UNIONBANK

UnionBank Plaza
Meralco Avenue cor. Onyx &
Sapphire Roads, Ortigas Center
Pasig City 1605
Tel: (632) 667 6388 Fax: (632) 636 6289
www.unionbankph.com

May 15, 2009

The PHILIPPINE STOCK EXCHANGE, INC.
PSE Centre Exchange Road
Ortigas Center, Pasig City

Attention: **MS. JANET A. ENCARNACION**
Head, Disclosure Department

Dear Ms. Encarnacion:

In compliance with your reportorial requirement, we are transmitting to you herewith our SEC Form 17-Q report as revised for the period ended March 31, 2009.

Very truly yours,

5/15

VIRGINIA C. SAN PASCUAL
Senior Manager

COVER SHEET

3 6 0 7 3

S.E.C. Registration Number

U N I O N B A N K O F T H E P H I L I P P I N E S

(Company's Full Name)

U B P P L A Z A M E R AL C O A V E C O R N E R

O N Y X A N D S A P P H I R E S T S O R T I G A S

O R T I G A S C E N T E R P A S I G C E N T E R

(Business Address : No. Street City / Town / Province)

ATTY. CESAR G. ILAGAN

Contact Person

(632) 667-6388

Company Telephone Number

1 2 3 1

Month *Day*

Fiscal Year

SEC FORM 17Q

FORM TYPE

0 5 2 9

Month *Day*

Annual Meeting

UNDERWRITER OF SECURITIES

Secondary License Type, If Applicable

C F D

Dept. Requiring this Doc.

Amended Articles Number/Section

Total Amount of Borrowings

5 7 5 4

Total No. of Stockholders

Domestic

Foreign

To be accomplished by SEC Personnel concerned

File Number

LCU

Document I.D.

Cashier

S T A M P S

Remarks = pls. use black ink for scanning purposes

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-Q

QUARTERLY REPORT PURSUANT TO SECTION 17 OF THE SECURITIES REGULATION CODE AND SRC RULE 17(2)(b) THEREUNDER

1. For the quarterly period ended **March 31, 2009**

2. Commission identification number **3607**

3. BIR Tax Identification No. **000-508-271**

UNIONBANK OF THE PHILIPPINES
4. Exact name of registrant as specified in its charter

PHILIPPINES
5. Province, country or other jurisdiction of incorporation or organization

6. Industry Classification Code: ________ (SEC Use Only)

UBP Plaza, Meralco Avenue
Corner Onyx & Sapphire Sts., Ortigas Center, Pasig City **1605**
7. Address of principal office Postal Code

(632) 667-6388
8. Registrant's telephone number, including area code

Not applicable
9. Former name, former address and former fiscal year, if changed since last report

10. Securities registered pursuant to Section 8 and 12 of the Code, or Sections 4 and 8 of the SRC

Title of Each Class	Number of Share of Common Stock outstanding and amount of debt outstanding
Common Stock P10 par value	**641,422,420**

11. Are any or all of the securities listed on a Stock Exchange? Yes (x) No ( )
If yes, state the name of such stock exchange and the classes of securities listed therein:

Philippine Stock Exchange Common

12. Indicate by check mark whether the registrant:

(a) Has filed all reports required to be filed by Section 17 of the Code and SRC Rule 17 thereunder or Section 11 of SRC and SRC Rule 11 (a)-1 thereunder and Section 26 and 141 of the Corporation Code of the Philippines during the preceding 12 months (or for such shorter period the registrant was required to file such reports) Yes (x) No ( )

(b) Has been subject to such filing requirements for the past 90 days Yes (x) No ( )

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Attached are the following:

Consolidated Statement of Condition	-	Annex "1"
Consolidated Income Statement	-	Annex "2"
Consolidated Statement of Changes in Capital Funds	-	Annex "3"
Consolidated Cash Flow Statement	-	Annex "4"
Notes to Consolidated Financial Statements	-	Annex "5"

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Annex "6"

PART II - OTHER INFORMATION

There are no material disclosures that have not been reported under SEC Form 17C during the period covered by this report.

SIGNATURES

Pursuant to the requirements of the Securities Regulation code, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CESAR G. ILAGAN
Financial Controller

GUIA C. LIM
Executive Vice President

May 15, 2009

Annex "1"

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENT OF CONDITION
MARCH 31, 2009
(With Comparative Figures for December 31, 2008)
(Amounts in Thousands of Philippine Pesos)

	March 31, 2009	December 31, 2008
		(audited)
RESOURCES		
Cash and Other Cash items	2,999,470	3,881,824
Due from Bangko Sentral ng Pilipinas	21,250,105	22,237,389
Due from Other Banks	1,947,063	5,237,025
Interbank Loans Receivable	19,168,250	3,849,985
Trading and Investment Securities		
At fair value through profit or loss	563,718	583,071
Available-for-sale-net	38,368,523	27,534,918
Held- to-maturity-net	24,850,718	22,312,600
Loans and Other Receivables-net	77,810,044	90,725,554
Investment in Subsidiaries	0	0
Bank Premises, Furnitures, Fixtures and Equipment-net	2,952,269	3,019,278
Assets Held for Sale	138,805	255,144
Investment Properies	12,702,054	12,729,874
Goodwill	7,876,135	7,876,135
Other Resources - net	4,979,591	3,658,306
TOTAL RESOURCES	215,606,745	203,901,103
LIABILITIES AND CAPITAL FUNDS		
Deposit Liabilities		
Demand	94,265,574	90,457,169
Savings	15,552,564	14,557,542
Time	59,059,083	56,406,320
Total Deposit Liabilities	168,877,221	161,421,031
Bills Payable	8,934,335	2,156,437
Notes Payable	1,287,100	1,287,100
Other Liabilities	8,746,072	12,019,775
TOTAL LIABILITIES	187,844,728	176,884,343
Capital Funds		
Common Stock	6,414,224	6,414,224
Capital Paid in Excess of Par Value	5,819,861	5,819,861
Surplus	16,070,965	15,505,786
Surplus Reserve for Trust Business	99,076	99,076
Net Unrealized Gain/(Loss) on Available-for-Sale Securities	(642,109)	(822,187)
TOTAL CAPITAL FUNDS	27,762,017	27,016,760
TOTAL LIABILITIES AND CAPITAL FUNDS	215,606,745	203,901,103
Equity Attributable to Equity Holders of the Parent	27,762,017	27,016,760

