative change in the market value of a portfolio at a given confidence level and over a specified time horizon.

The Group uses the parametric VaR approach in assessing the possible changes in the market value of held-for-trading and AFS financial assets based on historical data for a rolling one year period. The VaR models are designed to measure market risk in a normal market environment. The models assume that any changes occurring in the risk factors affecting the normal market environment will follow a normal distribution. The use of VaR has limitations because it is based on historical correlations and volatilities in market prices and assumes that future price movements will follow a statistical distribution. Due to the fact that VaR relies heavily on historical data to provide information and may not clearly predict the future changes and modifications of the risk factors, the probability of large market moves may be underestimated if changes in risk factors fail to align with the normal distribution assumption.

VaR may also be underestimated or overestimated due to the assumptions placed on risk factors and the relationship between such factors for specific instruments. Even though positions may change throughout the day, the VaR only represents the risk of the portfolios at the close of each business day, and it does not account for any losses that may occur beyond the 99% confidence level.

The VaR figures are backtested daily against actual and hypothetical profit and loss of the trading book to validate the robustness of the VaR model. To supplement the VaR, the Group performs stress tests wherein the trading portfolios are valued under extreme market scenarios not covered by the confidence interval of the Group's VaR model.

Since VaR is an integral part of the Group's market risk management, VaR limits have been established annually for all financial trading activities and exposures against the VaR limits and are monitored on a daily basis. Limits are based on the tolerable risk appetite of the Group.

A summary of the Group's VaR position at December 31, 2012 and 2011 follows (amounts in millions of Philippine pesos):

	2012			
	Foreign Exchange	**Interest Rate**	**Equity**	**Total VaR**
December 31	P 4.8	P 865.8	P 132.5	P 1,003.1
Average daily	5.8	922.9	115.6	1,044.3
Highest	16.6	1,644.9	203.8	1,799.5
Lowest	nil	637.7	89.9	736.2

	2011			
	Foreign Exchange	Interest Rate	Equity	Total VaR
December 31	P 13.0	P 1,507.3	P 147.3	P 1,667.6
Average daily	10.5	774.1	37.3	821.9
Highest	50.1	1,594.4	150.3	1,794.8
Lowest	nil	285.2	25.3	310.5

The high and low of the total portfolio may not equal to the sum of the individual components as the high and lows of the individual portfolios may have occurred on different trading days. The VaR for foreign exchange is the foreign exchange risk throughout the Parent Company.

4.5 Interest Rate Risk

A critical element of the Group's risk management program consists of measuring and monitoring the risks associated with fluctuations in market interest rates on the Group's net interest income and ensuring that the exposure in interest rates is kept within acceptable limits.

The Group employs "gap analysis" to measure the interest rate sensitivity of its resources and liabilities. The gap analysis measures, for any given period, any mismatch between the amounts of interest-earning resources and interest-bearing liabilities which would mature or reprice during the period. A positive gap occurs when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities while a negative gap occurs when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. Accordingly, during a period of rising interest rates, a company with a positive gap will have more interest rate sensitive assets repricing at a higher interest rate than interest rate sensitive liabilities which will be favorable to it. During a period of falling interest rates, a company with a positive gap will have more interest rate sensitive assets repricing at a lower interest rate than interest rate sensitive liabilities, which will be unfavorable to it.

The asset-liability gap position of the Parent Company at carrying amounts follows (amounts in millions of Philippine pesos):

	2012			
	Up to Six Months	**Beyond Six Months to One Year**	**Beyond One Year**	**Total**
Resources				
Placements	P 8,503	P -	P 27,450	P 35,953
Loans	92,525	8,607	18,507	119,639
Investments	1,273	778	86,870	88,921
	102,301	9,385	132,827	244,513
Liabilities				
Deposit liabilities	101,848	1,131	87,042	190,021
Bills payable	18,380	7	154	18,541
Notes payable	-	-	3,750	3,750
	120,228	1,138	90,946	212,312
Asset-Liability Gap	**(P 17,927)**	**P 8,247**	**P 41,881**	**P 32,201**

	2011			
	Up to Six Months	Beyond Six Months to One Year	Beyond One Year	Total
Resources				
Placements	P 33,103	P -	P 11,872	P 44,975
Loans	59,931	7,349	37,651	104,931
Investments	491	3,419	86,074	89,984
	93,525	10,768	135,597	239,890
Liabilities				
Deposit liabilities	68,365	852	137,553	206,770
Bills payable	5,457	1	161	5,619
Notes payable	-	-	3,750	3,750
	73,822	853	141,464	216,139
Asset-Liability Gap	P 19,703	P 9,915	(P 5,867)	P 23,751

The Parent Company's maturing financial liabilities within the one to six month period pertain to time deposits as well as bills payable due to banks and other financial institutions. Maturing bills payable are usually settled through repayments. When maturing financial assets are not sufficient to cover the related maturing financial liabilities, bills payable and other currently maturing financial liabilities are rolled over/refinanced or are settled by entering into new borrowing arrangements with other counterparties.

4.6 Foreign Exchange Risk

Foreign exchange risk is the risk to earnings or capital arising from changes in foreign exchange rates.

The Group's net foreign exchange exposure, taking into account any spot or forward exchange contracts, is computed as foreign currency assets less foreign currency liabilities. The foreign exchange exposure is limited to the day-to-day, over-the-counter buying and selling of foreign exchange in the Group's branches, as well as foreign exchange trading with corporate accounts and other financial institutions. The Group is permitted to engage in proprietary trading to take advantage of foreign exchange fluctuations.

The breakdown of the financial resources and liabilities of the Group and Parent Company as to foreign currency-denominated balances, translated to Philippine pesos as of December 31, 2012 and 2011 follows:

	2012		
	U.S. Dollar	Other Foreign Currencies	Total
Resources:			
Cash and other cash items	P 355,484	P 45,898	P 401,382
Due from other banks	2,054,577	684,703	2,739,280
Interbank loans receivables	5,101,113	302,383	5,403,496
Financial assets at FVTPL	100,002	-	100,002
AFS financial assets	42,187,420	819,030	43,006,450
Loans and other receivables	9,588,396	150,612	9,739,008
	59,386,992	2,002,626	61,389,618
Liabilities:			
Deposit liabilities	37,538,765	1,520,097	39,058,862
Bills payable	18,357,087	31,039	18,388,126
Derivative liabilities	1,965	-	1,965
Accrued interest and other expenses	55,072	552	55,624
Other liabilities	110,218	16,282	126,500
	56,063,107	1,567,970	57,631,077
Currency swaps and forwards	(3,067,314)	(289,457)	(3,356,771)
Net exposure	**P 256,571**	**P 145,199**	**P 401,770**

	2011		
	U.S. Dollar	Other Foreign Currencies	Total
Resources:			
Cash and other cash items	P 297,644	P 30,396	P 328,040
Due from other banks	2,649,588	380,659	3,030,247
Interbank loans receivables	11,622,024	1,367,120	12,989,144
Financial assets at FVTPL	113,588	-	113,588
AFS financial assets	48,571,746	56,976	48,628,722
Loans and other receivables	9,513,815	137,013	9,650,828
	72,768,405	1,972,164	74,740,569
Liabilities:			
Deposit liabilities	60,123,841	1,721,455	61,845,296
Bills payable	5,427,976	9,875	5,437,851
Derivative liabilities	28,557	-	28,557
Accrued interest and other expenses	105,504	613	106,117
Other liabilities	175,197	7,590	182,787
	65,861,075	1,739,533	67,600,608
Currency swaps and forwards	(8,093,494)	(209,492)	(8,302,986)
Net exposure	(P 1,186,164)	P 23,139	(P 1,163,025)

The Bank's foreign currency position for BSP reporting purposes is determined by also considering the foreign currency position of non-financial assets and liabilities that are denominated in foreign currencies, such as sundry debits, due from Head Office and branches, sundry credits and other dormant credits. The Bank's net foreign currency exposure for BSP reporting, which is required to be presented in aggregate net U.S. dollar amounts and translated to Philippine pesos, as of December 31, 2012 and 2011 follows:

	2012	2011
In U.S. dollars	**($ 14,520)**	($ 34,594)
In Philippine pesos	**(P 596,046)**	(P 1,516,601)

The Parent Company's policy is to maintain foreign currency exposure within acceptable limits and within existing regulatory guidelines. The Parent Company believes that its profile of foreign currency exposure on its assets and liabilities is within conservative limits for a financial institution engaged in the type of business in which the Parent Company is involved.

The following tables illustrate the sensitivity of the net results and capital funds to the changes in foreign exchange rates on the Group's financial assets and financial liabilities. The percentages change (increase and decrease) have been determined based on the average market volatility in exchange rates in the previous 12 months, using a confidence level of 99%. The sensitivity analysis is based on the Group's foreign currency-denominated financial instruments held at each reporting date, including currency swaps and forwards.

	2012		2011	
	Increase in % change	**Effect on net profit for the year**	Increase in % change	Effect on net profit for the year
U.S. dollars	1.0%	P 2,740	1.0%	(P 8,131)
Japanese yen	1.5%	181	2.0%	12
Euro	1.5%	1,736	2.0%	73
Others	1.1%	246	1.9%	378

4.7 Operational Risk

To standardize the practice and to conform to international standards, the Parent Company has adopted the Basel Committee's definition of operational risk. This is formalized in the Parent Company's approved Operational Risk Management Framework. Operational risk is the risk of loss arising from inadequate or failed internal processes, people, and systems or external events. This definition includes legal risk, but excludes strategic and reputational risk. This also covers potential losses that could occur as a result of the Parent Company's exposure in the use of technology-related products, services, delivery channels, and processes.

Each specific unit of the Parent Company has its roles and responsibilities in the management of operational risk and these are clearly stated in the operational risk management framework. At the BOD level, an ORMC was formed to provide overall direction in the management of operational risk.

The ORMC composed of three members of the BOD and two senior management officers of the Parent Company, covers the following areas of concern:

(a) The adequacy of the Parent Company's policies, procedures, organization and resources for preventing, or limiting the damage from unexpected loss due to deficiencies in information systems, business, operational and management processes, employees skills and supervision, equipment and internal controls.

(b) Results of periodic or special risk assessments conducted in various businesses and operating units of the Parent Company to proactively uncover operational risks that may result to actual loss or damage to the Parent Company.

(c) Results of internal audits, BSP examinations and investigation of administrative cases that highlight trends indicative of present or emerging exposures to specific operational risks.

(d) Risk assessment of major information systems to be implemented in the Parent Company.

(e) Regulatory compliance issues, whether currently existing, or anticipated to arise as a result of new laws or regulations.

(f) Business continuity strategies, plans, and resources.

An Operational Risk Management (ORM) Unit has been formed and was given the mandate to build and lead the roadmap in developing the foundations and systems necessary for the effective implementation of an Operational Risk Management Framework. The roadmap is primarily based on the best practices model as applied by other foreign and local financial institutions. In line with the adoption of an Enterprise Risk Management framework for the Parent Company, the ORM Unit together with all the other Risk Units, is now reporting directly to the Chief Risk Officer.

The Parent Company, as a matter of practice, has embedded in its processes the basic strategies necessary to manage exposure to operational risk. Foremost is the proper segregation of duties and responsibilities. It ensures that no person will be able to approve his own transaction, and provides the necessary control layers to provide check and balance.

In managing products and services, no new products or services are implemented without an operational risk assessment. As part of the product approval process, product managers ensure that risks are clearly identified and adequately controlled and mitigated. For existing products and services, regular reviews are conducted and controls are assessed to determine their continued effectiveness. The Parent Company, as part of its continuing effort to manage operational risk, has ensured that the basic strategies to manage exposure to operational risk have been embedded in its control processes.

For all technology-related activities and initiatives, the Parent Company has a Technology Steering Committee (TSC), to provide oversight function. Its members are composed of Senior Management officers from both the business and the operational units, thereby allowing a comprehensive and high level guidance on technology-related issues that may impact the Parent Company. The Parent Company has developed and implemented a Business Continuity Plan to give assurance that bank services will continue in the event of disasters or unforeseen circumstances.

4.8 Prepayment Risk

Prepayment risk is the risk that the Parent Company will incur a financial loss because its customers and counterparties repay or request repayment earlier than expected, such as fixed rate mortgages when interest rates fall. The Parent Company has exposures in consumer loans (e.g., housing and motor vehicles). These activities generate market risk since these loan products are inherently sensitive to changes in the level of market interest rates. Based on historical data from 2011 to twelve months ended December 31, 2012, and from 2010 to twelve months ended December 31, 2011 prepayment received by the Parent Company is less than 1% of the total consumer loan portfolio.

4.9 Legal Risk and Regulatory Risk Management

Legal risk pertains to the Bank's exposure to losses arising from cases decided not in favor of the Bank where significant legal costs have already been incurred, or in some instances, where the Bank may be required to pay damages. The Bank is often involved in litigation in enforcing its collection rights under loan agreements in case of borrower default. The Bank may incur significant legal expenses as a result of these events, but the Bank may still end up with non-collection or non-enforcement of claims. The Bank has established measures to avoid or mitigate the effects of these adverse decisions and engages several qualified legal advisors, who were endorsed to and carefully approved by senior management. At year-end, the Bank also ensures that material adjustments or disclosures are made in the financial statements for any significant commitments or contingencies which may have arisen from legal proceedings involving the Bank.

Regulatory risk refers to the potential risk for the Bank to suffer financial loss due to changes in the laws or monetary, tax or other governmental regulations of a country. The monitoring of the Bank's compliance with these regulations, as well as the study of the potential impact of new laws and regulations, is the primary responsibility of the Bank's Chief Compliance Officer. The Chief Compliance Office is responsible for communicating and disseminating new rules and regulations to all units, analyzing and addressing compliance issues, performing periodic compliance testing on branches and Head Office units, and reporting compliance findings to the Audit Committee and the BOD.

5. CAPITAL MANAGEMENT

5.1 Regulatory Capital

The Bank's lead regulator, the BSP, sets and monitors capital requirements of the Bank.

In implementing current capital requirements, the BSP requires the Bank to maintain a minimum capital amount and a prescribed ratio of qualifying capital to risk-weighted assets, known as the "capital adequacy ratio" (CAR). Risk-weighted assets is the aggregate value of assets weighted by credit risk, market risk, and operational risk, based on BSP-prescribed formula provided under its circulars.

Under BSP Circular No. 360, effective July 1, 2003, the capital-to-risk assets ratio is to be inclusive of a market risk charge. In August 2006, the BSP issued Circular No. 538 which contains the implementing guidelines for the revised risk-based capital adequacy framework to conform to Basel II recommendations. Under the revised framework, capital requirements for operational risk, credit derivatives and securitization exposures are to be included in the calculation of the Bank's capital adequacy. The revised framework also prescribes a more granular mapping of external credit ratings to the capital requirements and recognizes more type of financial collateral and guarantees as credit risk mitigants. Changes in the credit risk weights of various assets, such as foreign currency denominated exposures to the Philippine national government, non-performing exposures and ROPA, were also made. Exposures are required to be risk-weighted based on third party credit assessment of the individual exposure given by eligible external credit assessment institutions. Credit risk-weights range from 0% to 150% depending on the type of exposure and/or credit assessment of the obligor. The new guidelines took effect on July 1, 2007.

In computing the CAR, the regulatory qualifying capital is analyzed into two tiers which are: (i) Tier 1 Capital, and (ii) Tier 2 Capital; less deductions from the Total Tier 1 and Tier 2 for the following:

(a) investments in equity of unconsolidated subsidiary banks and other financial allied undertakings, but excluding insurance companies;

(b) investments in debt capital instruments of unconsolidated subsidiary banks;

(c) investments in equity of subsidiary insurance companies and non-financial allied undertakings;

(d) reciprocal investments in equity of other banks/enterprises; and

(e) reciprocal investments in other regulatory capital instruments of other banks and quasi-banks.

Provided, that any asset deducted from the qualifying capital in computing the numerator of the risk-based capital ratio shall not be included in the risk-weighted assets in computing the denominator of the ratio.