Annex "2"

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES

INCOME STATEMENT

FOR THE PERIOD ENDED MARCH 31, 2009

(With Comparative Figures for March 31, 2008)

(Amounts in Thousands of Philippine pesos, Except Per Share Data)

	2009	2008
INTEREST INCOME ON		
Loans and other receivables	1,720,877	1,158,415
Investments and trading securities	986,394	689,573
Due from other banks	308,588	81,490
Interbank loans receivables	4,624	160,004
	3,020,483	2,089,482
INTEREST EXPENSE ON		
Deposit liabilities	1,527,101	669,909
Bills payable and other liabilities	48,229	164,877
	1,575,330	834,786
NET INTEREST INCOME	1,445,153	1,254,696
IMPAIRMENT LOSSES	171,000	100,000
NET INTEREST INCOME		
AFTER IMPAIRMENT LOSSES	1,274,153	1,154,696
OTHER INCOME		
Service charges, fees and commissions	185,743	194,092
Trading gain-net	137,551	118,087
Miscellaneous	537,472	344,914
	860,766	657,093
OTHER EXPENSES		
Salaries and employee benefits	479,696	449,564
Taxes and Licenses	178,449	139,351
Depreciation and amortization	109,390	94,235
Occupancy	105,702	87,805
Miscellaneous	557,506	341,992
	1,430,743	1,112,947
INCOME BEFORE INCOME TAXES	704,176	698,842
TAX EXPENSE	138,997	96,352
NET INCOME FOR THE PERIOD	565,179	602,490
Attributable to:		
Equity Holders of the Parent	565,179	602,490
Minority Interests	0	0
	565,179	602,490
Basic/Diluted Earnings Per Share		
Attributable to Equity Holders of the Parent	3.52	3.76

Annex "3"

UNIONBANK OF THE PHILIPPINES AND SUBSIDIARIES
STATEMENT OF CHANGES IN CAPITAL FUNDS
For the Period Ended March 31, 2009
(With Comparative Figures for March 31, 2008
(Amounts in Thousands of Philippine Pesos)

	2009	2008
Common Stock		
Balance at beginning of year	**6,414,224**	6,414,224
Issuance of additional shares	**0**	0
Balance at quarter end	**6,414,224**	6,414,224
Additional Paid-in Capital		
Balance at beginning of year	**5,819,861**	5,819,861
Issuance of additional shares	**0**	
Balance at quarter end	**5,819,861**	5,819,861
Surplus Free		
Balance at beginning of year	**15,505,786**	14,523,946
Net Income	**565,179**	602,490
Cash Dividends	**0**	0
Apropriation for trust business	**0**	0
Balance at quarter end	**16,070,965**	15,126,436
Surplus Reserves		
Balance at beginning of year	**99,076**	89,524
Transfer from surplus	**0**	0
Balance at quarter end	**99,076**	89,524
Net Unrealized Gain(Loss) on Available-for-sale Securities	**(642,109)**	(944,455)
	27,762,017	26,505,590

Annex "4"

UnionBank of the Philippines and Subsidiaries
Cash Flow Statement
For the Period ended March 31, 2009
(With Comparative Figures for March 31, 2008)
(Amounts in Thousands of Philippine Pesos)

	2009	2008
CASH FLOW FROM OPERATING ACTIVITIES		
Profit before income tax	**704,176**	698,842
Adjustments for:		
Provision for impairment losses	**171,000**	100,000
Loss (gain) on decline (appreciation) in fair value		
of Investment Properties	**12,889**	-
Depreciation and amortization	**109,390**	94,235
Changes in operating resources and liabilities:		
Decrease (increase) in:		
Financial Assets at Fair Value Through		
Profit and Loss	**19,353**	781,713
Loans and Receivables	**12,744,510**	(3,078,695)
Other Resources	**(1,362,669)**	(883,149)
Increase (decrease) in:		
Deposit Liabilities	**7,456,190**	959,026
Other Liabilities	**(3,285,899)**	(1,881,635)
Net cash generated from operations	**16,568,940**	(3,209,663)
Income taxes paid	**(97,305)**	(110,475)
Net cash provided by operating activities	**16,471,635**	(3,320,138)
CASH FLOW FROM INVESTING ACTIVITIES		
Net disposal (acquisition) of:		
Available-for-Sale Securities	**(10,653,527)**	(11,642,955)
Held-to-Maturity Investments	**(2,538,118)**	(499,603)
Property and equipment	**(30,493)**	(67,093)
Investment Properties	**131,270**	40,995
Net cash provided by (used in) investing activities	**(13,090,868)**	(12,168,656)
CASH FLOW FROM FINANCING ACTIVITIES		
Increase (decrease) in:		
Bills Payable	**6,777,898**	(26,745,427)
Net cash provied by (used in) financing activities	**6,777,898**	(26,745,427)
NET INCREASE IN CASH AND CASH EQUIVALENTS	**10,158,665**	(42,234,221)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		
Cash and Other Cash Items	**3,881,824**	4,044,666
Due from Bangko Sentral ng Pilipinas	**22,237,389**	11,403,892
Due from Other Banks	**5,237,025**	1,028,433
Interbank Loans Receivable	**3,849,985**	74,177,043
	35,206,223	90,654,034
CASH AND CASH EQUIVALENTS AT END OF YEAR		
Cash and Other Cash Items	**2,999,470**	2,932,420
Due from Bangko Sentral ng Pilipinas	**21,250,105**	12,154,537
Due from Other Banks	**1,947,063**	803,184
Interbank Loans Receivable	**19,168,250**	32,529,672
	45,364,888	48,419,813

"ANNEX 5"

UNIONBANK OF THE PHILIPPINES
GENERAL NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED MARCH 31, 2009

1. Corporate Information

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 is the result of the merger of its accounts with International Exchange Bank (iBank), effective April 30, 2006.

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 March 31, 2009, the Bank has 169 branches and 177 on-site and 14 off-site automated teller machines, located nationwide.

The Bank's common shares are listed in the Philippine Stock Exchange (PSE). The Bank is effectively 38.66% 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.