Tier 1 Capital and Tier 2 Capital are defined as follows:

(a) Tier 1 Capital includes the following:

i. paid-up common stock,
ii. paid-up perpetual and non-cumulative preferred stock,
iii. common and perpetual, non-cumulative preferred stock dividends distributable,
iv. surplus,
v. surplus reserves,
vi. undivided profits (for domestic banks only),
vii. unsecured subordinated debt (with prior BSP approval), and,
viii. minority interest in the equity of subsidiary financial allied undertakings

Subject to deductions for:

i. treasury shares,
ii. unrealized losses on underwritten listed equity securities purchased,
iii. unbooked valuation reserves, and other capital adjustments based on the latest report of examination,
iv. outstanding unsecured credit accommodations, both direct and indirect, to directors, officers, stockholders and their related interests (DOSRI),
v. goodwill, and
vi. deferred income tax.

(b) Tier 2 Capital includes:

i. perpetual and cumulative preferred stock,
ii. limited life redeemable preferred stock with or without the replacement requirement subject to BSP conditions,
iii. dividends distributable of (i) and (ii) above,
iv. appraisal increment reserve – bank premises, as authorized by the Monetary Board (MB),
v. net unrealized gains on underwritten listed equity securities purchased,
vi. general loan loss provision,
vii. unsecured subordinated debt with a minimum original maturity of at least ten years (with prior BSP approval),
viii. unsecured subordinated debt with a minimum original maturity of at least five years (with prior BSP approval), and,
ix. deposit for stock subscription on:

- common stock,
- perpetual and non-cumulative preferred stock,
- perpetual and cumulative preferred stock subscription, and
- limited life redeemable preferred stock subscription with the replacement requirement upon redemption

Subject to deductions for:

i. Perpetual and cumulative preferred stock treasury shares,
ii. Limited life redeemable preferred stock treasury shares with the replacement requirement upon redemption,
iii. Sinking fund for redemption of limited life redeemable preferred stock with the replacement requirement upon redemption,
iv. Limited life redeemable preferred stock treasury shares without the replacement requirement upon redemption, and,
v. Sinking fund for redemption of limited life redeemable preferred stock without the replacement requirement upon redemption.

The Group's and the Bank's regulatory capital position as of December 31, 2012 and 2011 follow (amounts in millions):

	Group		Parent	
	2012	2011	**2012**	2011
Tier 1 Capital	**P 31,247**	P 25,296	**P 31,254**	P 25,303
Tier 2 Capital	**4,636**	4,776	**4,636**	4,776
Total Regulatory Capital	**35,883**	30,072	**35,890**	30,079
Deductions	**-**	-	**(2)**	(4)
Total Qualifying Capital, after deductions	**P 35,883**	P 30,072	**P 35,888**	P 30,075
Credit risk-weighted assets	**P 147,112**	P 144,841	**P 147,124**	P 144,850
Market risk-weighted assets	**6,557**	1,810	**6,557**	1,810
Operational risk-weighted assets	**19,832**	18,475	**19,832**	18,475
Total risk-weighted assets	**P 173,501**	P 165,126	**P 173,513**	P 165,135
Capital ratios:				
Total regulatory capital expressed as percentage of total risk weighted assets	**20.68%**	18.21%	**20.68%**	18.21%
Total Tier 1 expressed as percentage of total risk-weighted assets	**18.01%**	15.32%	**18.01%**	15.32%

The capital ratios comply with the BSP prescribed ratio of at least 10%.

The breakdown of credit risk-weighted assets and market risk-weighted assets follow:

	Group		Parent	
	2012	2011	**2012**	2011
On-books assets	**P 143,979**	P 143,041	**P 143,991**	P 143,050
Off-books assets	**2,530**	1,512	**2,530**	1,512
Counterparty risk-weighted assets in the trading books	**603**	288	**603**	288
Total Credit Risk-Weighted Assets	**P 147,112**	P 144,841	**P 147,124**	P 144,850
Interest rate exposures	**P 582**	P 275	**P 582**	P 275
Foreign exchange exposures	**5,975**	1,535	**5,975**	1,535
Total Market-Risk Weighted Assets	**P 6,557**	P 1,810	**P 6,557**	P 1,810

5.2 Minimum Capital Requirement

Under the relevant provisions of current BSP regulations, the required minimum capitalization of a universal bank is P4.95 billion. As of December 31, 2012 and 2011, the Bank is in compliance with this regulation.

5.3 Ensuring Sufficient Capital

On January 15, 2009, the BSP issued Circular No. 639 articulating the need for banks to adopt and document an internal capital adequacy assessment process ("ICAAP"). All universal and commercial banks are expected to perform a thorough assessment of all their material risks, as well as maintain capital adequate to support these risks. This is intended to complement the current regulatory capital requirement of at least 10% of risk assets, which covered only credit, market and operational risks. On December 29, 2009, BSP issued Circular No. 677 effectively extending the implementation of the ICAAP from January 2010 to January 2011.

Cognizant of the importance of a strong capital base to meet strategic and regulatory requirements, the Bank has adopted a robust ICAAP on a group-wide level that is consistent with its risk philosophy and risk appetite. The ICAAP Document embodies the Bank's risk philosophy, risk appetite, and risk governance framework and structure, and integrates these with: (a) the Bank's strategic objectives and long-term strategies called FOCUS 2020; (b) the five-year financial and business plans; and, (c) the capital plan and dividend policy.

The ICAAP's objective is to ensure that the BOD and Senior Management actively and promptly identify and manage the material risks arising from the general business environment, and that an appropriate level of capital is maintained to cover these risks. To test the adequacy of its capital even under difficult conditions, the Bank conducts regular stress testing to assess the effects of extreme but plausible events on its capital. The results are thoroughly discussed during RMC meetings, and reported to the Board. In the course of its discussions, the BOD and Senior Management may request for additional stress testing scenarios or revisions to the test assumptions in order to better align these to current trends and forecasts.

The Bank has a cross-functional ICAAP technical team, comprised of representatives from the core risk management units – credit, market and operational risks; financial controllership; treasury; corporate planning; internal audit; and compliance. This ensures a well-coordinated approach to the development, documentation, implementation, review, improvement, and maintenance of the various sub-processes included in the ICAAP. The members of the Bank's IAD were given further training to enhance their expertise particularly on the subjects of Basel II and ICAAP.

In September 2011, the Bank engaged an independent consultant to assist in the development and bank-wide implementation of an Enterprise Risk Management (ERM) discipline, envisioned to strengthen the Bank's capital and risk management framework. The consultant conducted an ERM awareness training for the Bank's BOD, members of the Senior Management and the ICAAP technical team. They also held ERM Awareness Workshops that was attended by identified risk champions from various levels of the organization who were deemed to possess extensive exposure to and knowledge of operations and risk issues. The engagement also includes the review and enhancement of the Bank's risk universe, risk dictionary, risk appetite and risk assessment, and development of risk treatment and action plans, risk indicators and an ERM manual.

On March 8, 2012, the BSP released through the Bankers Association of the Philippines, the Discussion Paper on Basel III Implementation in the Philippines. The discussion paper outlines the key proposals regarding the new regulatory capital framework set forth by the Basel Committee on Banking Supervision, as follows: (a) new categorization of the capital base; (b) revised eligibility criteria for the different categories of regulatory capital; (c) regulatory adjustments; (d) higher minimum capital requirements; (e) loss absorbency of regulatory capital at the point of non-viability; (e) introduction of a framework to promote the conservation of capital and the build-up of adequate buffers above the minimum; and (f) additional disclosure requirements. Subsequently, on January 15, 2013, the BSP issued Circular No. 781, which specifies the implementing guidelines on the revised risk-based capital adequacy framework in accordance with the Basel III standards, applicable to universal and commercial banks as well as their subsidiary banks and quasi-banks effective January 1, 2014. In this connection, the Bank in its 2013 ICAAP Document considered the possible impact of Basel III implementation on the eligibility of unsubordinated notes as qualifying capital and the changes in composition of qualifying capital.

The Bank's ICAAP document was subjected to independent review of IAD to provide reasonable assurance that the Bank met regulatory requirements. The results of the audit assessment were presented to the Audit Committee and the BOD in January 2013. Based on IAD's assessment of the Bank's ICAAP document, its related supporting documents, existing processes and structures, IAD reported that the Bank has satisfactorily complied with the minimum requirements prescribed in BSP Circular No. 639. IAD also noted that the Bank has undertaken improvements in its capital and risk management processes, considering the comments received from the BSP and results of the internal audit review.

The Bank's 2013 ICAAP Document was presented to and approved by the BOD on January 25, 2013 and submitted to the BSP on January 31, 2013.

6. SEGMENT REPORTING

6.1 Business Segments

The Group's main operating businesses are organized and managed separately according to the nature of products and services provided and the different markets served, with each segment representing a strategic business unit. These are also the basis of the Group in reporting to its chief operating decision-maker for its strategic decision-making activities. The Group's main business segments are as follows:

(a) Consumer Banking

This segment principally handles individual customers' deposits and provides consumer type loans, such as automobiles and mortgage financing, credit card facilities and funds transfer facilities;

(b) Corporate and Commercial Banking

This segment principally handles loans and other credit facilities and deposit and current accounts for corporate, institutional, small and medium enterprises, and middle market customers;

(c) Treasury

This segment is principally responsible for managing the Bank's liquidity and funding requirements, and handling transactions in the financial markets covering foreign exchange and fixed income trading and investments and derivatives; and,

(d) Headquarters

This segment includes corporate management, support and administrative units not specifically identified with Consumer Banking, Corporate Banking or Treasury.

These segments are the basis on which the Group reports its primary segment information. Transactions between segments are conducted at estimated market rates on an arm's length basis.

Segment resources and liabilities comprise operating resources and liabilities including items such as taxation and borrowings. Revenues and expenses that are directly attributable to business segment and the relevant portions of the Group's revenues and expenses that can be allocated to that business segment are accordingly reflected as revenues and expenses of that business segment.

6.2 Intersegment Transactions

There were no intersegment transactions for 2012, 2011 and 2010.

6.3 Analysis of Segment Information

Segment information of the Group as of and for the years ended December 31, 2012, 2011 and 2010 is presented as follows (amounts in millions of Philippine pesos):

	Consumer Banking	Corporate and Commercial Banking	Treasury	Headquarters	Total
December 31, 2012					
Results of operations					
Net interest income and other income	P 4,795	P 2,182	P 8,006	P 3,159	P 18,142
Other expenses	(3,170)	(987)	(822)	(3,690)	(8,669)
Income before impairment losses and income tax	**P 1,625**	**P 1,195**	**P 7,184**	**(P 531)**	P 9,473
Impairment losses					(1,560)
Tax expense					(328)
Net income					**P 7,585**
Segment resources	**P 47,240**	**P 71,637**	**P 138,425**	**P 22,443**	**P 279,745**
Segment liabilities	**P 102,294**	**P 56,554**	**P 55,433**	**P 17,617**	**P 231,898**
Other information:					
Depreciation and amortization	**P 105**	**P 54**	**P 4**	**P 188**	**P 351**
Capital expenditures	**130**	**12**	**5**	**65**	**212**
December 31, 2011					
Results of operations					
Net interest income and other income	P 4,764	P 1,768	P 7,142	P 2,867	P 16,541
Other expenses	(3,201)	(843)	(658)	(3,480)	(8,182)
Income before impairment losses and income tax	P 1,563	P 925	P 6,484	(P 613)	8,359
Impairment losses					(1,550)
Tax expense					(214)
Net income					P 6,595
Segment resources (as restated)	P 42,755	P 71,010	P 116,309	P 42,555	P 272,629
Segment liabilities (as restated)	P 110,826	P 70,551	P 34,751	P 13,662	P 229,790
Other information:					
Depreciation and amortization	P 132	P 59	P 8	P 158	P 357
Capital expenditures	64	5	3	27	99

	Consumer Banking	Corporate and Commercial Banking	Treasury	Headquarters	Total
December 31, 2010					
Results of operations					
Net interest income and other income	P 4,685	P 2,013	P 5,543	P 967	P 13,208
Other expenses	(2,831)	(794)	(751)	(2,122)	(6,498)
Income before impairment losses and income tax	P 1,854	P 1,219	P 4,792	(P 1,155)	6,710
Impairment losses					(524)
Tax expense					(833)
Net income					P 5,353
Segment resources (as restated)	P 35,252	P 63,779	P 105,667	P 49,085	P 253,783
Segment liabilities (as restated)	P 107,093	P 61,734	P 36,257	P 12,714	P 217,798
Other information:					
Depreciation and amortization	P 140	P 58	P 10	P 165	P 373
Capital expenditures	164	2	6	23	195

7. CASH AND BALANCES WITH THE BSP

These accounts are composed of the following as of December 31:

	Group		Parent	
	2012	2011	**2012**	2011
Cash and other cash items	**P 4,242,361**	P 3,686,931	**P 4,242,324**	P 3,686,914
Due from BSP				
Mandatory reserves	**-**	16,900,000	**-**	16,900,000
Other than mandatory	**27,450,311**	11,871,881	**27,450,311**	11,871,881
	27,450,311	28,771,881	**27,450,311**	28,771,881
	P 31,692,672	P 32,458,812	**P 31,692,635**	P 32,458,795

Cash consists primarily of funds in the form of Philippine currency notes and coins in the Bank's vault and those in the possession of tellers, including ATMs. Other cash items include cash items (other than currency and coins on hand) such as checks drawn on other banks or other branches that were received after the Bank's clearing cut-off time until the close of the regular banking hours.

Mandatory reserves represent the balance of the deposit account maintained with the BSP to meet reserve requirements and to serve as clearing account for interbank claims. Due from BSP bears annual interest rates ranging from 0.3% to 4.7% in 2012, 0.1% to 4.6% in 2011 and 2.0% to 4.1% in 2010, except for the amounts within the required reserve as determined by BSP. Total interest income earned amounted to P112,025, P830,021 and P1,025,967 in 2012, 2011 and 2010, respectively, and is presented as part of Interest Income on Due from Other Banks account in the statements of income.

Cash and due from BSP are included in cash and cash equivalents for cash flow statement reporting purposes.

Under Section 254 of the Manual of Regulations for Banks (MORB), a bank is required to maintain at least 25 percent of its reserve requirement in the form of deposits with the BSP as among the allowable instruments for reserve cover. Section 254.1 of the MORB further provides that such deposit account with the BSP is not considered as a regular current account as drawings against such deposits shall be limited to: (a) settlement of obligation with the BSP, and (b) withdrawals to meet cash requirements.

8. DUE FROM OTHER BANKS

The balance of this account consists of regular deposits with the following:

	Group		Parent	
	2012	2011	**2012**	2011
Foreign banks	**P 2,675,813**	P 2,554,037	**P 2,675,813**	P 2,554,037
Local banks	**323,526**	659,703	**323,385**	659,562
	P 2,999,339	P 3,213,740	**P 2,999,198**	P 3,213,599

The breakdown of this account as to currency follows:

	Group		Parent	
	2012	2011	**2012**	2011
U.S. dollar	**P 2,054,577**	P 2,649,588	**P 2,054,577**	P 2,649,588
Philippine peso	**260,059**	183,493	**259,918**	183,352
Other currencies	**684,703**	380,659	**684,703**	380,659
	P 2,999,339	P 3,213,740	**P 2,999,198**	P 3,213,599

Annual interest rates on these deposits range from 0.00% to 1.00% in 2012 and 2011. Total interest income on Due from Other Banks amounted to P635 in 2012, P1,561 in 2011 and P1,338 in 2010, and is presented as part of Interest Income on Due from Other Banks account in the statements of income.

Due from other banks are included in cash and cash equivalents for cash flow statement reporting purposes.

9. INTERBANK LOANS RECEIVABLE

Interbank loans receivable consists of loans granted to other banks. These loans have terms ranging from one to seven days.

Significant interbank loans receivable as of December 31, 2012 and all interbank loans receivable as of December 31, 2011 are denominated in foreign currencies. The breakdown of this account as to currency (translated to Philippine peso at year-end for foreign currency denominated interbank loans) follows:

	Group and Parent	
	2012	2011
U.S. dollar	**P 5,101,113**	P 11,622,024
Australian dollar	**235,673**	201,620
Philippine peso	**100,000**	-
British pound	**66,710**	30,658
Euro	**-**	1,134,842
	P 5,503,496	P 12,989,144

Interest income earned on interbank loans amounted to P24,843 in 2012, P32,113 in 2011 and P53,336 in 2010 and is presented as Interest Income on Interbank Loans Receivable in the statements of income. Annual interest rates on interbank loans receivable range from 0.03% to 4.38% in 2012, 0.05% to 4.65% in 2011 and 0.01% to 4.50% in 2010.

10. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

This account is composed of the following as at December 31:

	Group		Parent	
	2012	2011	**2012**	2011
Derivative assets	**P 343,229**	P 225,238	**P 343,229**	P 225,238
Debt securities	**53,899**	44,877	**53,899**	44,877
Equity securities	**349**	755	**-**	-
	P 397,477	P 270,870	**P 397,128**	P 270,115

The breakdown of this account as to currency follows:

	Group		Parent	
	2012	2011	**2012**	2011
Philippine peso	**P 297,475**	P 157,282	**P 297,126**	P 156,527
U.S. dollars	**100,002**	113,588	**100,002**	113,588
	P 397,477	P 270,870	**P 397,128**	P 270,115

All financial assets at FVTPL are held for trading. Fair values of derivative assets were determined through valuation technique using the net present value computation. The fair values of debt and equity securities have been determined directly by reference to published prices quoted in active markets.

The Group recognized fair value gain on FVTPL amounting to P395,268, P111,183 and P186,060 in 2012, 2011 and 2010, respectively, in the Group and Parent Company financial statements and is included as part of Trading Gain – net account in the statements of income.

Derivative instruments include foreign currency forwards and warrants. Foreign currency forwards represent commitments to purchase/sell foreign currency on a future date at an agreed exchange rate.

The aggregate contractual or notional amount of derivative financial instruments and the total fair values of derivative financial assets and liabilities are set out below (see Note 23):

	December 31, 2012		
	Notional Amount	**Fair Values**	
		Assets	**Liabilities**
Currency forwards			
Bought	P 33,153,852	P 16,923	P 1,039,471
Sold	36,889,857	287,513	8,467
Warrants	3,694,500	38,793	-
	P 73,738,209	**P 343,229**	**P 1,047,938**

	December 31, 2011		
	Notional Amount	Fair Values	
		Assets	Liabilities
Currency forwards			
Bought	P 14,018,995	P 141,342	P 28,366
Sold	20,359,309	42,467	130,782
Warrants	3,945,600	41,429	-
	P 38,323,904	P 225,238	P 159,148

On December 1, 2010, the Bank participated in a bond exchange program which was offered by the Philippine Government wherein owners of certain eligible bonds were allowed to exchange these old bonds for new bonds. In the exchange program, the Bank exchanged investments designated as financial assets at FVTPL with fair value of P1,109,829 for investments with fair value of P1,083,022, which were designated as AFS. The difference between the carrying amount of the bonds given up and the fair value of the new bonds of P26,807 was recognized in profit or loss under the Trading Gain – net account in the 2010 statement of income.

11. AVAILABLE-FOR-SALE FINANCIAL ASSETS

Available-for-sale financial assets consist of the following:

	Group		Parent	
	2012	2011	**2012**	2011
Government bonds	**P 30,389,526**	P 34,270,091	**P 30,389,526**	P 34,270,091
Other debt securities:				
Fixed rate treasury notes	**31,074,146**	28,938,441	**31,074,146**	28,938,441
Private bonds and commercial papers	**18,777,608**	21,135,297	**18,777,608**	21,135,297
Equity securities	**8,573,317**	5,677,918	**8,538,849**	5,648,687
	88,814,597	90,021,747	**88,780,129**	89,992,516
Allowance for impairment	**(256,321)**	(278,231)	**(256,321)**	(278,231)
	P 88,558,276	P 89,743,516	**P 88,523,808**	P 89,714,285

The breakdown of this account as to currency follows:

	Group		Parent	
	2012	2011	**2012**	2011
Philippine peso	**P 45,551,826**	P 41,114,794	**P 45,517,358**	P 41,085,563
U.S. dollar	**42,187,420**	48,571,746	**42,187,420**	48,571,746
Others	**819,030**	56,976	**819,030**	56,976
	P 88,558,276	P 89,743,516	**P 88,523,808**	P 89,714,285

Government bonds and other debt securities issued by resident and non-resident corporations earned interest at 3.8% to 12.2% per annum in 2012, 4.0% to 14.0% per annum in 2011 and 4.0% to 11.6% in 2010.

Government bonds with face value of P463,537 as of December 31, 2012 and 2011 are deposited with BSP as security for the Bank's faithful compliance with its fiduciary obligations (see Note 29).

Equity securities include unquoted equity securities consisting of club shares, preferred shares and common shares of various unlisted local companies.

Changes in AFS financial assets are as follows:

		Group		Parent	
	Notes	**2012**	2011	**2012**	2011
Balance at beginning of year		**P 89,743,516**	P 33,812,760	**P 89,714,285**	P 33,781,022
Additions		**229,461,137**	156,232,639	**229,459,630**	156,232,639
Disposals		**(226,917,123)**	(132,394,572)	**(226,830,093)**	(132,394,572)
Foreign currency revaluation	26	**(3,081,213)**	(233,933)	**(3,081,213)**	(233,935)
Fair value gains (losses)		**(652,881)**	1,861,847	**(743,641)**	1,864,356
Impairment reversal (loss)		**5,171**	(15,151)	**5,171**	(15,151)
Reclassification to loans and receivables		**(331)**	-	**(331)**	-
Reclassification from HTM investments	12	**-**	30,479,926	**-**	30,479,926
Balance at end of year		**P 88,558,276**	P 89,743,516	**P 88,523,808**	P **89,714,285**

The fair values of government bonds and quoted AFS securities (other debt and equity securities) have been determined directly by reference to quoted prices generated in active markets. For unquoted AFS equity securities included under equity securities, the fair value is not reliably determinable either by reference to similar financial instruments or through valuation technique using the net present value of the future cash flows. Accordingly, unquoted AFS equity securities are carried at cost.

The trading gain on AFS financial assets shown as part of Trading Gain – net in the statements of income amounted to P6,047,477, P5,283,060 and P2,459,513 in 2012, 2011, and 2010, respectively.

The net fair value gains (losses) on AFS financial assets directly recognized in other comprehensive income amounted to (P586,928), P1,966,880 and P752,037 in 2012, 2011 and 2010, respectively, in the Group financial statements, and (P677,688), P1,969,389 and P763,734 in 2012, 2011 and 2010, respectively, in the Parent Company financial statements.

The Group recognized impairment losses amounting to P15,151 in 2011 on its investments in equity securities whose market value had significantly declined over a long period of time. In 2012, certain investments in equity securities amounting to P1,821 were sold and the related allowance for impairment amounting to P5,171 was accordingly reversed.

The Group recognized the deterioration of the world's financial markets that occurred in the third quarter of 2008. The enormity and extent of the global credit crisis was crystallized by the substantial government programs instituted by major economies in response to the crisis, including temporary liquidity facilities, outright purchase of commercial papers and mortgaged-backed securities, guarantee of new unsecured debt issued by banks and purchase of equity stakes in financial institutions. Related to this, in 2008, the Group reclassified certain financial assets as allowed under the amended PAS 39 and PFRS 7. The Group reclassified Republic of the Philippines (ROP) bond investments with total carrying value of P14,741,578 out of the AFS category to HTM effective September 10, 2008. The fair value of the investments as of the date of reclassification is equal to the carrying amount of the investments. Total fair value loss in 2008 recognized in capital funds before reclassification amounted to P225,792. The total fair value loss of P225,792 as at date of reclassification shall remain in equity and will be amortized over the remaining maturity of the ROP bond investments using the effective interest method. Amortization of unrealized losses for the years ended December 31, 2011 and 2010 amounted to P4,121 and P10,841 (nil in 2012), respectively. In 2011, substantially all of these reclassified investments were disposed of. At December 31, 2012 and 2011, the carrying value of the reclassified investments amounted to P30 and P28, respectively, while the fair value of the investments totaled P37 and P35, respectively.

On December 1, 2010, the Bank participated in a bond exchange program which was offered by the Philippine Government wherein owners of certain eligible bonds were allowed to exchange these old bonds for new bonds. In the exchange program, the Bank exchanged investments designated at AFS with fair value of P278,987 at the date of the exchange for investments with fair value of P295,052, which were also designated as AFS. The difference between the fair value of the bonds given up and the fair value of the new bonds of P16,065 was recognized in profit or loss under the Trading Gain – net account in the 2010 statement of income.

12. HELD-TO-MATURITY INVESTMENTS

On December 1, 2010, the Bank participated in a bond exchange program which was offered by the Philippine Government wherein owners of certain eligible bonds were allowed to exchange these old bonds for new bonds maturing in 2020 and 2035. In the exchange program, the Bank exchanged HTM investments with carrying value of P1,479,429 at the date of the exchange for investments with fair value of P1,466,252, which were designated also as HTM. The difference between the carrying value of the bonds given up and the fair value of the new bonds of P13,177 will be amortized over the remaining life of the new bonds as adjustment on interest income to be earned on these investments. Effective interest rates on the new investments range from 3.80% to 8.13%. The exchange program was covered by a relief from the tainting provision of PAS 39 as allowed by BSP and SEC (see also Note 2.1). The HTM investments under this bond exchange program were fully disposed of in 2011.

In 2011, the Bank disposed of more than an insignificant amount of its HTM investments amounting to P5,716,283. The related trading gain recognized amounted to P671,690 and is presented as part of Trading Gain – net in the 2011 statement of income. Consequently, in accordance with PAS 39, the remaining HTM investments portfolio amounting to P30,479,926 was reclassified to AFS financial assets (see Note 11). In 2012, substantially all of these reclassified investments were disposed of. At December 31, 2012 and 2011, the carrying value of the reclassified investments amounted to P2,683,597 and P6,608,913 respectively, while the fair value of the investments totaled P2,777,582 and P6,903,767.

13. LOANS AND OTHER RECEIVABLES

This account consists of the following as of December 31:

	Group		Parent	
	2012	2011	**2012**	2011
Receivables from customers:				
Loans and discounts	**P 85,257,866**	P 78,306,119	**P 85,257,866**	P 78,306,119
Bills purchased	**3,078,367**	3,144,843	**3,078,367**	3,144,843
Customers' liabilities under acceptances and trust receipts	**2,788,504**	3,854,215	**2,788,504**	3,854,215
Accrued interest receivable	**516,329**	583,839	**516,329**	583,839
	91,641,066	85,889,016	**91,641,066**	85,889,016
Unearned discounts	**(139,749)**	(171,780)	**(139,749)**	(171,780)
Allowance for impairment	**(10,663,736)**	(9,149,390)	**(10,663,736)**	(9,149,390)
	80,837,581	76,567,846	**80,837,581**	76,567,846
Other receivables:				
SPURRA	**35,300,000**	25,200,000	**35,300,000**	25,200,000
Sales contracts receivable	**2,025,018**	1,137,258	**2,025,018**	1,137,258
Accounts receivable	**1,121,303**	1,114,575	**1,057,238**	1,052,120
Accrued interest receivable	**1,014,420**	1,540,703	**1,014,420**	1,540,703
Installment contracts receivable	**16,516**	20,831	**-**	-
UDSCL	**-**	22,752	**-**	22,752
	39,477,257	29,036,119	**39,396,676**	28,952,833
Allowance for impairment	**(598,249)**	(592,759)	**(595,047)**	(589,656)
	38,879,008	28,443,360	**38,801,629**	28,363,177
	P 119,716,589	P 105,011,206	**P 119,639,210**	P 104,931,023

In 2010, the Group disposed of unquoted debt securities with carrying amount of P7,371,659. Total gain recognized on the disposal amounted to P201,000 which is included under Trading Gain – net account in the 2010 statement of income.

Current banking regulations allow banks that have no unbooked valuation reserves and capital adjustments required by BSP to exclude from nonperforming classification those loans classified as loss in the latest examination of the BSP that are fully covered by allowance for credit losses, provided that interest on said receivables shall not be accrued. As of December 31, 2012 and 2011, the Bank has no unbooked valuation reserves.

As of December 31, 2012 and 2011, non-performing loans (NPLs) of the Bank as reported to the BSP, net of accounts classified as "Loss" that are 100% covered by loan loss reserves are as follows:

	Group and Parent	
	2012	2011
Gross NPLs	**P 10,200,181**	P 8,973,738
Less loans classified as "loss" with 100% reserves	**7,014,341**	6,202,687
Net NPLs	**P 3,185,840**	P 2,771,051

As of December 31, 2012 and 2011, total loan loss reserves of the Group amounted to P10,627,442 and P9,025,192, respectively. These represent the balance of the allowance for impairment on receivables from customers as of December 31, 2012 and 2011 less the allowance for impairment on accrued interest receivable of P36,294 and P124,198, respectively.

Restructured loans of the Group amounted to P1,335,840 as of December 31, 2012 and P1,319,318 as of December 31, 2011. Interest income on these restructured loans amounted to P27,683, P16,653 and P38,917 in 2012, 2011 and 2010, respectively.

The breakdown of total loans and other receivables (net of unearned discounts) as to secured, with corresponding collateral types, and unsecured loans follows:

	Group		Parent	
	2012	2011	**2012**	2011
Secured:				
Government securities	**P 36,023,304**	P 26,379,636	**P 36,023,304**	P 26,379,636
Real estate	**16,650,771**	16,826,018	**16,634,255**	16,805,187
Chattel mortgage	**6,694,793**	8,600,650	**6,694,793**	8,600,650
Deposit hold-out	**700,330**	2,575,033	**700,330**	2,575,033
Assignment of receivables	**156,378**	269,065	**156,378**	269,065
Others	**1,185,233**	1,722,010	**1,182,774**	1,722,010
	61,410,809	56,372,412	**61,391,834**	56,351,581
Unsecured	**69,567,765**	58,380,943	**69,506,159**	58,318,488
	P 130,978,574	P 114,753,355	**P 130,897,993**	P 114,670,069

The breakdown as to secured and unsecured of non-accruing loans of the Group and the Bank reported to the BSP as of December 31 follows:

	Group and Parent	
	2012	2011
Secured	**P 3,429,621**	P 2,199,022
Unsecured	**7,146,606**	7,059,907
	P 10,576,227	P 9,258,929

The maturity profile of loans and other receivables follows:

	Group		Parent	
	2012	2011	**2012**	2011
Less than one year	**P 78,839,912**	P 67,463,860	**P 78,817,738**	P 67,447,892
One year to less than five years	**27,983,938**	26,189,560	**27,932,731**	26,126,037
Beyond five years	**24,154,724**	21,099,935	**24,147,524**	21,096,140
	P 130,978,574	P 114,753,355	**P 130,897,993**	P 114,670,069

Loans and other receivables bear annual interest at the range of 1.64% to 18.37% in 2012, 2.13% to 16.00% in 2011 and 2.03% to 16.50% in 2010.

The breakdown of loans (receivable from customers excluding accrued interest receivable) as to type of interest rate follows:

	Group and Parent	
	2012	2011
Variable interest rates	**P 68,799,614**	P 63,024,694
Fixed interest rate	**22,325,123**	22,280,483
	P 91,124,737	P 85,305,177

The amounts of interest income per type of loans and receivables for each reporting period are as follows:

	Group		
	2012	2011	2010
Receivables from customers	**P 5,604,878**	P 4,997,577	P 5,341,152
Other receivables:			
SPURRA	**609,343**	1,109,447	621,265
Sales contracts receivable	**140,241**	134,613	158,800
UDSCL	**11,341**	12,652	155,396
Installment contracts receivable	**1,825**	1,889	1,939
Others	**616,426**	619,434	95,982
	P 6,984,054	P 6,875,612	P 6,374,534

	Parent		
	2012	2011	2010
Receivables from customers	**P 5,604,878**	P 4,997,385	P 5,340,911
Other receivables:			
SPURRA	**609,343**	1,109,447	621,265
Sales contracts receivable	**140,241**	134,613	158,800
UDSCL	**11,341**	12,652	155,396
Others	**616,191**	619,402	95,978
	P 6,981,994	P 6,873,499	P 6,372,350

As of December 31, 2012 and 2011, loans and discounts amounting to P19,046 and P33,618, respectively, have been assigned to BSP to secure the Bank's borrowings under BSP rediscounting privileges (see Note 21).