The Bank's subsidiaries (all incorporated in the Philippines), its effective percentage of ownership and the nature of the subsidiaries' businesses follow:

Subsidiary	Effective Percentage of Ownership	Nature of Business
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
Union Properties, Inc. (UPI)	100%	Real estate administration
Interventure Capital Corporation (IVCC)	60%	Venture capital

* FUDC and FUPI are wholly-owned subsidiaries of UPI.

2.1 Basis of Preparation of Financial Statements

(a) Statement of Compliance with Philippine Financial Reporting Standards

The consolidated financial statements of the Group have been prepared in accordance with Philippine Financial Reporting Standards (PFRSs). PFRSs are adopted by the Financial Reporting Standards Council (FRSC) from the pronouncements issued by the International Accounting Standards Board.

The financial statements have been prepared using the measurement bases specified by PFRS for each type of resource, liability, income and expense. These financial statements have been prepared on the historical basis, except for the revaluation of certain financial assets and investment properties. The measurement bases are more fully described in the accounting policies that follow.

(b) Functional and Presentation Currency

These financial statements are presented in Philippine pesos, the Group's functional and presentation currency, and all values represent absolute amounts except when otherwise indicated.

2.2 ***Impact of New Amendments and Interpretations to Existing Standards***

(a) Effective in 2008 that are Relevant to the Group

In 2008, the Group adopted for the first time the following new interpretation and amended standards which are mandatory in 2008.

Philippine Accounting Standard (PAS) 39 and PFRS 7 (Amendments)	:	PAS 39, Financial Instruments: Recognition and Measurement and PFRS 7, Financial Instruments: Disclosures
Philippine Interpretation IFRIC 14	:	PAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

Discussed in the succeeding sections are the impacts on the financial statements of these new accounting standards.

(i) PAS 39 (Amendment), *Financial Instruments: Recognition and Measurement* and PFRS 7 (Amendment), *Financial Instruments: Disclosures* (effective from July 1, 2008). The amendments permit an entity to, among others:

- reclassify non-derivative financial assets, other than those designated at FVTPL upon initial recognition, out of the FVTPL category:
  - a. 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,
  - b. if the financial asset would have met the definition of loans and receivables and if the financial asset had not been required to be classified as held-for-trading (HFT) at initial recognition and the entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity.
- transfer from AFS category to the loans and receivables category a non-derivative financial asset that would have met the definition of loans and receivables if the entity has the intention and ability to hold that financial asset for the foreseeable future or until maturity.

The amendments are applicable in a partially retrospective manner up to July 1, 2008 provided that the reclassification was made on or before November 15, 2008, the cut-off date set by FRSC. After the cut-off date, all reclassifications will only take effect prospectively.

Pursuant to these amendments and guidelines, the Group reclassified certain financial assets from AFS to HTM

(ii) Philippine Interpretation IFRIC 14, *PAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. This Philippine Interpretation provides general guidance on how to assess the limit in PAS 19, *Employee Benefits*, on the amount of the surplus that can be recognized as an asset. It standardizes practice and ensures that entities recognize an asset in relation to a surplus on a consistent basis. The Group has determined that this interpretation has no significant impact in the consolidated financial statements.

The first-time application of these amendments and interpretations has not resulted in any prior period adjustments of statement of condition, net income or cash flow line items.

(b) Effective in 2008 but not Relevant to the Group

Philippine Interpretation IFRIC 11	:	Group and Treasury Share Transactions
Philippine Interpretation		

IFRIC 12	:	Service Concession Arrangements

(c) *Effective Subsequent to 2008 which the Group Adopted Earlier*
In 2008, the Group decided to adopt early PAS 40 (Amendment), *Investment Property,* which is effective in 2009. PAS 40 is amended to include property under construction or development for future use as investment property in its definition of investment property. This results in such property being within the scope of PAS 40; previously, it was within the scope of PAS 16. Also, if an entity's policy is to measure investment property at fair value, but during construction or development of an investment property the entity is unable to reliably measure its fair value, then the entity would be permitted to measure the investment property at cost until construction or development is complete. At such time, the entity would be able to measure the investment property at fair value.

The early adoption of the Group of this amendment resulted to reclassification of certain properties under development from other resources to investment properties.

(d) *Effective Subsequent to 2008*
There are new and amended standards and Philippine Interpretation that are effective for periods subsequent to 2008. The following new standards, effective for annual periods beginning on or after January 1, 2009, are relevant to the Group which the Group will apply in accordance with their transitional provisions.

PAS 1 (Revised 2007)	:	Presentation of Financial Statements
PAS 27 (Revised 2009)	:	Consolidated and Separate Financial Statements
PAS 32 and PAS 1 (Amendments)	:	Financial Instruments: Presentation and Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation
PFRS 8	:	Operating Segments
Philippine Interpretation IFRIC 13	:	Customer Loyalty Programmes
Various Standards	:	2008 Annual Improvements to PFRS

Below is a discussion of the possible impact of these accounting standards.

(i) PAS 1 (Revised 2007), *Presentation of Financial Statements* (effective from January 1, 2009). The amendment requires an entity to present all items of income and expense recognized in the period in a single statement of comprehensive income or in two statements: a separate income statement and a statement of comprehensive income. The income statement shall disclose income and expense recognized in profit and loss in the same way as the current version of PAS 1. The statement of comprehensive income shall disclose profit or loss for the period, plus each component of income and expense recognized outside of profit and loss classified by nature (e.g., gains or losses on available-for-sale assets or translation differences related to foreign operations). Changes in equity (capital funds in the case of the Group) arising from transactions with owners are excluded from the statement of comprehensive income (e.g., dividends and capital increase). An entity would also be required to include in its set of financial statements a statement showing its financial position (or balance sheet) at the beginning of the previous period when the entity retrospectively applies an accounting policy or makes a retrospective restatement. The Group will apply PAS 1 (Revised 2007) in its 2009 consolidated financial statements.

(ii) PAS 27 (Revised), *Consolidated and Separate Financial Statements* (effective from July 1, 2009). The revised standard requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control and these transactions will no longer result in goodwill or gains and losses. The standard also specifies the accounting when control is lost. Any remaining interest in the equity is re-measured to fair value, and a gain or loss is recognized in profit or loss. Since there are no non-controlling interests in the subsidiaries within the Group, this revised standard has no impact in the Group's financial statements.