The movements in the allowance for impairment of loans and other receivables are summarized below (see Note 19):

	Group		Parent	
	2012	2011	**2012**	2011
Balance at beginning of year	**P 9,742,149**	P 8,683,102	**P 9,739,046**	P 8,680,016
Impairment losses during the year	**1,559,839**	1,410,515	**1,559,839**	1,410,515
Other adjustments/transfers	**(40,003)**	(351,468)	**(40,102)**	(351,485)
Balance at end of year	**P 11,261,985**	P 9,742,149	**P 11,258,783**	P 9,739,046

14. INVESTMENTS IN SUBSIDIARIES

This account in the Parent Company financial statements pertains to the Bank's investments in the following subsidiaries which are carried at cost:

	% Interest Held	Parent 2012	Parent 2011
UPI	100%	**P 624,861**	P 624,861
UBPSI	100%	**5,000**	5,000
UDC	100%	**3,125**	3,125
UBPIBI	100%	**2,500**	2,500
UCBC	100%	**1,000**	1,000
		P 636,486	P 636,486

The Bank is the ultimate parent company of UPI's wholly-owned subsidiaries, FUPI and FUDC. No equity investment account is reflected in the Bank's 2012 and 2011 separate financial statements for FUPI and FUDC since UPI's investments in these subsidiaries were already eliminated at consolidation level for UPI. Other subsidiaries of the Bank are dormant. IVCC was not included in the consolidation due to immateriality of its account balances.

The following table presents financial information for UPI, FUPI and FUDC as of and for the years ended December 31, 2012 and 2011:

	Assets	Liabilities	Revenues	Net Profit (Loss)
2012				
UPI	P 463,142	P 9,417	P 17,462	(P 18,427)
FUPI	4,060,213	3,526,449	1,567,684	133,636
FUDC	7,159	1,413	7,779	2,418
2011				
UPI	P 471,830	P 5,689	P 12,513	(P 9,086)
FUPI	2,550,035	2,178,195	1,624,088	194,940
FUDC	6,744	3,415	8,740	4,113

The Bank also has investments in certain SPCs. These SPCs were established primarily to manage certain investment properties of the Bank. In the Group and Parent Company financial statements, these SPCs are consolidated through the Investment Properties account instead of equity investments even if the Bank acquired the shares of stock of the SPCs and not the investment properties themselves.

15. BANK PREMISES, FURNITURE, FIXTURES AND EQUIPMENT

The gross carrying amounts and accumulated depreciation and amortization of bank premises, furniture, fixtures and equipment at the beginning and end of 2012 and 2011 are shown below.

Group

	Land	Buildings	Furniture, Fixtures and Equipment	Leasehold Rights and Improvements	Total
December 31, 2012					
Cost	P 533,737	P 2,134,496	P 1,819,766	P 820,969	P 5,308,968
Accumulated depreciation and amortization	-	(294,344)	(1,234,483)	(674,351)	(2,203,178)
Net carrying amount	**P 533,737**	**P 1,840,152**	**P 585,283**	**P 146,618**	**P 3,105,790**
December 31, 2011					
Cost	P 245,216	P 2,056,188	P 1,956,576	P 781,644	P 5,039,624
Accumulated depreciation and amortization	-	(273,954)	(1,378,822)	(617,282)	(2,270,058)
Net carrying amount	P 245,216	P 1,782,234	P 577,754	P 164,362	P 2,769,566
January 1, 2011					
Cost	P 477,615	P 1,865,951	P 1,825,908	P 759,542	P 4,929,016
Accumulated depreciation and amortization	-	(243,072)	(1,263,667)	(559,667)	(2,066,406)
Net carrying amount	P 477,615	P 1,622,879	P 562,241	P 199,875	P 2,862,610

Parent

	Land	Buildings	Furniture, Fixtures and Equipment	Leasehold Rights and Improvements	Total
December 31, 2012					
Cost	P 533,737	P 2,134,496	P 1,804,221	P 818,127	P 5,290,581
Accumulated depreciation and amortization	-	(294,344)	(1,220,291)	(671,509)	(2,186,144)
Net carrying amount	**P 533,737**	**P 1,840,152**	**P 583,930**	**P 146,618**	**P 3,104,437**
December 31, 2011					
Cost	P 245,216	P 2,056,188	P 1,941,177	P 781,639	P 5,024,220
Accumulated depreciation and amortization	-	(273,954)	(1,365,225)	(617,277)	(2,256,456)
Net carrying amount	P 245,216	P 1,782,234	P 575,952	P 164,362	P 2,767,764
January 1, 2011					
Cost	P 477,615	P 1,865,951	P 1,810,631	P 756,700	P 4,910,897
Accumulated depreciation and amortization	-	(243,072)	(1,250,690)	(556,830)	(2,050,592)
Net carrying amount	P 477,615	P 1,622,879	P 559,941	P 199,870	P 2,860,305

A reconciliation of the carrying amounts at the beginning and end of 2012 and 2011 of bank premises, furniture, fixtures and equipment is shown below.

Group

	Land	Buildings	Furniture, Fixtures and Equipment	Leasehold Rights and Improvements	Total
Balance at January 1, 2012, net of accumulated depreciation and amortization	P 245,216	P 1,782,234	P 577,754	P 164,362	P 2,769,566
Additions	220,660	217,643	224,296	48,151	710,750
Disposals	(50,115)	(87,853)	(290,205)	-	(428,173)
Reclassifications/ adjustments	117,976	(30,062)	235,061	(11,663)	311,312
Depreciation and amortization charges for the year	-	(41,810)	(161,623)	(54,232)	(257,665)
Balance at December 31, 2012, net of accumulated depreciation and amortization	**P 533,737**	**P 1,840,152**	**P 585,283**	**P 146,618**	**P 3,105,790**
Balance at January 1, 2011, net of accumulated depreciation and amortization	P 477,615	P 1,622,879	P 562,241	P 199,875	P 2,862,610
Additions	-	222,566	202,696	57,929	483,191
Disposals	(109,485)	(28,399)	(19,568)	-	(157,452)
Reclassifications/ adjustments	(122,914)	3,489	(6,683)	(31,925)	(158,033)
Depreciation and amortization charges for the year	-	(38,301)	(160,932)	(61,517)	(260,750)
Balance at December 31, 2011, net of accumulated depreciation and amortization	P 245,216	P 1,782,234	P 577,754	P 164,362	P 2,769,566

Parent

	Land	Buildings	Furniture, Fixtures and Equipment	Leasehold Rights and Improvements	Total
Balance at January 1, 2012, net of accumulated depreciation and amortization	P 245,216	P 1,782,234	P 575,952	P 164,362	P 2,767,764
Additions	220,660	217,643	224,151	48,151	710,605
Disposals	(50,115)	(87,853)	(290,205)	-	(428,173)
Reclassifications/ adjustments	117,976	(30,062)	235,061	(11,663)	311,312
Depreciation and amortization charges for the year	-	(41,810)	(161,029)	(54,232)	(257,071)
Balance at December 31, 2012, net of accumulated depreciation and amortization	**P 533,737**	**P 1,840,152**	**P 583,930**	**P 146,618**	**P 3,104,437**
Balance at January 1, 2011, net of accumulated depreciation and amortization	P 477,615	P 1,622,879	P 559,941	P 199,870	P 2,860,305
Additions	-	222,566	202,574	57,929	483,069
Disposals	(109,485)	(28,399)	(19,568)	-	(157,452)
Reclassifications/ adjustments	(122,914)	3,489	(6,683)	(31,925)	(158,033)
Depreciation and amortization charges for the year	-	(38,301)	(160,312)	(61,512)	(260,125)
Balance at December 31, 2011, net of accumulated depreciation and amortization	P 245,216	P 1,782,234	P 575,952	P 164,362	P 2,767,764

Under BSP rules, investments in bank premises, furniture, fixtures and equipment should not exceed 50% of the Bank's unimpaired capital. As of December 31, 2012 and 2011, the Bank has satisfactorily complied with this requirement.

16. INVESTMENT PROPERTIES

The Group's investment properties include several parcels of land and buildings held for capital appreciation and are stated at fair value. Investment properties are revalued at every year-end, as determined by independent appraisal companies accredited by the BSP. The breakdown of this account as to type follows:

	Group		Parent	
	2012	2011	**2012**	2011
Land	**P 7,884,895**	P 8,568,605	**P 7,884,895**	P 8,568,605
Building	**1,891,863**	1,982,946	**1,891,863**	1,982,946
Land improvements	**1,778,318**	1,615,418	**1,514,230**	1,344,617
	P 11,555,076	P 12,166,969	**P 11,290,988**	P 11,896,168

The net fair value gains and losses from investment properties account is presented under Miscellaneous Income account in the statements of income (see Note 26.1). Real property taxes related to these investment properties paid by the Group and recognized as expense for the years ended December 31, 2012, 2011 and 2010 totaled P15,091, P11,427 and P16,396, respectively, and are included as part of Taxes and Licenses account in the statements of income [see Note 35.1(d)].

The changes in this account can be summarized as follows:

	Group		Parent	
	2012	2011	**2012**	2011
Balance at beginning of year	**P 12,166,969**	P 12,382,162	**P 11,896,168**	P 12,109,192
Additions	**586,070**	496,998	**586,070**	496,998
Fair value gains	**379,873**	44,476	**379,873**	44,476
Reclassification to bank premises, furniture, fixtures and equipment (see Note 15)	**(422,658)**	(228,362)	**(422,658)**	(228,362)
Disposals	**(161,935)**	(251,437)	**(161,935)**	(249,410)
Transfers to sales contracts receivable	**(1,038,988)**	(277,739)	**(1,032,275)**	(277,597)
Rescinded sales	**45,745**	871	**45,745**	871
Balance at end of year	**P 11,555,076**	P 12,166,969	**P 11,290,988**	P 11,896,168

Rent income earned by the Group on its investment properties under operating leases amounted to P108,108, P122,100 and P76,726 in 2012, 2011 and 2010, respectively, while rent income earned by the Parent Company on these investment properties amounted to P103,418, P119,772 and P77,704 in 2012, 2011 and 2010, respectively, and is included as part of Rental account under Miscellaneous Income in the statements of income (see Note 26.1).

17. ASSETS HELD FOR SALE

The balance of this account as of December 31, 2012 and 2011 pertains mainly to chattel and other personal properties that are expected to be sold within one year from the end of the reporting periods.

18. OTHER RESOURCES

The composition of Other Resources account as of December 31 follows:

	Group		Parent	
	2012	2011 (As Restated - see Note 2.1)	2012	2011
Trust fund assets	P 3,886,730	P 2,443,067	P -	P -
Deferred tax assets – net (see Note 28.1)	2,848,912	2,478,602	2,848,933	2,480,325
Returned checks and other cash items	289,070	36,548	289,070	36,548
Computer software – net	258,023	253,879	258,023	253,879
Sundry debits	126,436	162,971	126,436	162,971
Prepaid expenses	70,737	61,847	67,115	57,547
Retirement benefit asset (see Note 27.2)	29,585	34,636	27,622	32,160
Documentary stamps and other supplies on hand	15,888	31,808	15,888	31,808
Miscellaneous – net	566,036	576,342	543,233	549,492
	8,091,417	6,079,700	4,176,320	3,604,730
Allowance for impairment	(159,503)	(159,565)	(141,804)	(141,867)
	P 7,931,914	P 5,920,135	P 4,034,516	P 3,462,863

In 2012, the Group restated its 2011 and 2010 consolidated financial statements to appropriately recognize the trust fund assets of FUPI that were inadvertently offset against deposit liabilities in the consolidation for those years. The restatement resulted to the increase in the previously reported balances of the Other Resources and the Deposit Liabilities – Savings accounts of the Group by P2,443,067 and P783,503 as of December 31, 2011 and 2010, respectively. The restatement has no effect on the previously reported capital funds of the Group as of December 31, 2011 and 2010, and on the Group's reported net income and, basic and diluted earnings per share for the years then ended. The restatement has also no effect on the previously reported financial statements of the Parent Company as of December 31, 2011 and 2010 and for the years then ended.

The trust fund assets of FUPI consisted of the following as of December 31, 2012 and 2011:

	Group	
	2012	2011
Assets:		
Investments in:		
Debt securities	P 2,695,863	P 1,600,357
Equity securities	761,448	227,579
Unit investment trust fund	367,685	201,654
Accrued interest and other assets	72,051	424,182
	3,897,047	2,453,772
Liabilities	(10,317)	(10,705)
	P 3,886,730	P 2,443,067

Miscellaneous other resources include foreclosed machineries with carrying amount of P238,621 and P285,908 as of December 31, 2012 and 2011, respectively. Depreciation expense recognized by the Group and the Parent for these machineries amounted to P47,287 in 2012, P48,083 in both 2011 and 2010, and is included as part of Depreciation and Amortization account in the statements of income.

The movements in the Computer Software account follow:

	Group and Parent	
	2012	2011
Balance at beginning of year	**P 253,879**	P 250,763
Additions	**50,852**	52,041
Reclassifications	**(173)**	7
Amortization charges for the year	**(46,535)**	(48,932)
Balance at end of year	**P 258,023**	P 253,879

19. ALLOWANCE FOR IMPAIRMENT

Movements in the allowance for impairment are shown below:

		Group		Parent	
	Notes	**2012**	2011	**2012**	2011
Balance at beginning of year:					
AFS financial assets	11	**P 278,231**	P 40	**P 278,231**	P 40
HTM investments	12	**-**	263,040	**-**	263,040
Loans and other receivables	13	**9,742,149**	8,683,102	**9,739,046**	8,680,016
Other resources	18	**159,565**	36,581	**141,867**	18,882
		10,179,945	8,982,763	**10,159,144**	8,961,978
Movements during the year:					
Provision for impairment	11, 13 17, 18	**1,559,839**	1,549,552	**1,559,839**	1,549,552
Write-off/sale		**-**	(325,868)	**-**	(325,868)
Adjustments/ reclassifications		**(61,975)**	(26,502)	**(62,075)**	(26,518)
		1,497,864	1,197,182	**1,497,764**	1,197,166
Balance at end of year:					
AFS financial assets	11	**256,321**	278,231	**256,321**	278,231
Loans and other receivables	13	**11,261,985**	9,742,149	**11,258,783**	9,739,046
Other resources	18	**159,503**	159,565	**141,804**	141,867
		P 11,677,809	P 10,179,945	**P 11,656,908**	P 10,159,144

With the foregoing level of allowance for impairment and credit losses, management believes that the Group has sufficient allowance for any losses that the Group may incur from the noncollection or nonrealization of its receivables and other risk assets.