(iii) PAS 32 (Amendment), *Financial Instruments: Presentation* and PAS 1 (Amendment), *Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation* (effective from January 1, 2009). The amendments require certain financial instruments that represent a residual interest in the net assets of an entity, which would otherwise be classified as financial liabilities, to be classified as equity, if both the financial instrument and the capital structure of the issuing entity meet certain conditions. The Group does not expect any significant impact on its consolidated financial statements when it adopts the amendments in 2009.

(iv) PFRS 8, *Operating Segments*, (effective from January 1, 2009). Under this new standard, a reportable operating segment is identified based on the information about the components of the entity that management uses to make decisions about operating matters. In addition, segment assets, liabilities and performance, as well as certain disclosures, are to be measured and presented based on the internal reports prepared for and reviewed by the chief decision makers. The Group identifies operating segments and reports on segment assets, liabilities and performance based on internal management reports therefore, adoption of this new standard will not have a material impact on the Group's financial statements.

(v) Philippine Interpretation IFRIC 13, *Customer Loyalty Programmes*. This new Philippine Interpretation explains how entities that grant loyalty award credits to customers should account for their obligations to provide free or discounted goods or services to customers who redeem their award credits. Currently, the Group's loyalty points program arising from its credit card transactions are accounted for in accordance with this interpretation.

(vi) 2008 Annual Improvements to PFRS. The FRSC has adopted the *Improvements to International Financial Reporting Standards 2008*. These amendments become effective in the Philippines in annual periods beginning on or after January 1, 2009. The Group expects the amendments to the following standards to be relevant to the Group's accounting policies:

- PAS 23 (Amendment), *Borrowing Costs*. The amendment clarifies the definition of borrowing costs to include interest expense determined using the effective interest method under PAS 39. Management has initially assessed that the amendment has no effect in the Group's 2009 financial statements.

- PAS 1 (Amendment), *Presentation of Financial Statements*. The amendment clarifies that financial instruments classified as held for trading in accordance with PAS 39 are not necessarily required to be presented as current assets or current liabilities. Instead, normal classification principles under PAS 1 should be applied. Since the Group does not distinguish current and non-current resources and liabilities for financial statement presentation, the amendment has no impact in the Group's financial statements.

- PAS 19 (Amendment), *Employee Benefits*. The amendment includes the following:

  - Clarification that a curtailment is considered to have occurred to the extent that benefit promises are affected by future salary increases and a reduction in the present value of the defined benefit obligation results in negative past service cost.
  - Change in the definition of return of plan assets to require the deduction of plan administration costs in the calculation of plan assets return only to the

extent that such costs have been excluded from measurement of the defined benefit obligation.

- Distinction between short-term and long-term employee benefits will be based on whether benefits are due to be settled within or after 12 months of employee service being rendered.
- Removal of the reference to recognition in relation to contingent liabilities in order to be consistent with PAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, which requires contingent liabilities to be disclosed and not recognized.

Management is currently evaluating the impact of this amendment in its 2009 consolidated financial statements.

- PAS 38 (Amendment), *Intangible Assets*. The amendment clarifies when to recognize a prepayment asset, including advertising or promotional expenditures. In the case of supply of goods, the entity recognizes such expenditure as an expense when it has a right to access the goods. For services, an expense is recognized on receiving the service. Also, prepayment may only be recognized in the event that payment has been made in advance of obtaining right of access to goods or receipt of services. The Group initially determined that adoption of this amendment will not have a material effect on its 2009 consolidated financial statements.

- PAS 39 (Amendment), *Financial Instruments: Recognition and Measurement*. The definition of financial asset or financial liability at fair value through profit or loss as it relates to items that are held for trading was changed. A financial asset or liability that is part of a portfolio of financial instruments managed together with evidence of an actual recent pattern of short-term profit taking is included in such a portfolio on initial recognition. The Group is currently determining the possible impact of this amendment on its 2009 financial statements.

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, 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 consolidated financial statements.

The financial statements of subsidiaries are prepared for the same reporting period as the Bank, using consistent accounting principles.

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 commonly exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which the Group obtains control and are de-consolidated from the date the control ceases.

Unrealized gains on transactions between the Group and its subsidiaries are eliminated to the extent of the Group's interest in the subsidiaries. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies have been changed where necessary to ensure consistency with the policies adopted by the Group.

Subsidiaries are consolidated from the date the Bank obtains control until such time that such control ceases.

Acquired subsidiaries are subject to the application of the purchase method for acquisitions. This involves the revaluation at fair value of all identifiable assets and liabilities, including contingent liabilities of the subsidiary, at the acquisition date, regardless of whether or not they were recorded in the financial statements of the subsidiary prior to acquisition. On initial recognition, the assets and liabilities of the subsidiary are included in the consolidated statement of condition at their revalued amounts, which are also used as the bases for subsequent measurement in accordance with the Group accounting policies.

Goodwill (positive) represents the excess of the acquisition cost over the fair value of the former iBank's identifiable net assets on its merger with the Bank on April 30, 2006

2.4 ***Financial Assets***

Financial assets include cash and financial instruments. The Group classifies its financial assets into the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and

available-for-sale 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. The designation of financial assets is re-evaluated at every reporting date at which date a choice of classification or accounting treatment is available, subject to compliance with specific provisions of applicable accounting standards.

Cash and other cash items comprise of cash and amounts due from other banks. For purposes of reporting cash flows, cash and cash equivalents include cash and other cash items, amounts due from BSP and other banks and interbank loans receivable.

Regular purchase 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 transaction costs. Financial assets carried at FVTPL are initially recognized at fair value and transaction costs are expensed in the income statement.

The foregoing categories of financial instruments are more fully described below.

(a) *Financial Assets at Fair Value through Profit or Loss*

This category includes derivative financial instruments and financial assets that are either classified as held for trading or are designated by the Group to be carried at fair value through profit or loss upon initial recognition. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorized as "held-for-trading" unless they are designated as hedges.

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 HFT 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. 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. It is established through an allowance account which is charged to expense. Loans and receivables are written off against the allowance for impairment losses when management believes that the collectibility of the principal is unlikely, subject to BSP regulations.

(c) *Held-to-maturity Investments*
These include non-derivative financial assets with fixed or determinable payments and a fixed date of maturity. Investments are classified as held-to maturity if the Group has the positive intention and ability to hold them until maturity. Investments intended to be held for an undefined period are not included in this classification.