Reconciliation of the allowance for impairment by class follows:

Group

	2012											
	Loans and Receivables											
	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Balance at beginning of year	P 4,021,796	P 855,672	P 4,059,118	P 583,803	P 131,943	P 1,211	P 88,606	P 9,742,149	P 278,231	P -	P 159,565	P 10,179,945
Provision during the year	-	365,633	1,265,364	13,636	(86,727)	-	1,933	1,559,839	-	-	-	1,559,839
Other adjustments	153,834	(201,725)	-	(7,653)	(1,670)	-	17,211	(40,003)	(21,910)	-	(62)	(61,975)
Balance at end of year	**P 4,175,630**	**P 1,019,580**	**P 5,324,482**	**P 589,786**	**P 43,546**	**P 1,211**	**P 107,750**	**P 11,261,985**	**P 256,321**	**P -**	**P 159,503**	**P 11,677,809**

* *Corporate includes accounts under Asset Recovery Group. Other loan accounts includes Bills Purchase, Branch Loans, HR Loans and Salary Loans.*

Impairment at end of year broken down as to individual and collective assessment:

	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Individual impairment	P 3,426,871	P 748,616	P 3,835,003	P 589,786	P 43,546	P 1,211	P 76,156	P 8,721,189	P 256,321	P -	P 159,503	P 9,137,013
Collective impairment	748,759	270,964	1,489,479	-	-	-	31,594	2,540,796	-	-	-	2,540,796
	P 4,175,630	**P 1,019,580**	**P 5,324,482**	**P 589,786**	**P 43,546**	**P 1,211**	**P 107,750**	**P 11,261,985**	**P 256,321**	**P -**	**P 159,503**	**P 11,677,809**

Parent

	2012											
	Loans and Receivables											
	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Balance at beginning of year	P 4,021,796	P 855,672	P 4,059,118	P 581,911	P 131,943	P -	P 88,606	P 9,739,046	P 278,231	P -	P 141,867	P 10,159,144
Provision during the year	-	365,633	1,265,364	13,636	(86,727)	-	1,933	1,559,839	-	-	-	1,559,839
Other adjustments	153,834	(201,725)	-	(7,752)	(1,670)	-	17,211	(40,102)	(21,910)	-	(63)	(62,075)
Balance at end of year	**P 4,175,630**	**P 1,019,580**	**P 5,324,482**	**P 587,795**	**P 43,546**	**P -**	**P 107,750**	**P 11,258,783**	**P 256,321**	**P -**	**P 141,804**	**P 11,656,908**

* *Corporate includes accounts under Asset Recovery Group. Other loan accounts includes Bills Purchase, Branch Loans, HR Loans and Salary Loans.*

Impairment at end of year broken down as to individual and collective assessment:

	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Individual impairment	P 3,426,871	P 748,616	P 3,835,003	P 587,795	P 43,546	P -	P 76,156	P 8,717,987	P 256,321	P -	P 141,804	P 9,116,112
Collective impairment	748,759	270,964	1,489,479	-	-	-	31,594	2,540,796	-	-	-	2,540,796
	P 4,175,630	**P 1,019,580**	**P 5,324,482**	**P 587,795**	**P 43,546**	**P -**	**P 107,750**	**P 11,258,783**	**P 256,321**	**P -**	**P 141,804**	**P 11,656,908**

Group

	2011											
	Loans and Receivables											
	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Balance at beginning of year	P 4,179,902	P 515,603	P 3,323,794	P 523,793	P 56,010	P 1,211	P 82,789	P 8,683,102	P 40	P 263,040	P 36,581	P 8,982,763
Provision during the year	110,743	412,554	730,574	79,897	75,921	-	826	1,410,515	15,151	-	123,886	1,549,552
Other adjustments	(268,849)	(72,485)	4,750	(19,887)	12	-	4,991	(351,468)	263,040	(263,040)	(902)	(352,370)
Balance at end of year	P 4,021,796	P 855,672	P 4,059,118	P 583,803	P 131,943	P 1,211	P 88,606	P 9,742,149	P 278,231	P -	P 159,565	P 10,179,945

** Corporate includes accounts under Asset Recovery Group. Other loan accounts includes Bills Purchased, Branch Loans, HR Loans and Salary Loans.*

Impairment at end of year broken down as to individual and collective assessment:

	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Individual impairment	P 3,202,805	P 344,717	P 3,442,939	P 583,803	P 131,943	P 1,211	P 75,260	P 7,782,678	P 278,231	P -	P 159,565	P 8,220,474
Collective impairment	818,991	510,955	616,179	-	-	-	13,346	1,959,471	-	-	-	1,959,471
	P 4,021,796	P 855,672	P 4,059,118	P 583,803	P 131,943	P 1,211	P 88,606	P 9,742,149	P 278,231	P -	P 159,565	P 10,179,945

Parent

	2011											
	Loans and Receivables											
	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Balance at beginning of year	P 4,179,902	P 515,603	P 3,323,794	P 521,918	P 56,010	P -	P 82,789	P 8,680,016	P 40	P 263,040	P 18,882	P 8,961,978
Provision during the year	110,743	412,554	730,574	79,897	75,921	-	826	1,410,515	15,151	-	123,886	1,549,552
Other adjustments	(268,849)	(72,485)	4,750	(19,904)	12	-	4,991	(351,485)	263,040	(263,040)	(901)	(352,386)
Balance at end of year	P 4,021,796	P 855,672	P 4,059,118	P 581,911	P 131,943	P -	P 88,606	P 9,739,046	P 278,231	P -	P 141,867	P 10,159,144

** Corporate includes accounts under Asset Recovery Group. Other loan accounts includes Bills Purchased, Branch Loans, HR Loans and Salary Loans.*

Impairment at end of year broken down as to individual and collective assessment:

	Corporate *	Commercial	Consumer	Accounts Receivable	Accrued Interest Receivable	Sales and Installment Contract Receivable	Other Loan Accounts	Total	AFS Financial Assets	HTM Investments	Other Resources and Assets Held for Sale	Total
Individual impairment	P 3,202,805	P 344,717	P 3,442,939	P 581,911	P 131,943	P -	P 75,260	P 7,779,575	P 278,231	P -	P 141,867	P 8,199,673
Collective impairment	818,991	510,955	616,179	-	-	-	13,346	1,959,471	-	-	-	1,959,471
	P 4,021,796	P 855,672	P 4,059,118	P 581,911	P 131,943	P -	P 88,606	P 9,739,046	P 278,231	P -	P 141,867	P 10,159,144

20. DEPOSIT LIABILITIES

The breakdown of deposit liabilities account follows:

	Group		Parent	
	2012	2011 (As Restated - see Note 2.1)	**2012**	2011
Due to banks:				
Demand	**P 559,518**	P 260,604	**P 559,518**	P 260,604
Savings	**251,909**	232,922	**251,909**	232,922
Time	**1,363,449**	917,345	**1,363,449**	917,345
	2,174,876	1,410,871	**2,174,876**	1,410,871
Due to customers:				
Demand	**62,252,209**	114,491,693	**62,322,153**	114,608,177
Savings	**23,616,803**	22,288,975	**23,726,819**	22,288,984
Time	**101,797,469**	68,461,805	**101,797,469**	68,461,805
	187,666,481	205,242,473	**187,846,441**	205,358,966
	P 189,841,357	P 206,653,344	**P 190,021,317**	P 206,769,837

The breakdown of deposit liabilities account as to currency follows:

	Group		Parent	
	2012	2011 (As Restated - see Note 2.1)	**2012**	2011
Philippine peso	**P 150,782,495**	P 144,808,048	**P 150,962,455**	P 144,924,541
Foreign currency	**39,058,862**	61,845,296	**39,058,862**	61,845,296
	P 189,841,357	P 206,653,344	**P 190,021,317**	P 206,769,837

The maturity profile of this account is presented below:

	Group		Parent	
	2012	2011 (As Restated - see Note 2.1)	**2012**	2011
Less than one year	**P 189,558,514**	P 206,365,601	**P 189,738,474**	P 206,482,094
One to five years	**80,790**	132,369	**80,790**	132,369
Beyond five years	**202,053**	155,374	**202,053**	155,374
	P 189,841,357	P 206,653,344	**P 190,021,317**	P 206,769,837

Deposit liabilities bear annual interest at rates ranging from 0.0% to 3.0% in 2012, 0.0% to 4.0% in 2011 and 0.0% to 4.0% in 2010. Demand and savings deposits usually have either fixed or variable interest rates while time deposits have fixed interest rates.

Under existing BSP regulations, non-FCDU deposit liabilities of the Bank are subject to liquidity reserve equivalent to 11.0% and statutory reserve equivalent to 8.0% from November 14, 2008 to June 23, 2011 (under BSP Circular 632), and liquidity reserve equivalent to 11.0% and statutory reserve equivalent to 9.0% from June 24, 2011 to August 4, 2011 (under BSP Circular 726), and liquidity reserve equivalent to 11.0% and statutory reserve equivalent to 10.0% from August 5, 2011 to April 5, 2012 (under BSP Circular 732) and unified reserve requirement equivalent to 18.0% from April 6, 2012 and thereafter (under BSP Circular 753). As of December 31, 2012 and 2011, the Group is in compliance with such regulations.

Liquidity and statutory reserves as of December 31, 2012 and 2011 are as follows:

	Group and Parent	
	2012	2011
Cash and other cash items	**P -**	P 3,655,846
Due from BSP	**27,436,437**	28,722,311
	P 27,436,437	P 32,378,157

21. BILLS PAYABLE

Bills payable consist of borrowings from:

	Group		Parent	
	2012	2011	**2012**	2011
Banks, other financial institutions and individuals	**P 18,388,125**	P 5,423,279	**P 18,388,125**	P 5,423,279
BSP	**19,046**	33,618	**19,046**	33,618
Others	**134,096**	162,347	**133,596**	161,847
	P 18,541,267	P 5,619,244	**P 18,540,767**	P 5,618,744

Bills payable to banks and other financial institutions consist mainly of amortized cost balance of short-term borrowings.

Bills payable to BSP mainly represent short-term borrowings availed of under the rediscounting facility of the BSP. These are collateralized by eligible loans (see Note 13).

The breakdown of bills payable as to currency follows:

	Group		Parent	
	2012	2011	**2012**	2011
Foreign currency	**P 18,388,126**	P 5,437,851	**P 18,388,126**	P 5,437,851
Philippine peso	**153,141**	181,393	**152,641**	180,893
	P 18,541,267	P 5,619,244	**P 18,540,767**	P 5,618,744

The breakdown of interest expense on bills payable follow:

	Group and Parent					
	2012		2011		2010	
Banks, other financial institutions and individuals	**P**	**78,845**	P	30,923	P	12,981
BSP		**106**		75		7,284
Others		**14,167**		17,012		20,245
	P	**93,118**	P	48,010	P	40,510

The range of interest rates of bills payable per currency follows:

	Group and Parent		
	2012	2011	2010
Philippine peso	**3.6% to 12.0%**	5.0% to 12.0%	1.8% to 12.0%
Foreign currency	**0.2% to 1.8%**	0.2% to 2.5%	0.1% to 2.3%

22. NOTES PAYABLE

The Group's notes payable as of December 31, 2010 of P5,037,100 pertain to the outstanding balance of unsecured subordinated notes (the Notes), of which P3,750,000 was issued by the Group on October 14, 2009 due on October 14, 2019 and callable on October 15, 2014; and P1,287,100 was issued by the former iBank on March 23, 2006 due on September 24, 2016 and callable on September 26, 2011. On July 22, 2011, the BOD approved to exercise the call option on the latter unsecured subordinated note. Accordingly, on the call option date of September 26, 2011, the Bank exercised the option and redeemed the outstanding note from noteholders. Consequently, the balance of the Notes as of December 31, 2012 and 2011 amounted to P3,750,000. No gain or loss was recognized on the transaction.

Among the significant terms and conditions of the Notes follow:

(a) The Notes were issued on the initial issue date at 100% of the face value of the Notes. Subsequent issuance of the Notes, if any, will be issued at par, discount or premium depending on market conditions at the time of its issuance (and will include a price adjustment for interest accrued as of the initial issue date) based on a formula to be uniformly applied per tranche;

(b) The Notes shall not be used as collateral for any loan made by the Parent Company or any of its subsidiaries and affiliates. The Noteholders or their transferees shall not be allowed, and waive their right to set-off any amount that may be due the Parent Company;

(c) The Notes constitute direct, unconditional, unsecured and subordinated obligations of the Parent Company. Claims of Noteholders in respect of the Notes shall at all times rank pari passu and without any preference among themselves; and,

(d) The Notes shall not be redeemable or terminable at the instance of the Noteholders before the maturity date, unless otherwise expressly provided therein.

The P3,750,000 Notes bear interest at the rate of 7.375% per annum payable quarterly in arrears to the Noteholders on October 14, January 14, April 14, and July 14 of each year, with the first interest payment date on January 14, 2010 for the period from and including the issue date up to but excluding the first banking day of the 21st interest period (if the call option is not exercised) or the call option date (if the call option is exercised). The interest rate from and including October 14, 2014 up to but excluding October 14, 2019 will be reset and such step-up interest rate shall be payable to the Noteholders beginning on the 21st interest period up to the last interest period in the event that the Parent Company does not exercise the call option.

On the other hand, the P1,287,100 Notes bore interest at the rate of 9.5% per annum payable semi-annually in arrears to the noteholders on September 23 and March 23 of each year, with the first interest payment date on September 23, 2006 for the period from and including the issue date up to but excluding the last day of the 11th interest period (if the call option was not exercised) or the call option date (if the call option was exercised).

Interest expense on notes payable amounted to P276,562 in 2012, P366,693 in 2011 and P400,535 in 2010 and is included under Interest Expense on Bills Payable and Other Liabilities account in the statements of income.

23. OTHER LIABILITIES

Other liabilities consist of the following as of December 31:

	Group		Parent	
	2012	2011	**2012**	2011
Manager's checks	**P 5,067,041**	P 3,460,884	**P 5,067,041**	P 3,460,884
Pre-need reserve	**3,523,329**	2,132,842	**-**	-
Due to Treasurer of the Philippines	**3,071,036**	1,038,123	**3,071,036**	1,038,123
Domestic bills purchased	**2,975,895**	3,031,209	**2,975,895**	3,031,209
Accrued taxes and other expenses	**1,925,004**	1,902,221	**1,918,325**	1,894,905
Accounts payable	**1,374,027**	1,217,155	**1,373,146**	1,215,352
Derivative liabilities (see Note 10)	**1,047,938**	159,148	**1,047,938**	159,148
Other dormant credits	**372,700**	333,676	**372,700**	333,676
Payment orders payable	**193,315**	56,454	**193,315**	56,454
Withholding taxes payable	**64,740**	80,890	**64,105**	80,213
Miscellaneous	**150,094**	354,712	**322,658**	429,278
	P 19,765,119	P 13,767,314	**P 16,406,159**	P 11,699,242

The breakdown of Accrued taxes and other expenses account follows:

	Group				Parent			
	2012		2011		**2012**		2011	
Accrued interest payable	**P**	**310,199**	P	431,381	**P**	**310,101**	P	431,282
Accrued sick leave benefits		**198,887**		165,787		**196,879**		165,662
Accrued income and other taxes		**103,047**		584,266		**101,648**		581,247
Other accruals		**1,312,871**		720,787		**1,309,697**		716,714
	P	**1,925,004**	P	1,902,221	**P**	**1,918,325**	P	1,894,905

Other accruals represent mainly fringe and other Bank personnel benefits.

24. CAPITAL FUNDS

24.1 Common Stock

The authorized capital stock of the Bank is at P6,700,000 divided into 670 million shares. The Bank's outstanding common stock as of December 31, 2012 and 2011 of P6,414,224 consists of 641.4 million shares with P10 par value.

On June 29, 1992, the Bank was originally listed with then Makati Stock Exchange, now PSE. A total of 89.7 million shares were issued at an issue price of P22.50. As of December 31, 2012 and 2011, there are 641.4 million shares listed at the PSE. The number of holders and the closing price of the said shares is 5,353 and P112.70 per share in 2012, respectively, and 5,526 and P66 per share in 2011, respectively.

24.2 Surplus Free

The following is a summary of the dividends declared and distributed by the Group in 2012, 2011 and 2010:

Date of Declaration	Date of Record	Date of BSP Approval	Date of Payment	Dividend per Share		Shares Outstanding	Total Amount	
January 27, 2012	March 13, 2012	February 27, 2012	April 11, 2012	P	3.00	641,422,420	P	1,924,267
January 28, 2011	April 8, 2011	March 16, 2011	May 6, 2011		2.50	641,422,420		1,603,556
January 22, 2010	May 11, 2010	April 14, 2010	June 4, 2010		2.20	641,422,420		1,411,129

In compliance with BSP regulations, the Bank ensures that adequate reserves are in place for future bank expansion requirements. The foregoing cash dividend declarations were made within the BSP's allowable limit of dividends.

24.3 Capital Allocation

The allocation of capital between specific operations and activities is, to a large extent, driven by optimization of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital, but in some cases the regulatory requirements do not reflect fully the varying degree of risk associated with different activities. In such cases the capital requirements may be flexed to reflect differing risk profiles subject to the overall level of capital to support a particular operation or activity not falling below the minimum required for regulatory purposes. The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation and is subject to review by the ALCO.

Although maximization of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Bank to particular operations or activities, it is not the sole basis used for decision making. Also taken into considerations are synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Bank's longer term strategic objectives. The Bank's policies in respect of capital management and allocation are reviewed regularly by its BOD.