Held-to-maturity 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. 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 held-to-maturity investments, the entire category would be tainted and reclassified as available-for-sale securities. The tainting provision will not apply if the sales or reclassifications of held-to-maturity 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.

(d) *Available-for-sale Securities*
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, with changes in value recognized in capital funds, net of any effects arising from income taxes. Gains and losses arising from securities classified as available-for-sale are recognized in the income statement when they are sold or when the investment is impaired.

In the case of impairment, the cumulative loss previously recognized directly in capital funds is transferred to the income statement. If circumstances change, impairment losses on available-for-sale financial assets are not reversed through income statement. Losses recognized in prior period consolidated income statement resulting from the impairment of debt instruments are reversed through the income statement, when there is recovery in the amount of previously recognized impairment losses.

For investments that are actively traded in organized financial markets, fair value is determined by reference to stock exchange quoted market bid prices at the close of business on the statement of condition date. For investments where there is no quoted market price, fair value is determined by using valuation techniques. Valuation techniques include using recent arm's length transactions, reference to the current fair value of another instrument which is substantially the same, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Gains and losses arising from changes in the fair market value of the financial assets at fair value through profit or loss category are included in Trading Gain account in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale securities are recognized directly in capital funds, until the financial asset is derecognized or impaired at which time the cumulative gain or loss previously recognized in capital funds shall be recognized in profit or loss. However, interest calculated using effective interest method is recognized in the income statement. Dividends on available-for-sale equity instruments are recognized in the income statement when the entity's right to receive payment is established.

Non-compounding interest 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.

Derecognition of financial assets occurs when the rights to receive cash flows from the financial instruments expire or are transferred and substantially all of the risks and rewards of ownership have been transferred.

2.5 ***Derivative Financial Instruments***

The Group is a party to various options, foreign currency forwards and swaps, and interest rate swap contracts. These contracts are entered into as a means of reducing or managing the Group's foreign exchange and interest rate exposures and as a service to customers, as well as for trading purposes.

Derivatives are initially recognized at fair value on the date on which derivative contract is entered into and are subsequently measured at their fair value. 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 profits 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, usually an increase, 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 condition.

Certain derivatives embedded in other financial instruments, such as the conversion option in a convertible 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 the income statement.

Changes in the fair value of derivatives are recognized in profit or loss.

2.6 Non-current Assets Held-for-Sale

Non-current assets held-for-sale include real and other properties acquired through repossession or foreclosure that the Group intends to sell within one year from the date of classification as held for sale.

Non-current 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 income statement.

2.7 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. When assets are sold, retired or otherwise disposed of, their cost and related accumulated depreciation and amortization and impairment losses are removed from the accounts and any resulting gain or loss is reflected in income for the period.

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

The residual values and estimated useful lives of bank premises, furniture, fixtures and equipment are reviewed, and adjusted if appropriate, at each statement of condition date.

An item of bank premises, furniture, fixtures and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the period the item is derecognized.

2.8 Investment Properties

Investment properties are measured initially at acquisition cost which comprise its purchase price and directly attributable cost incurred. These include land and building 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 appraisers The carrying amounts recognized in the statement of condition reflect the prevailing market conditions at the statement of condition date.

Any gain or loss resulting from either a change in the fair value or the sale of an investment property is immediately recognized in the income statement as Fair Value Gains from Investment Properties under Other Income account in the income statement.

Investment property is 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 the income statement 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.

2.9 Intangible Assets

Goodwill represents the excess of the cost of acquisition over the fair value of the Bank's acquisition of the assets and liabilities of the former iBank. 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 the basis of the expected useful lives of five to ten years. Costs associated with maintaining computer software are expensed as incurred.

2.10 Land Trust Investment

The properties contributed by the Group under the agreement were reclassified from Other Resources to Investment Properties account, in accordance with the Group's early adoption of PAS 40. This account was measured previously at the lower of cost and net realizable value under Other Resources and valued at fair value at the date of reclassification to Investment Properties.

2.11 Financial Liabilities

Financial liabilities include deposit liabilities, bills payable, notes payable, outstanding acceptances payable, due to other banks, derivative liabilities, accrued taxes, interest and other expenses, and other liabilities.

Financial liabilities are recognized when the Group becomes a party to the contractual agreements of the instrument.

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 bonds payable are subsequently stated at amortized cost; any difference between the proceeds, net of transaction costs and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest method.

Derivative liabilities are recognized initially and subsequently measured at fair value with changes in fair value recognized in the income statement.

Accrued taxes, interests and other expenses and other liabilities are recognized initially at their fair value and subsequently measured at amortized cost 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 condition only when the obligations are extinguished either through discharge, cancellation or expiration.

2.12 Offsetting Financial Instruments

Financial assets and liabilities are offset and the net amount reported in the statement of condition when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

2.13 Provisions

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 commitment that has resulted from past events, for example, legal disputes or onerous contracts.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the statement of condition date, 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, where time value of money is material.

Provisions are reviewed at each statement of condition date 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.

Probable 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.

2.14 Pre-Need Reserves (PNR) and Insurance Premium Reserves (IPR)

In the Group’s consolidated financial statements, PNR 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, *Provisions, Contingent Liabilities and Contingent Assets*, and the specific method of computation required by the SEC 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 statement of condition date. 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 SEC 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.

2.15 Capital Funds

Common stock is determined using 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.

Surplus free includes all current and prior period results as disclosed in the income statement 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 gain (loss) on available-for-sale securities pertain to cumulative mark-to-market valuation of available-for-sale financial assets.

2.16 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. Specific recognition criteria of income and expenses described below must also be met before revenue is recognized.

(a) *Interest* – Interest income and expenses are recognized in the income statement 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) *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.

(c) *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 the outstanding securities classified as FVTPL at quarter-end.

(d) *Profit from assets sold or exchanged* – Profit 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. This is included in the Other Income account in the income statement.

(e) *Dividends* – Dividend income is recognized when the Group's right to receive payment is established. Dividend income is included as part of Miscellaneous Income (Charges) account in the income statement.

(f) *Rental income* – Rental income arising from leased properties is accounted for on a straight-line basis over the lease terms on ongoing leases and is recorded in the income statement as part of Other Income.

(g) *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.

Cost and expenses are recognized in the income statement upon utilization of the assets or services or at the date these are incurred. All finance costs are reported on an accrual basis.