25. SERVICE CHARGES, FEES AND COMMISSIONS

This account is broken down as follows:

	Group		
	2012	2011	2010
Service charges	**P 577,776**	P 560,483	P 557,306
Bank commissions	**215,904**	208,207	122,941
Others	**67,952**	77,894	1,899
	P 861,632	P 846,584	P 682,146

	Parent		
	2012	2011	2010
Service charges	**P 577,776**	P 560,483	P 557,306
Bank commissions	**210,497**	203,207	122,321
Others	**66,087**	76,601	1,697
	P 854,360	P 840,291	P 681,324

26. MISCELLANEOUS INCOME AND EXPENSES

26.1 Miscellaneous Income

Miscellaneous income is composed of the following:

	Notes	Group 2012	Group 2011	Group 2010
Dividend		**P 522,880**	P 496,662	P 463,388
Income from trust operations	29	**473,114**	375,689	105,087
Fair value gains on investment properties – net	16	**379,873**	44,476	118,737
Foreign exchange gains – net	10, 11, 12, 13	**270,931**	378,587	823,849
Penalties		**203,640**	136,465	379,070
Gain (loss) from sale of assets		**129,428**	131,933	(48,132)
Rental	16, 33	**113,876**	128,424	83,160
Gains from acquisition of investment properties		**26,803**	29,239	74,947
Others		**132,844**	201,153	319,192
		P 2,253,389	P 1,922,628	P 2,319,298

	Notes	Parent 2012	Parent 2011	Parent 2010
Dividend		**P 520,737**	P 491,792	P 458,842
Fair value gains on investment properties	16	**379,873**	44,476	118,737
Foreign exchange gains – net	10, 11, 12, 13	**270,931**	378,587	823,849
Penalties		**203,640**	136,465	379,070
Income from trust operations	29	**154,230**	140,107	105,138
Gain (loss) from sale of assets		**129,428**	131,933	(48,132)
Rental	16, 33	**109,186**	126,096	84,138
Gains from acquisition of investment properties		**26,803**	29,239	74,947
Others		**64,238**	127,737	167,930
		P 1,859,066	P 1,606,432	P 2,164,519

26.2 Miscellaneous Expenses

The breakdown of miscellaneous expenses follows:

	Group		
	2012	2011	2010
Insurance	**P 390,600**	P 439,354	P 443,970
Outside services	**284,934**	324,678	324,678
Repairs and maintenance	**210,017**	226,791	207,047
Management and professional fees	**200,879**	237,566	281,083
Litigation	**136,596**	132,426	101,639
Communication	**130,785**	162,094	142,782
Stationery and supplies	**88,464**	78,576	79,666
Supervision fees	**77,764**	55,095	76,885
Transportation and travel	**53,495**	85,074	29,172
Representation and entertainment	**48,666**	76,640	112,269
Advertising and publicity	**41,603**	28,205	29,519
Others	**629,161**	339,003	276,755
	P 2,292,964	P 2,185,502	P 2,105,465

	Parent		
	2012	2011	2010
Insurance	**P 383,230**	P 425,792	P 441,831
Outside services	**284,056**	323,793	323,833
Repairs and maintenance	**209,352**	225,627	205,616
Management and professional fees	**195,214**	237,602	281,471
Litigation	**136,596**	132,426	101,639
Communication	**130,136**	161,520	142,309
Stationery and supplies	**87,964**	77,969	79,154
Supervision fees	**77,764**	55,095	76,885
Transportation and travel	**52,922**	66,031	27,947
Representation and entertainment	**46,278**	74,199	111,129
Advertising and publicity	**41,549**	28,162	29,478
Others	**315,500**	185,062	238,360
	P 1,960,561	P 1,993,278	P 2,059,652

27. SALARIES AND EMPLOYEE BENEFITS

27.1 Salaries and Employee Benefits Expense

Expenses recognized for employee benefits are as follows:

	Group		
	2012	2011	2010
Salaries and wages	**P 1,607,900**	P 1,368,881	P 1,097,127
Bonuses	**672,778**	643,735	492,181
Fringe benefits	**659,700**	599,443	542,858
Post-employment benefits	**237,012**	222,389	197,048
Social security costs	**52,300**	50,744	46,212
Other benefits	**74,373**	73,400	76,320
	P 3,304,063	P 2,958,592	P 2,451,746

	Parent		
	2012	2011	2010
Salaries and wages	**P 1,590,081**	P 1,355,876	P 1,085,772
Bonuses	**666,699**	641,010	489,947
Fringe benefits	**659,700**	599,443	542,858
Post-employment benefits	**236,499**	221,862	196,188
Social security costs	**51,839**	50,281	45,762
Other benefits	**74,553**	73,363	76,977
	P 3,279,371	P 2,941,835	P 2,437,504

27.2 Post-employment Benefits

The Group maintains a tax-qualified, noncontributory pension plan that is being administered by the Bank's Trust and Investment Services Group (TISG) covering all regular full-time employees. Under this pension plan, all covered employees are entitled to cash benefits after satisfying certain age and service requirements. Actuarial valuations are made annually to update the post-employment benefit costs and the amount of contributions.

The Bank maintains two separate retirement plans for UnionBank and former iBank employees, hence, the Bank presents pension information in its financial statements separately for the two plans.

The amounts of retirement benefit asset (liability for UnionBank plan) recognized are determined as follows (see Note 18):

	Group		
	2012	2011	2010
Present value of the obligation	**P 2,439,865**	P 2,047,411	P 1,786,914
Fair value of plan assets	**1,753,903**	1,483,554	1,288,987
Deficiency of plan assets	**(685,962)**	(563,857)	(497,927)
Unrecognized actuarial loss	**715,547**	598,493	568,124
	P 29,585	P 34,636	P 70,197

	Parent – UnionBank Plan		
	2012	2011	2010
Present value of obligation	**P 2,013,112**	P 1,703,277	P 1,469,537
Fair value of plan assets	**1,351,301**	1,153,758	989,629
Deficiency of plan assets	**(661,811)**	(549,519)	(479,908)
Unrecognized actuarial loss	**649,319**	540,781	499,255
	(P 12,492)	(P 8,738)	P 19,347

	Parent – Former iBank Plan		
	2012	2011	2010
Present value of obligation	**P 417,492**	P 337,070	P 310,876
Fair value of plan assets	**392,556**	320,652	291,017
Deficiency of plan assets	**(24,936)**	(16,418)	(19,859)
Unrecognized actuarial loss	**65,050**	57,316	69,619
	P 40,114	P 40,898	P 49,760

The movements in the present value of the retirement benefit obligation recognized in the books follow:

	Group		
	2012	2011	2010
Balance at beginning of year	**P 2,047,411**	P 1,786,914	P 1,401,222
Actuarial loss	**254,095**	74,917	195,821
Current service cost	**172,552**	161,608	118,440
Interest cost	**130,106**	127,696	121,109
Benefits paid by the plan	**(164,299)**	(103,724)	(49,678)
Balance at end of year	**P 2,439,865**	P 2,047,411	P 1,786,914

	Parent – UnionBank Plan		
	2012	2011	2010
Balance at beginning of year	**P 1,703,277**	P 1,469,537	P 1,171,212
Actuarial loss	**217,531**	83,090	149,068
Current service cost	**140,629**	129,271	93,622
Interest cost	**108,839**	106,100	101,661
Benefits paid by the plan	**(157,164)**	(84,721)	(46,026)
Balance at end of year	**P 2,013,112**	P 1,703,277	P 1,469,537

	Parent – Former iBank Plan		
	2012	2011	2010
Balance at beginning of year	**P 337,070**	P 310,876	P 224,897
Current service cost	**31,299**	31,703	24,289
Interest cost	**20,831**	21,140	19,004
Actuarial loss (gain)	**35,427**	(7,646)	46,337
Benefits paid by the plan	**(7,135)**	(19,003)	(3,651)
Balance at end of year	**P 417,492**	P 337,070	P 310,876

The movements in the fair value of plan assets follow:

	Group 2012	Group 2011	Group 2010
Balance at beginning of year	**P 1,483,554**	P 1,288,987	P 914,714
Contributions paid into the plan	**231,961**	186,828	207,080
Benefits paid by the plan	**(164,299)**	(103,724)	(49,678)
Expected return on plan assets	**89,013**	90,229	65,589
Actuarial gain	**113,674**	21,234	151,282
Balance at end of year	**P 1,753,903**	P 1,483,554	P 1,288,987

	Parent – UnionBank Plan 2012	Parent – UnionBank Plan 2011	Parent – UnionBank Plan 2010
Balance at beginning of year	**P 1,153,758**	P 989,629	P 700,924
Contributions paid into the plan	**198,280**	158,736	171,541
Benefits paid by the plan	**(157,164)**	(84,721)	(46,026)
Expected return on plan assets	**69,226**	69,274	50,467
Actuarial gain	**87,201**	20,840	112,723
Balance at end of year	**P 1,351,301**	P 1,153,758	P 989,629

	Former iBank Plan 2012	Former iBank Plan 2011	Former iBank Plan 2010
Balance at beginning of year	**P 320,652**	P 291,017	P 206,250
Contributions paid into the plan	**33,681**	26,179	35,539
Expected return on plan assets	**19,239**	20,371	14,850
Benefits paid by the plan	**(7,135)**	(19,003)	(3,651)
Actuarial gain	**26,119**	2,088	38,029
Balance at end of year	**P 392,556**	P 320,652	P 291,017

The plan assets consist of the following:

	Group 2012	Group 2011	Group 2010
Investments in:			
Equity securities	**P 1,381,926**	P 962,201	P 790,836
Debt securities	**347,012**	380,604	412,429
Bank deposits	**23,902**	136,272	81,255
Others	**1,063**	4,477	4,467
	P 1,753,903	P 1,483,554	P 1,288,987

	Parent – UnionBank Plan 2012	Parent – UnionBank Plan 2011	Parent – UnionBank Plan 2010
Investments in:			
Equity securities	**P 997,470**	P 736,294	P 598,654
Debt securities	**341,787**	340,844	336,874
Bank deposits	**10,981**	72,860	50,523
Others	**1,063**	3,760	3,578
	P 1,351,301	P 1,153,758	P 989,629

	Parent – Former iBank Plan		
	2012	2011	2010
Investments in:			
Equity securities	**P 374,684**	P 217,066	P 184,188
Debt securities	**5,225**	39,760	75,555
Bank deposits	**12,647**	63,101	30,375
Others	**-**	725	899
	P 392,556	P 320,652	P 291,017

Equity securities under the fund are primarily investments in corporations listed in the PSE, which includes P130,923 investment in the shares of stocks of the Bank (see Note 30.7); while debt securities represent investments in government and corporate bonds. The retirement fund neither provides any guarantee or surety for any obligation of the Bank nor its investments in the Bank's shares of stocks covered by any restriction and liens. Bank deposits are maintained with reputable financial institutions, which includes P4,374 deposits to the Bank.

Actual returns on plan assets were P156,427 in 2012, P90,115 in 2011 and P163,189 in 2010 for UnionBank and P45,358 in 2012, P22,460 in 2011 and P52,879 in 2010 for iBank.

The amounts of retirement benefits recognized in the statements of income are as follows:

	Group		
	2012	2011	2010
Current service cost	**P 172,552**	P 161,608	P 118,440
Interest cost	**130,106**	127,696	121,109
Expected return on plan assets	**(89,013)**	(90,229)	(65,444)
Net actuarial loss recognized	**23,367**	23,314	22,943
	P 237,012	P 222,389	P 197,048

	Parent – UnionBank Plan		
	2012	2011	2010
Current service cost	**P 140,629**	P 129,271	P 93,622
Interest cost	**108,839**	106,100	101,661
Expected return on plan assets	**(69,226)**	(69,274)	(50,467)
Net actuarial loss recognized	**21,792**	20,724	20,341
	P 202,034	P 186,821	P 165,157

	Parent – Former iBank Plan		
	2012	2011	2010
Current service cost	**P 31,299**	P 31,703	P 24,289
Interest cost	**20,831**	21,140	19,004
Expected return on plan assets	**(19,239)**	(20,371)	(14,850)
Net actuarial loss recognized	**1,574**	2,569	2,588
	P 34,465	P 35,041	P 31,031

The movements in retirement benefit asset are as follows:

	Group		
	2012	2011	2010
Balance at beginning of year	**P 34,636**	P 70,197	P 60,165
Expense recognized	**(237,012)**	(222,389)	(197,048)
Actual contributions	**231,961**	186,828	207,080
Balance at end of year	**P 29,585**	P 34,636	P 70,197

	Parent – UnionBank Plan		
	2012	2011	2010
Balance at beginning of year	**(P 8,738)**	P 19,347	P 12,963
Expense recognized	**(202,034)**	(186,821)	(165,157)
Actual contributions	**198,280**	158,736	171,541
Balance at end of year	**(P 12,492)**	(P 8,738)	P 19,347

	Parent – Former iBank Plan		
	2012	2011	2010
Balance at beginning of year	**P 40,898**	P 49,760	P 45,252
Expense recognized	**(34,465)**	(35,041)	(31,031)
Actual contributions	**33,681**	26,179	35,539
Balance at end of year	**P 40,114**	P 40,898	P 49,760

Presented below are the historical information related to the present value of the retirement benefit obligation, fair value of plan assets and excess or deficit in the plan, as well as experience adjustments arising on plan assets and liabilities.

UnionBank Plan

	2012	2011	2010	2009	2008
Present value of the obligation	**P 2,013,112**	P 1,703,277	P 1,469,537	P 1,171,212	P 966,301
Fair value of plan assets	**(1,351,301)**	(1,153,758)	(989,629)	(700,924)	(478,740)
Deficit in the plan	**P 661,811**	P 549,519	P 479,908	P 470,288	P 487,561

	2012	2011	2010	2009
Experience adjustments arising on plan liabilities	**P 20,614**	P 143,270	P 76,053	P 19,295
Experience adjustments arising on plan assets	**87,201**	20,840	112,723	84,070

Former iBank Plan

	2012	2011	2010
Present value of the obligation	**P 417,492**	P 337,070	P 310,876
Fair value of plan assets	**(392,556)**	(320,652)	(291,017)
Deficit in the plan	**P 24,936**	P 16,418	P 19,859

	2012	2011	2010
Experience adjustments arising on plan liabilities	**P 3,974**	P 9,227	P 8,758
Experience adjustments arising on plan assets	**26,119**	2,089	38,029

The Bank expects to contribute P226.7 million for the UnionBank Plan and P39.4 million for the Former iBank Plan in 2013.

In determining the retirement benefits, the following actuarial assumptions were used:

	Parent – UnionBank Plan		
	2012	2011	2010
Retirement age	**60**	60	60
Average remaining working life	**17 years**	18 years	27 years
Discount rate	**6.39%**	7.22%	8.68%
Expected rate of return on plan assets	**6.00%**	7.00%	7.20%
Expected rate of salary increase	**6.00%**	8.00%	8.00%

	Former iBank Plan		
	2012	2011	2010
Retirement age	**60**	60	60
Average remaining working life	**15 years**	16 years	25 years
Discount rate	**6.18%**	6.80%	8.45%
Expected rate of return on plan assets	**6.00%**	7.00%	7.20%
Expected rate of salary increase	**6.00%**	8.00%	8.00%

Assumptions regarding future mortality and disability are based on published statistics and mortality tables.

The expected long-term rate of return is based on the portfolio as a whole and not on the sum of the returns on individual asset categories. The return is based exclusively on historical returns, without adjustments.