2.17 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 the income statement on a straight-line basis over the lease term. Associated costs, such as 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 the income statement 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.

2.18 Functional Currency and Foreign Currency Transactions

(a) Functional and Presentation Currency

Items included in the financial statements of the Group are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The financial statements are presented in Philippine peso, which is also the Group's functional and presentation currency. The financial statements of the foreign currency deposit unit (FCDU) of the Bank which are also expressed in Philippine pesos as its presentation currency, are translated using the prevailing current exchange rates for statement of condition accounts and average exchange rate during the period for income statement accounts.

(b) Transactions and Balances

The accounting records of the Group are maintained in Philippine pesos, except for the FCDU which are maintained in U.S. 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 monetary assets and liabilities of the Bank's FCDU are translated to Philippine pesos based on the Philippine Dealing System closing rates (PDSCR) prevailing at the end of the quarter, while income statement accounts are translated to Philippine pesos using the PDS weighted average rate (PDSWAR) for the quarter.

Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at closing exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement.

2.19 Impairment of Financial Assets

The Group assesses at each statement of condition date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is 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, the Group includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. 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 receivable or held-to-maturity 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 the income statement. If a loan or held-to-maturity 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 and subject to BSP guidelines, it is written off 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 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 the income statement.

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 the income statement.

(b) *Assets Carried at Fair Value with Changes Recognized to Capital Funds*
In the case of investments classified as available-for-sale 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 available-for-sale 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 capital funds and recognized in the income statement. Impairment losses recognized in the income statement on equity instruments are not reversed through the income statement.

If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale 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 the income statement.

(c) Assets Carried at Cost

The Group assesses at each statement of condition date 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 income statement.

2.20 Impairment of Non-financial Assets

The Group's investments in subsidiaries, intangible assets (consisting of goodwill and computer software and recorded as part of Other Resources), bank premises, furniture, fixtures and equipment, investment properties and non-current assets held-for-sale are subject to impairment testing. Intangible assets with an indefinite useful life or 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. The recoverable amount is the higher of fair value, reflecting market conditions less costs to sell and value in use, based on an internal discounted cash flow evaluation. Impairment loss is charged pro rata to the other assets in the cash generating unit.

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.

2.21 Employee Benefits

(a) Retirement Benefit Obligations

Retirement benefits are provided to employees through a defined benefit plan, as well as a defined contribution plan.

The defined benefit plan is a retirement plan that defines an amount of retirement 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 retirement 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 defined benefit retirement plan covers all regular full-time employees. The retirement plan is tax-qualified, noncontributory and administered by a trustee.

The liability recognized in the statement of condition for defined benefit retirement plans is the present value of the defined benefit obligation (DBO) at the statement of condition date less the fair value of plan assets, together with adjustments for unrecognized actuarial gains or losses and past service costs. The DBO is calculated 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 high quality corporate bonds 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 retirement 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 the income statement, unless the changes to the pension 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.

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.

(b) 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: (a) terminating the employment of current employees due to resignation; or (b) providing termination benefits as a result of a redundancy. Benefits falling due more than 12 months after the statement of condition date are discounted to present value.

(c) 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 Company also recognizes a provision for profit-sharing and bonus plans where there is a past practice that has created a constructive obligation.

(d) Compensated Absences
Compensated absences are recognized for the number of paid leave days (including holiday entitlement) remaining at the statement of condition date. They are included in the Accrued Taxes, Interest and Other Expenses account at the undiscounted amount that the Group expects to pay as a result of the unused entitlement.

2.22 Income Taxes

Current tax assets or liabilities comprise those claims from, or obligations to, tax authorities relating to the current or prior reporting period, that are unpaid at the statement of condition date. They are calculated according to the tax rates and tax laws applicable to the 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 the income statement.

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

Under the balance sheet 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.

The carrying amount of deferred tax assets is reviewed at each statement of condition date 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 statement of condition date.

Most changes in deferred tax assets or liabilities are recognized as a component of tax expense in the income statement. Only changes in deferred tax assets or liabilities that relate to a change in value of assets or liabilities that is charged directly to capital funds are charged or credited directly to capital funds.

2.23 Related Parties

Parties are considered related when one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

2.24 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 issued during the period. However, net income attributable to common shares and the weighted average number of common shares outstanding are adjusted to reflect the effects of any potentially dilutive preferred shares, stock options and warrants. As of March 31, 2009 and 2008, the Group has no outstanding potentially dilutive securities, hence, the basic earnings per share are equal to diluted earnings per share.

2.25 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 income arising thereon are excluded from these financial statements, as they are not resources of the Group.

2.26 Segment Reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

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.

2.27 Subsequent Events

Any post-quarter-end event that provides additional information about the Group's position at the statement of condition date (adjusting event) is reflected in the financial statements. Post-quarter-end events that are not adjusting events, if any, are disclosed when material to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES

The Group's financial statements prepared in accordance with PFRS require management to make judgments and estimates that affect 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 circumstances. Actual results may ultimately differ from these estimates and the difference could be significant.

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) 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) Held-to-maturity Investments

The Group follows the guidance of PAS 39, *Financial Instruments: Recognition and Measurement*, in classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgment. In making this judgment, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments at maturity other than for the allowed specific circumstances – for example, selling a not insignificant amount close to maturity – it will be required to reclassify the entire class to available-for-sale securities. The investments would therefore be measured at fair value and not at amortized cost.

(c) Impairment of Available-for-sale Financial Assets

The Group follows the guidance of PAS 39, *Financial Instruments: Recognition and Measurement*, in determining whether an investment is permanently impaired. This determination 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.

(d) Distinction Between Investment Properties and Owner-occupied Properties

The Group determines whether a property qualifies as investment property. In making its judgment, the Group considers whether the property generated cash flows largely independently 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 portion can be sold separately (or leased out separately under finance lease), the Group accounts for the portions separately. If the portion 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) 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.

Rent expense charged to operations amounted to P76,066 in March 2009 and P63,174 in March 2008 in the consolidated financial statements. Rent income earned by the Group amounted to P22,487 in March 2009 and P19,726 in March 2008.

(f) *Classification of Acquired Properties and Fair Value Determination of Non-current 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 Non-current Assets Held-for-Sale if the Group expects that the properties will be recovered through sale 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 internal and external appraisers. The appraised value is determined based on the current economic and market conditions as well as the physical condition of the property.

(g) *Provisions and Contingencies*
Judgment is exercised by management to distinguish between provisions and contingencies.

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 statement of condition date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

(a) *Impairment Losses on Financial Assets (AFS securities, loans and receivables and held-to-maturity investments)*
The Group reviews its loan and held-to-maturity investments portfolios to assess impairment at least on an annual basis. In determining whether an impairment loss should be recorded in the income statement, 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.

The Group carries certain financial assets at fair value, which requires the extensive use of accounting estimates and judgment. Significant components of fair value measurement were determined using verifiable objective evidence such as foreign exchange rates, interest rates, volatility rates. However, the amount of changes in fair value would differ if the Group utilized different valuation methods and assumptions. Any change in fair value of these financial assets and liabilities would affect profit and loss and equity.

(b) *Fair Values of Financial Assets and Liabilities*

(i) *Due from other banks and BSP*
Due from BSP pertains to deposits made by the Group to BSP for clearing and reserve requirements. Due from other banks includes 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) Available-for-sale securities
The fair value of available-for-sale securities is determined by direct reference to published price quoted in an active market for traded securities. On the other hand, non-quoted available-for-sale securities are carried at cost because the fair value cannot be reliably determined either by reference to similar financial instruments or through valuation technique.

(iii) Held-to-maturity investments
Fair value for held-to-maturity assets 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 non-interest-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) 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 each statement of condition date.

(d) Useful Lives of Bank Premises, Furniture, Fixtures and Equipment
The Group estimates the useful lives of bank premises, furniture, fixtures and equipment and investment properties 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 investment properties 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 investment properties is based on collective assessment of industry practice, internal technical evaluation and experience with similar assets. It is possible, however, that future results of operations could be materially affected by changes in estimates brought about by changes in factors mentioned above. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of bank premises, furniture, fixtures and equipment and investment properties would increase recorded operating expenses and decrease bank premises, furniture, fixtures and equipment and investment properties.

Bank premises, furniture, fixtures and equipment net of accumulated depreciation and amortization amounted to P2,952,269 and P3,019,278 as of March 31, 2009 and December 31, 2008, respectively, in the consolidated financial statements.

(e) *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 as of statement of condition date. Any gain or loss from change in fair value of investment properties is included in the income statement in the period when the valuation was performed.

(f) *Realizable Amount of Deferred Tax Assets*
The Group reviews its deferred tax assets at each statement of condition date 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.

(g) *Impairment of Non-financial Assets*
Except for intangible assets with indefinite useful lives, PFRS requires that an impairment review be performed when certain impairment indicators are present. 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.

(h) *Retirement and Other Benefits*
The determination of the Group's obligation and cost of pension and other retirement benefits is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. 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 Parent Company 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 statement of condition dates.

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's principal financial instruments, other than derivatives, consist of financial assets at fair value through profit or loss, available-for-sale securities, held-to-maturity investments, loans and receivables, interbank loans receivable, and financial liabilities such as deposit, 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 the Group's operations.

The Group is exposed to risks that are particular to its lending and trading businesses and the environment within which it operates. The Group's goal in risk management is to ensure that it identifies, understands, measures and monitors the various risks that arise from the financial instruments it invests in and that it adheres strictly to the policies, procedures and controls which are established to address these risks. The key risks that the Group faces are: credit risk, market risk, liquidity risk, foreign exchange risk and operational risk. It is also exposed to other types of risks such as technology risk, strategic and business risks and legal risk.

4.1 *Enterprise-wide Risk Management*

An emerging model is to be able to manage risk across all units of the Group by applying the enterprise-wide risk management approach. It considers identifying, measuring, monitoring, and controlling/mitigating all types of risk that is present in the Group. It recognizes that risk management is a continuing process and for all risks that are being taken, there underlies opportunities for the Bank to earn profitably. It considers that the Parent Company must promote an efficient and effective process for the assessment of risk, increase risk awareness, and improve the management of risk all throughout the Parent Company. The Parent Company is in the business of taking risk and as such, the basic objective of enterprise-wide risk management is not to eliminate risk but provide a way on how risk can be properly managed.

4.1.1 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 real and other properties acquired ("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 firm-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 counsel to the other committees including the Market Risk Committee ("MRC") and the Operations Risk Management Committee ("ORMC").

(c) The MRC, composed of the Chairman of the BOD, the President and three other 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) *Audit Committee*

The Audit Committee is a committee of the BOD that plays a key role in corporate governance. It is composed of five 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 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.

(iii) *Oversight of the risk management process***.** This function involves receiving from senior management periodic information on risk exposure and risk management activities, such as those relating to operation, legal and other risks facing the Parent Company.

In the performance of these functions, the Audit Committee is supported by the IAD, as led by the IAD Head. 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 only 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 frequencies, select subjects, determine scopes 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, headed by an independent board member, 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.

(f) Corporate Governance Committee

The Corporate Governance Committee ("CGC") serves as the primary resource for the BOD to study, evaluate and make recommendations about the structure, charter, policies and practices of the BOD and its committees in order to improve corporate governance. It is responsible for ensuring the BOD's effectiveness and due observance of corporate governance principles and guidelines. The CGC is composed of seven members of the following: six members of the BOD, two of whom are independent directors; and one member who belongs to the Parent Company's senior management.

The Committee has two sub-committees: the Nominations Sub-Committee, which pre-screens candidates for members of the BOD, and the Compensation and Remuneration Sub-Committee, which recommends and oversees the program of salaries and benefits for directors and senior management in order to attract the best talents for the Parent Company. The Nomination Sub-Committee has three voting members who are directors, one of whom is an independent director; and one non-voting member who is the Parent Company's Human Resources director. The Compensation and Remuneration Sub-Committee has three members, one of whom is an independent director.

The Parent Company's Risk Management Group ("RMG") is 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, and, in coordination with the respective business units, is 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 RMG'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 that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The risk may arise from lending, trade finance, treasury, investments, derivatives and other activities undertaken by the Parent Company. The Parent Company's credit risk and loan portfolio is managed by the RMG at the transaction, borrower, product and portfolio levels. The Parent Company has structured and standardized credit ratings and approval processes according to the business and/or product segment.

The RMG undertakes several functions with respect to credit risk management. The RMG independently performs credit analysis and review for both retail 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 constantly evolve to meet the changing demands of the business. The RMG is also responsible for developing procedures to streamline and expedite the processing of credit applications.