28. TAXES

28.1 Current and Deferred Taxes

The components of tax expense for the years ended December 31, 2012, 2011 and 2010 are as follows:

	Group		
	2012	2011	2010
Current tax expense:			
Final tax at 20% and 7.5%	**P 608,800**	P 623,915	P 592,208
Regular corporate income tax (RCIT) at 30%	**1,409**	2,581	205
MCIT at 2%	**91,043**	67,512	61,441
	701,252	694,008	653,854
Deferred tax expense (income) relating to origination and reversal of temporary differences	**(373,212)**	(479,499)	179,351
Tax expense reported in profit or loss	**P 328,040**	P 214,509	P 833,205
Tax expense reported in other comprehensive income	**P 4,604**	P 22,509	P 17,904

	Parent		
	2012	2011	2010
Current tax expense:			
Final tax at 20% and 7.5%	**P 607,760**	P 623,656	P 591,678
MCIT at 2%	**90,745**	67,368	61,441
	698,505	691,024	653,119
Deferred tax expense (income) relating to origination and reversal of temporary differences	**(373,212)**	(479,643)	177,035
Tax expense reported in profit or loss	**P 325,293**	P 211,381	P 830,154
Tax expense reported in other comprehensive income	**P 4,604**	P 22,509	P 17,904

The reconciliation of the tax on pretax profit computed at the statutory tax rates to tax expense is shown below:

	Group		
	2012	2011	2010
Tax on pretax profit at 30%	**P 2,374,018**	P 2,042,972	P 1,855,937
Adjustment for income subjected to lower income tax rates	**(86,443)**	(236,514)	(236,087)
Tax effects of:			
FCDU income before tax	**(1,540,308)**	(1,862,238)	(1,306,737)
Non-taxable income	**(1,092,964)**	(633,852)	(398,433)
Non-deductible expenses	**380,106**	360,631	334,254
Unrecognized deferred tax asset	**95,987**	607,271	625,895
Others	**197,644**	(63,761)	(41,624)
Tax expense reported in profit or loss	**P 328,040**	P 214,509	P 833,205

	Parent		
	2012	2011	2010
Tax on pretax profit at 30%	**P 2,338,145**	P 1,985,063	P 1,822,050
Adjustment for income subjected to lower income tax rates	**(85,923)**	(236,385)	(235,822)
Tax effects of:			
FCDU income before tax	**(1,540,308)**	(1,862,238)	(1,306,737)
Non-taxable income	**(1,014,991)**	(561,369)	(354,771)
Non-deductible expenses	**334,167**	360,629	333,849
Unrecognized deferred tax asset	**90,745**	340,133	613,560
Others	**203,458**	185,548	(41,975)
Tax expense reported in the profit or loss	**P 325,293**	P 211,381	P 830,154

The components of the net deferred tax assets (presented under Other Resources – see Note 18) as of December 31, 2012, 2011 and 2010 are as follows:

	Group Statements of Financial Position		
	2012	2011	2010
Deferred tax assets:			
Allowance for impairment losses	**P 3,644,186**	P 3,286,184	P 2,919,162
Accrued other expenses	**266,907**	265,200	217,303
Sick leave benefits	**8,384**	-	-
Unrealized fair value loss on AFS financial assets	**-**	4,604	-
Unrealized foreign exchange loss	**-**	-	327,060
Others	**85,312**	95,133	93,338
	4,004,789	3,651,121	3,556,863
Deferred tax liabilities:			
Fair value gains on investment properties	**1,018,142**	1,022,488	1,020,888
Foreign currency swap revaluation gain	**60,923**	45,653	459,678
Capitalized interest	**37,340**	37,340	38,439
Unrealized foreign exchange gain	**-**	26,964	-
Unrealized fair value gains on AFS financial assets	**-**	-	17,904
Others	**39,472**	40,074	44,140
	1,155,877	1,172,519	1,581,049
Net deferred tax assets	**P 2,848,912**	P 2,478,602	P 1,975,814

	Parent Statements of Financial Position		
	2012	2011	2010
Deferred tax assets:			
Allowance for impairment losses	**P 3,643,823**	P 3,285,821	P 2,918,716
Accrued other expenses	**266,903**	265,196	217,303
Sick leave benefits	**8,384**		
Unrealized fair value loss on AFS financial assets	**-**	4,604	-
Unrealized foreign exchange loss	**-**	-	327,060
Others	**82,776**	93,697	93,338
	4,001,886	3,649,318	3,556,417
Deferred tax liabilities:			
Fair value gains on investment properties	**1,015,218**	1,019,564	1,022,365
Foreign currency swap revaluation gain	**60,923**	45,653	459,678
Capitalized interest	**37,340**	37,340	38,439
Unrealized foreign exchange gain	**-**	26,964	-
Unrealized fair value gains on AFS financial assets	**-**	-	17,904
Others	**39,472**	39,472	39,858
	1,152,953	1,168,993	1,578,244
Net deferred tax assets	**P 2,848,933**	P 2,480,325	P 1,978,173

	Group Statements of Income		
	2012	2011	2010
Foreign currency swap revaluation loss (gain)	**P 15,270**	(P 414,025)	P 204,036
Impairment losses	**(358,002)**	(367,105)	(157,339)
Unrealized foreign exchange loss (gain)	**(26,964)**	354,024	(262,151)
Accrued other expenses	**(1,707)**	(47,893)	58,111
Net fair value gains (losses) on investment properties	**(4,346)**	(2,801)	35,621
NOLCO	**-**	-	281,933
MCIT	**-**	-	70,436
Others	**2,537**	(1,699)	(51,296)
Deferred tax expense (income)	**(P 373,212)**	(P 479,499)	P 179,351

	Parent Company Statements of Income		
	2012	2011	2010
Foreign currency swap revaluation loss (gain)	**P 15,270**	(P 414,025)	P 204,036
Impairment losses	**(358,002)**	(367,105)	(157,339)
Unrealized foreign exchange loss (gain)	**(26,964)**	354,024	(262,151)
Accrued other expenses	**(1,707)**	(47,893)	58,111
Net fair value gains (losses) on investment properties	**(4,346)**	(2,801)	35,621
NOLCO	**-**	-	281,933
MCIT	**-**	-	70,436
Others	**2,537**	(1,843)	(53,612)
Deferred tax expense (income)	**(P 373,212)**	(P 479,643)	P 177,035

Deferred tax expense reported in other comprehensive income amounted to P4,604 in 2012, P22,509 in 2011 and P17,904 in 2010.

The unrecognized deferred tax assets as of December 31, 2012 and 2011 pertain to the following temporary differences:

	Group	
	2012	2011
NOLCO	**P 822,365**	P 1,277,740
MCIT	**219,554**	185,453
Others	**-**	224
	P 1,041,919	P 1,463,417

	Parent	
	2012	2011
NOLCO	**P 822,365**	P 1,259,826
MCIT	**219,554**	185,178
	P 1,041,919	P 1,445,004

The Group did not recognize the above deferred tax assets mainly on NOLCO and MCIT since management believes that it is not reasonably possible that the related tax benefits from these deferred tax assets may be realized in the future.

The breakdown of NOLCO of the Parent Company (nil for the subsidiaries) follows:

Inception Year	Amount	Applied/ Expired	Balance	Expiry Year
2011	P 909,218	P -	P 909,218	2014
2010	1,831,998	-	1,831,998	2013
2009	1,517,916	(1,517,916)	-	
	P 4,259,132	(P 1,517,916)	P 2,741,216	

The breakdown of the Parent Company's (nil for subsidiaries) MCIT follows:

Inception Year	Amount	Movements	Balance	Expiry Year
2012	P 90,745	P	P 90,745	2015
2011	67,368	-	67,368	2014
2010	61,441	-	61,441	2013
2009	56,645	(56,645)	-	
	P 276,199	(P 56,645)	P 219,554	

28.2 Relevant Tax Regulations

The following are the relevant tax regulations affecting the Group:

28.2.1 Income Tax

(a) MCIT of 2% based on gross income, as defined under the Tax Code, is required to be computed and paid (if higher than the RCIT) at the end of each quarter beginning on the income tax return for fiscal quarter ending September 30, 2007, as provided for under Revenue Regulation (RR) 12-2007;

(b) NOLCO can be claimed as deduction against taxable income within three years after NOLCO is incurred;

(c) FCDU transactions with non-residents of the Philippines and other offshore banking units (offshore income) are tax-exempt, while interest income on foreign currency loans from residents other than OBUs or other depository banks under the expanded system is subject to 10% income tax;

(d) Withholding tax of 7.5% is imposed on interest earned by residents under the expanded foreign currency deposit system.

28.2.2 Documentary Stamp Tax

Documentary stamp taxes (DST) (at varying rates) are imposed on the following:

(a) Bank checks, drafts, or certificate of deposit not bearing interest, and other instruments;

(b) Bonds, loan agreements, promissory notes, bills of exchange, drafts, instruments and securities issued by the Government or any of its instrumentalities, deposit substitute debt instruments, certificates of deposits bearing interest and other not payable on sight or demand;

(c) Acceptance of bills of exchange and letters of credit; and,

(d) Bills of lading or receipt.

On February 7, 2004, RA 9243, *An Act Rationalizing the Provisions on the Documentary Stamp Tax of the NIRC*, was passed amending the rates of DST, the significant provisions of which are summarized below:

(a) On every issue of debt instruments, there shall be collected a DST of P1.00 on each P200 or fractional part thereof of the issue price of any such debt instrument; provided, that for such debt instruments with terms of less than one year, the DST to be collected shall be of a proportional amount in accordance with the ratio of its term in number of days to 365 days; provided further that only one DST shall be imposed on either loan agreement or promissory notes to secure such loan.

(b) On all sales or transfer of shares or certificates of stock in any corporation, there shall be collected a DST of P0.75 on each P200, or fractional part thereof, of the par value of such stock.

(c) On all bills of exchange or drafts, there shall be collected a DST of P0.30 on each P200, or fractional part thereof, of the face value of any such bill of exchange or draft.

(d) The following instruments, documents and papers shall be exempt from DST:

- Borrowings and lending of securities executed under the Securities Borrowing and Lending Program of a registered exchange, or in accordance with regulations prescribed by the appropriate regulatory authority;

- Loan agreements or promissory notes, the aggregate of which does not exceed P250,000 or any such amount as may be determined by the Secretary of Finance, executed by an individual for his purchase on installment for his personal use;

- Sale, barter or exchange of shares of stock listed and traded through the local stock exchange (as amended by RA 9648);

- Fixed income and other securities traded in the secondary market or through an exchange;

- Derivatives including repurchase agreements and reverse repurchase agreements;

- Bank deposit accounts without a fixed term or maturity; and,

- Interbank call loans with maturity of not more than seven days to cover deficiency in reserve against deposit liabilities.

28.2.3 Optional Standard Deduction

In 2012, 2011 and 2010, the Bank opted to claim itemized deductions.

29. TRUST OPERATIONS

The following securities and other properties held by the Bank in fiduciary or agency capacity (for a fee) for its customers are not included in the accompanying statement of financial position since these are not properties of the Bank (see Note 33.2).

	2012	2011
Investments	**P 36,212,930**	P 39,282,658
Others	**83,499**	157,627
	P 36,296,429	P 39,440,285

In compliance with the requirements of the General Banking Act relative to the Bank's trust functions:

a. Investment in government securities (shown as part of AFS financial assets) with a total face value of P463,537 as of December 31, 2012 and 2011 are deposited with BSP as security for the Bank's faithful compliance with its fiduciary obligations (see Note 11); and,

b. Ten percent of the Bank's trust income is transferred to surplus reserves. This yearly transfer is required until the surplus reserves for trust function is equivalent to 20% of the Bank's authorized capital stock. No part of such reserves shall at anytime be paid out as dividends, but losses accruing in the course of business may be charged against such surplus. As of December 31, 2012, the reserve for trust functions amounted to P149,596 and is included as part of Surplus Reserves in the statement of changes in capital funds.

Also, in accordance with BSP regulations, the UITFs managed by the Bank's TISG maintain reserve deposit account with the BSP and government securities to meet the reserve requirement on peso-denominated UITFs and other similarly managed funds. The balances of the BSP reserve deposit account amounted to P3,700 as of December 31, 2011(nil as of December 31, 2012). Income from trust operations of the Group amounted to P473,114, P375,689 and P105,087 for the years ended December 31, 2012, 2011 and 2010, respectively, and shown as Income from trust operations account under Miscellaneous Income in the Group statements of income (see Note 26.1).

30. RELATED PARTY TRANSACTIONS

The Group's and Parent Company's related parties include subsidiaries, stockholders, key management personnel and others as described below.

The summary of the Bank's significant transactions with its related parties as of and for the years ended December 31, 2012 and 2011 are as follows:

Related Party Category	Notes	2012 Amount of Transaction	2012 Outstanding Balance	2011 Amount of Transaction	2011 Outstanding Balance
Subsidiaries					
Lease of properties	30.1	**P 863**	**P -**	P 717	P -
Management services	30.2	**2,343**	**284**	3,710	369
Deposit liabilities	30.3				
Outstanding balance		**-**	**179,960**	-	116,494
Net movements		**63,466**	**-**	(143,928)	-
Interest expense on deposits		**4,763**	**-**	1,381	-
Advances	30.4	**-**	**3,917**	-	3,917
Stockholders					
Deposit liabilities	30.3				
Outstanding balance		**-**	**6,660,350**	-	7,303,008
Net movements		**(642,658)**	**-**	(4,579,544)	-
Interest expense on deposits		**216,548**	**-**	55,798	-
Key management personnel	30.5	**925,403**	**-**	742,625	-
Others					
DOSRI	30.6				
Directors and officers		**823,066**	**823,066**	640,005	640,005
Stockholders		**5,000**	**5,000**	-	-
Other related interests		**50,308**	**50,308**	12,118	12,118

Outstanding receivables from and payables to related parties, if any, arising from lease of properties, management services and advances are unsecured, noninterest-bearing and generally settled in cash within 12 months or upon demand.

The Bank and its subsidiaries' retirement plans have transactions directly and indirectly with the Bank as of December 31, 2012 as follows:

	Amount of Transaction	Outstanding Balance
Investment in Bank shares	P 120,306	P 130,923
Investment in Bank's notes payable		
Outstanding balance	-	188,210
Net movements	6,635	-
Interest income	10,039	-
Accrued interest income	-	1,435
Deposits		
Outstanding balance	-	4,374
Net movements	(84,160)	-
Interest income on deposits	5,913	2
Dividend income	774	-
Trading gain	75	-

30.1 Lease of Properties

The Bank entered into an agreement with UPI, whereby the latter leases out one of its investment properties to the former for a period of five years. In consideration for these, the Bank pays a monthly rent of P78, VAT exclusive.

30.2 Management Services

The Bank entered into a sales management agreement with FUDC whereby the latter sells UnionBank Visa Credit Cards through its direct selling network. Under the terms of the agreement, the Bank pays a fixed monthly sales management fee of P200 (net of applicable taxes) plus commission per approved principal card.

30.3 Deposit Liabilities and Interest Expense

The deposit accounts of subsidiaries and stockholders with the Bank generally earn interest based on daily bank deposit rates.

30.4 Advances

The Bank has also noninterest-bearing and unsecured advances to UBPSI which are generally settled in cash upon demand. There were no movements on this account as of December 31, 2012 and 2011. No impairment losses were provided for these advances as of December 31, 2012 and 2011.

30.5 Key Management Personnel Compensation

The compensation of key management personnel for the Group and Parent Company follows:

	Group		
	2012	2011	2010
Short-term benefits	**P 708,372**	P 568,269	P 419,526
Post-employment benefits	**58,640**	41,561	52,416
Other long-term benefits	**165,516**	137,416	119,181
	P 932,528	P 747,246	P 591,123

	Parent		
	2012	2011	2010
Short-term benefits	**P 701,247**	P 563,648	P 414,773
Post-employment benefits	**58,640**	41,561	52,416
Other long-term benefits	**165,516**	137,416	117,831
	P 925,403	P 742,625	P 585,020

Directors' fees incurred by the Group amounted to P23,253 in 2012, P19,616 in 2011 and P15,622 in 2010, and by the Parent Company amounted to P23,247 in 2012, P19,611 in 2011 and P15,615 in 2010.

30.6 DOSRI

In the ordinary course of business, the Group has loans, deposits and other transactions with its related parties and with certain DOSRI. Under the Group's existing policies, these transactions are made substantially on the same terms and conditions as transactions with other individuals and businesses of comparable risks. The amount of individual loans to DOSRI, of which 70% must be secured, should not exceed the amount of the deposit and book value of their investment in the Group. In the aggregate, loans to DOSRI generally should not exceed the total equity or 15% of the total loan portfolio of the Group, whichever is lower. As of December 31, 2012 and 2011, the Bank is in compliance with these regulatory requirements.

The following additional information is presented relative to DOSRI loans:

	Group and Parent	
	2012	2011
Total DOSRI loans	**P 878,374**	P 652,123
Unsecured DOSRI loans	**118,985**	94,228
% of DOSRI loans to total loan portfolio	**0.7%**	0.6%
% of unsecured DOSRI loans to total DOSRI loans	**13.6%**	14.5%
% of past due DOSRI loans to total DOSRI loans	**0.0%**	0.0%
% of non-accruing DOSRI accounts to total DOSRI loans	**0.0%**	0.0%

On January 31, 2007, BSP issued Circular No. 560 which provides the rules and regulations that govern loans, other credit accommodations and guarantees granted to subsidiaries and affiliates of banks and quasi-banks. Under the said circular, the total outstanding exposures to each of the Bank's subsidiaries and affiliates shall not exceed 10% of bank's net worth, the unsecured portion of which shall not exceed 5% of such net worth. Further, the total outstanding exposures to subsidiaries and affiliates shall not exceed 20% of the net worth of the lending bank.

30.7 Transactions with the Retirement Plan

The retirement fund of the Bank covered under defined benefit post-employment plan maintained for qualified employees is administered by the Retirement Committee. The members of the Retirement Committee are Senior Executives and officers of the Bank as approved by the Chairman/CEO. Through its Retirement Committee, it has appointed TISG as the trustee for the retirement fund which is covered by trust agreements.

The retirement plan assets and their carrying values of the Bank and its subsidiaries as of December 31, 2012 are the following:

	Group	Parent
Investments in:		
Equity securities	P 1,381,926	1,372,154
Debt securities	347,012	347,012
Bank deposits	23,902	23,628
Others	1,063	1,063
	P 1,753,903	**P 1,743,857**

As of December 31, 2012, the carrying value of the fund is equivalent to its fair value.

The Bank's retirement fund includes investments in shares of stock and notes payable of the Bank amounting to P130,923 and P188,210, respectively, as of December 31, 2012. The investment in Bank shares are primarily held for re-sale and the Bank's retirement fund does not intend to exercise its voting rights over those shares. The terms of the investment in notes payable are discussed in Note 22.

The retirement fund of the Bank and the combined retirement funds of the Group have demand deposits with the Bank amounting to P4,100 and P4,374, respectively, as of December 31, 2012.

The related dividend income, interest income and trading gain amounted to P774, P15,952 and P75, respectively, in 2012.

31. EARNINGS PER SHARE

Basic earnings per share were computed as follows:

	Group		
	2012	2011	2010
Net profit	**P 7,585,352**	P 6,595,398	P 5,353,251
Divided by the weighted average number of outstanding common shares	**641,422**	641,422	641,422
Basic earnings per share	**P 11.83**	P 10.28	P 8.35

	Parent		
	2012	2011	2010
Net profit	**P 7,468,522**	P 6,405,494	P 5,243,345
Divided by the weighted average number of outstanding common shares	**641,422**	641,422	641,422
Basic earnings per share	**P 11.64**	P 9.99	P 8.17

As of December 31, 2012, 2011 and 2010, the Group and Parent Company have no outstanding potentially dilutive securities, hence, basic earnings per share are equal to diluted earnings per share.

32. SELECTED FINANCIAL PERFORMANCE INDICATORS

The following are some measures of the Bank's financial performance:

	2012	2011	2010
Return on average capital funds:			
Net profit / Average total capital funds	**17.0%**	16.7%	15.5%
Return on average resources:			
Net profit / Average total resources	**3.0%**	2.5%	2.2%
Net interest margin:			
Net interest income / Average interest-earning resources	**3.5%**	3.1%	3.5%
Liquidity ratio:			
Current Assets / Current Liabilities	**86.5%**	79.2%	82.8%
Debt-to-equity ratio:			
Liabilities / Equity	**4.8:1**	5.4:1	6.1:1
Asset-to-equity ratio:			
Asset / Equity	**5.8:1**	6.4:1	7.1:1
Interest rate coverage ratio:			
Earnings before interests and taxes / Interest expense	**3.2:1**	2.4:1	2.3:1

33. COMMITMENTS AND CONTINGENT LIABILITIES

33.1 Leases

The Bank leases various branch premises for an average of seven years. The lease contracts are cancelable or renewable at the Bank's option under certain terms and conditions. Various lease contracts include escalation clauses, most of which bear an annual rent increase of 5%. Some leases include a clause to enable adjustment of the rental charge on an annual basis based on prevailing market rates. As of December 31, 2012, 2011 and 2010, the Bank has neither a contingent rent payable nor an asset restoration obligation in relation with these lease agreements.

Rentals charged against current operations included under Occupancy account in the statements of income are as follows:

	2012	2011	2010
Group	**P 399,276**	P 399,753	P 360,052
Bank	**399,278**	400,470	361,243

The estimated minimum future annual rentals payable under non-cancellable operating leases follows:

	Group		
	2012	2011	2010
Within one year	**P 96,321**	P 96,607	P 86,409
Beyond one year but within five years	**192,066**	284,228	273,870
Beyond five years	**3,670**	23,021	3,265
	P 292,057	P 403,856	P 363,544

	Parent		
	2012	2011	2010
Within one year	**P 96,321**	P 96,607	P 86,409
Beyond one year but within five years	**192,066**	284,228	273,870
Beyond five years	**3,670**	23,021	3,265
	P 292,057	P 403,856	P 363,544

The Group has entered into commercial property leases on the Group's surplus offices. These non-cancellable leases have remaining non-cancellable lease terms of between one and four years.

Total rent income earned (included under Other Operating Income account in the statements of income – see Note 26.1) by the Group and the Bank for the years ended December 31, 2012, 2011 and 2010 are as follows:

	2012	2011	2010
Group	**P 113,876**	P 128,424	P 83,160
Bank	**109,186**	126,096	84,138

The estimated minimum future annual rentals receivable under non-cancelable operating leases follows:

	Group		
	2012	2011	2010
Within one year	**P 42,277**	P 73,686	P 65,287
Beyond one year but within five years	**80,485**	75,985	62,718
	P 122,762	P 149,671	P 128,005

	Parent		
	2012	2011	2010
Within one year	**P 35,231**	P 71,495	P 62,520
Beyond one year but within five years	**66,392**	66,392	62,718
	P 101,623	P 137,887	P 125,238

33.2 Others

In the normal course of the Group's operations, there are various outstanding commitments and contingent liabilities such as guarantees, commitments to extend credit, etc., which are not reflected in the accompanying financial statements. The Group recognizes in its books any losses and liabilities incurred in the course of its operations as soon as these become determinable and quantifiable. Management believes that, as of December 31, 2012, no additional material losses or liabilities are required to be recognized in the accompanying financial statements as a result of the above commitments and transactions.

Following is a summary of the Bank's commitments and contingent accounts:

	Note	**2012**	2011
Trust department accounts		**P 36,296,429**	P 39,440,285
Unused commercial letters of credit	4.2.3	**3,000,347**	2,703,773
Inward bills for collections		**7,000,052**	6,771,913
Outstanding guarantees issued	4.2.3	**545,906**	440,845
Late deposits/payments received		**73,643**	57,840
Outward bills for collection		**58,104**	53,044
Unsold travellers' checks		**-**	12,481
Other contingent accounts		**2,646**	1,957

There are several suits and claims that remain unsettled. Management believes, based on the opinion of its legal counsels, that the ultimate outcome of such cases and claims will not have a material effect on the Bank's financial position and results of operations.

UPI acts as the project and fund manager of Kingswood Project. As fund manager, UPI is responsible for the treasury and money management as well as arranging the necessary facilities and accounting for the development of the project. UPI also receives a certain percentage of the sales price related to Kingswood Project as sales commission and to compensate for the marketing expenses incurred.

34. EVENTS AFTER THE END OF THE REPORTING PERIOD

34.1 Dividend Declaration

On January 25, 2013, the BOD approved the declaration of cash dividends at P3.50 per share or for a total of P2,244,978 based on the outstanding common stock of 641,422,420 shares as of December 31, 2012. The BSP, in its letter to the Bank dated March 6, 2013, has approved the cash dividend declaration of the Bank with record date of March 20, 2013 and payment date of April 18, 2013.

34.2 Acquisition of City Savings Bank, Inc.

On January 8, 2013, the BOD approved the purchase of all the issued and outstanding shares of City Savings Bank, Inc. (CSB) held by AEVI and its wholly owned subsidiary, Pilmico Foods Corporation (PFC). AEVI and PFC own 99.54% of CSB's issued and outstanding capital stock. AEVI owns 116,262 shares or 59.54% while PFC owns 78,109 shares or 40.00%. The acquisition was approved by the Monetary Board of the BSP on March 21, 2013.

35. SUPPLEMENTARY INFORMATION REQUIRED BY THE BUREAU OF INTERNAL REVENUE

Presented below is the supplementary information required by the Bureau of Internal Revenue (BIR) under its existing revenue regulations to be disclosed as part of the notes to financial statements. This supplementary information is not a required disclosure under PFRS.

35.1 Requirements under Revenue Regulations (RR) 15-2010

(a) Gross Receipts Tax

In lieu of the value-added tax (VAT), the Bank is subject to the gross receipts tax (GRT) imposed on all banks and non-bank financial intermediaries pursuant to Section 121 of the Tax Code.

The Bank reported total GRT amounting to P716,904 in 2012 as shown under Taxes and Licenses account [see Note 35.1(d)]. GRT paid for the year 2012 amounted to P714,948, net of creditable percentage tax withheld by government-payor. Total GRT payable as of December 31, 2012 amounted to P65,829 included under Accrued Taxes and Other Expenses account (see Note 23).

(b) Documentary Stamp Tax

The Bank is enrolled under the Electronic DST System. In general, the Bank's DST transactions arise from the execution of debt instruments, security documents, and bills of exchange.

For the year ended December 31, 2012, DST affixed amounted to P446,295. Of this amount, P250,131 was charged to clients while the balance of P196,164 was for the account of the Bank and accordingly charged to profit and loss.

(c) Withholding Taxes

The details of total withholding taxes for the year ended December 31, 2012 are shown below.

Final	P	502,535
Compensation and benefits		523,587
Expanded		121,826
	P	1,147,948

(d) Taxes and Licenses

The details of taxes and licenses in 2012 of the Parent Company are as follows:

	Notes		
GRT	35.1(a)	P	716,904
DST	35.1(b)		446,295
Real property taxes	16		41,132
Fringe benefits tax (FBT)	27		23,808
Local taxes and business permits			29,466
Miscellaneous			9,319
			1,266,924
Less:			
DST charged to customers	35.1(b)		250,131
FBT charged to employee benefits			23,808
			273,939
		P	992,985

(e) Excise Taxes

The Bank does not have excise taxes accrued since it does not have any transactions subject to excise tax.

(f) Deficiency Tax Assessments and Tax Cases

The Bank has no outstanding deficiency tax assessments pending with the BIR.

The Bank's existing tax assessments pending with the Court of Tax Appeals (CTA) for tax liabilities of the former iBank and the Bank were all covered by the BIR's tax amnesty program for calendar years 2005 and earlier pursuant to RA 9480, An Act Enhancing Revenue Administration and Collection by Granting an Amnesty on All Unpaid Internal Revenue Taxes. The Bank availed of this amnesty program on February 4 and 19, 2008. Consequently, the Bank contends that these tax assessments pending with the CTA have become moot and academic.

Prior to the Bank's availment of the tax amnesty program, on June 29, 2007, pursuant to RR 15-2006, the Bank filed 12 applications for administrative abatement of the Bank's and the former iBank's DST assessments for years 2004 and earlier, for which the Bank paid the BIR a total of P147,728. Four of these applications were subsequently denied while the other eight were not acted upon by the BIR. Because of the BIR's inaction and denial of these applications coupled with the Bank's availment of the tax amnesty program, on March 4, 2009, the Bank filed with the BIR a claim for refund and/or issuance of Tax Credit Certificate for the amount paid under the abatement program. Because of the inaction of the BIR on the claim for refund, on June 29, 2009, the Bank elevated the claim with the Court of Tax Appeals to toll the running of the two-year prescriptive period imposed on claims for refund.

(g) Other Required Tax Information

The Bank has not paid or accrued any excise taxes or customs' duties and tariff fees as it has no importation for the year ended December 31, 2012.

35.2 Requirements under RR 19-2011

On December 9, 2011, the BIR issued RR 19-2011 which prescribes the new form for income tax filing covering and starting with period ending December 31, 2011.

The amounts of taxable revenues and income, and deductible costs and expenses presented below are based on relevant tax regulations issued by the BIR, hence, these may not be the same as the amounts reflected in the 2012 statement of comprehensive income.

(a) Taxable Revenues

The Bank's taxable revenue amounted to P6,003,671 representing interest income for the year ended December 31, 2012.

(b) Deductible Costs of Services

Deductible costs of services for the year ended December 31, 2012 comprise the following:

Cost of services		
Interest expense	P	2,097,457
Salaries		1,425,697
Insurance		251,389
Supervision fee		58,323
	P	3,832,866

(c) Taxable Non-operating and Other Income

The details of taxable non-operating and other income in 2012 which are subject to regular tax rate are shown below:

Service charges, fees and commissions	P	817,310
Net realized foreign exchange gain		483,246
Profit from assets sold		523,788
Other income		542,097
	P	2,366,441

(d) Itemized Deductions

The amounts of itemized deductions for the year ended December 31, 2012 are as follows:

Salaries and allowances	P	1,843,167
Taxes and licenses		674,977
Rental		552,159
Depreciation		350,532
Miscellaneous		761,662
		4,182,497
NOLCO applied		354,749
	P	4,537,246

Report of Independent Auditors To Accompany Supplementary Information Required by the Securities and Exchange Commission Filed Separately from the Basic Financial Statements

The Board of Directors and Stockholders
UnionBank of the Philippines
UnionBank Plaza, Meralco Avenue
Corner Onyx Street and Sapphire Road
Ortigas Center, Pasig City

We have audited in accordance with Philippine Standards on Auditing, the consolidated financial statements of UnionBank of the Philippines and subsidiaries (the Group) and of UnionBank of the Philippines (the Parent Company) for the year ended December 31, 2012, on which we have rendered our report dated March 22, 2013. Our audit was made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The applicable supplementary information (see Index to Supplementary Schedules under List of Supplementary Information) are presented for purposes of additional analysis in compliance with the requirements of the Securities Regulation Code Rule 68, and are not a required part of the basic financial statements prepared in accordance with financial reporting standards in the Philippines for banks. Such supplementary information are the responsibility of the Group's management. The supplementary information have been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

PUNONGBAYAN & ARAULLO

By: **Leonardo D. Cuaresma, Jr.**
Partner

CPA Reg. No. 0058647
TIN 109-227-862
PTR No. 3671448, January 2, 2013, Makati City
SEC Group A Accreditation
Partner - No. 0007-AR-3 (until Jan. 18, 2015)
Firm - No. 0002-FR-3 (until Jan. 18, 2015)
BIR AN 08-002511-7-2011 (until Sept. 21, 2014)
Firm's BOA/PRC Cert. of Reg. No. 0002 (until Dec. 31, 2015)

March 22, 2013

THE BANK

Union Bank of the Philippines
UnionBank Plaza
Meralco Avenue corner Onyx & Sapphire Roads
Ortigas Center, Pasig City 1605
Philippines

SOLE LEAD ARRANGER AND BOOKRUNNER

MARKET MAKER, and SELLING AGENT

The Hongkong and Shanghai
Banking Corporation Limited
8/F The Enterprise Center Tower I
6766 Ayala Avenue corner Paseo de Roxas
Makati City, Philippines

MARKET MAKER A

The Hongkong and Shanghai
Banking Corporation Limited
8/F The Enterprise Center Tower I
6766 Ayala Avenue corner Paseo de Roxas
Makati City, Philippines

SELLING AGENT

Multinational Investment
Bancorporation
22/F Multinational Bancorporation Center
6805 Ayala Avenue
Makati City, Philippines

SELLING AGENT *(TO THE EXTENT ALLOWED UNDER THE GOVERNING REGULATIONS)*

Union Bank of the Philippines
UnionBank Plaza
Meralco Avenue corner Onyx & Sapphire Roads
Ortigas Center, Pasig City 1605
Philippines

REGISTRAR AND PAYING AGENT

Deutsche Bank AG, Manila Branch
Tower Once,
Ayala Triangle
Makati City, Philippines

LEGAL ADVISER

To the Sole Lead Arranger
Romulo Mabanta Buenaventura Sayoc & de los Angeles
30/F Citibank Tower, Citibank Plaza
8741 Paseo de Roxas
Makati City, Philippines

INDEPENDENT AUDITOR

Punongbayan & Araullo
20/F The Enterprise Center Tower I
6766 Ayala Avenue
Makati City, Philippines