The RMG reviews the Parent Company's loan portfolio in line with the Parent Company's policy of not having 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 that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. 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 specific guidelines for maintaining a diversified portfolio (e.g. concentration limit). Identified concentrations of credit risks are controlled and managed accordingly. RMG 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

For large corporate credit transactions, the Bank has a comprehensive procedure for credit evaluation and risk assessment. It also has well-defined concentration limits which are established for each type of borrower, individual risk rating and type of product or program to mitigate risk exposure across business units.

The Bank has a credit scoring system for corporate financial products that assesses risks relating to the borrower and the loan exposure. 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 above 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.

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 thru 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.

Marginal - 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 represent inadequacy of cash flows and a real risk to non-payment of principal. The probability of default increases as we go down from a credit score of CCC and lower.

In addition to the BRR, the Bank assigns a loan exposure rating (“LER”), a 100-point system which comprises 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 except when 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. The industry risk evaluation is performed by an independent research unit, a non-lending unit, to ensure objectivity in the credit scoring system. Any major change in the credit scoring system, the RAAC range and/or the risk-adjusted pricing system is presented and approved by the EC.

4.2.2 Commercial Loans

The Parent Company’s commercial banking activities are undertaken by its Commercial Banking Center (ComBank) and comprise the provision of banking products and services to customers from entities that are predominantly belonging to the small and medium scale enterprises (“SMEs”) group. The products and services provided to commercial banking customers include similar products and services provided to large corporate customers under the Parent Company’s corporate banking segment, as well as trade finance related products and services.

ComBank uses a 10-scale credit scoring system separate and distinct from the RAAC system used by the Corporate Banking Group. ComBank’s rating system consists of the following: an Obligor Risk Rating (“ORR”), a Facility Risk Adjustment (“FRA”), a Final Risk Rating (“FRR”) and an Estimated Cash Risk Position taking into account security items.

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 condition 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 more than high risk, thus may be required by the Bank to pledge very satisfactory collateral.

Substantially Risk Free (with credit score of 1) - 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 thru the public markets at any time.

Minimal Risk (with credit score of 2) - 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 (with credit score of 3)- 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(with credit score of 4) - 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 (with credit score of 5) - 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 (with credit score of 6) - 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 (with credit score of 7 and below)- 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.

With the ORR is 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 the Adjusted Obligor Risk Rating ("AORR").

After rating the account, the Account Officer submits a recommended FRR based on the AORR and all other perceived relevant factors which may or may not have been considered in the credit scoring system. The above description of Combank's credit score will then apply to the recommended 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 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 single 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 was initially provided by a foreign consultant but 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 Collateral Held As Security and Other Credit Enhancements

The Group holds collateral against loans and receivables from customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over due from other banks, interbank loans and investment securities, except when securities are held as part of reverse repurchase and securities borrowing activity.

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. 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 limits 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.

Liquidity is monitored by the Group on a daily basis and under stressed situations.

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 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 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 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 are monitored on a daily basis. Limits are based on the tolerable risk appetite of the Group.

4.4 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 would be in a better position to invest in higher yielding assets more quickly than it would need to refinance its interest-bearing liabilities. During a period of falling interest rates, a company with a positive gap would tend to see its assets repricing at a faster rate than one with a negative gap, which may restrain the growth of its net interest income or result in a decline in net interest income.

4.5 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 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.

4.6 Operational Risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events.

The Bank's exposure to operational risk is managed by the ORMC and an independent ORMC director.

The ORMC, composed of senior directors and senior management officers of the Parent Company, covers the following areas of concern:

1. 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.

2. Results of periodic or special risk assessments conducted in various business and operating units of the Parent Company to proactively uncover operational risks that can result to actual loss or damage to the Parent Company.

3. Summarized results of internal audits, BSP examinations and investigation of administrative cases that highlight trends indicative of present or emerging exposures to specific operational risks.

4. Risk assessment of major information systems to be implemented in the Parent Company.

5. Regulatory compliance issues, whether currently existing, or anticipated to arise as a result of new laws or regulations.

6. Business continuity strategies, plans, and resources. The ORMC director has been mandated 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 that have been culled from various papers of the Parent Company from the Bank for International Settlements or the Basel Committee, and as applied by other foreign and local financial institutions.

The Parent Company, however, has already embedded in its processes the basic strategies necessary in order to manage exposure to operations risk prior to the formal creation of this unit. Foremost is the proper segregation of duties and responsibilities. It has been ensured that no person will be able to approve his own transaction, and created the necessary control layers to provide check and balance. Even in the use of a straight-thru processing and technology, it also made certain that proper control processes are in place to adequately handle operational risk exposures.

For managing products and services, the following are the basic guidelines that are being followed. First, no new products or services are to be implemented without performing operations risk assessment. As part of the product approval process, product managers make sure that risks were clearly identified and adequately controlled and mitigated. Second, for existing products and services, regular review is being conducted and that previous controls are also being assessed to determine its effectiveness and whether new risks have arisen during the product/service implementation.

In terms of policies and documentation, all manuals and Parent Company circulars are regularly reviewed and updated as new regulations and policies are being issued. This will ascertain that the Parent Company manuals will be a rich source of material on how transactions are to be handled and that proper controls are to be observed in processing these transactions. Amendments to these manuals are disseminated and implemented through circulars sent to all offices.

In the use of technology, the Parent Company has institutionalized the application of Technology Risk Assessment to form the basis for identifying the risk in various systems that the Parent Company is using. Accordingly, control and mitigation processes are to be put in place with the objective of ensuring continuous operations in case of system failures. Overall, the Parent Company has developed a Business Continuity Plan that shall be used as basis of what units will do in case of unexpected events. This will give comfort that services can proceed even in case of disasters.

Moving towards the use of mathematical models in managing operations risk, the Parent Company is starting to centralize all information related to losses and near losses that the Parent Company has experienced. This can very well be the source of creating metrics that will enable the Parent Company to monitor and assess its operational risk profile. Using the information, key risk indicators can be developed that will help the Parent Company proactively manage operations risk. Mathematical models can also be formed to have a realistic basis for determining capital charge allocated for operations risk with the ultimate goal of lowering the risk.

4.7 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 or later 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.

4.8 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-collections or non-enforcement of claims. The Bank has established measures to avoid or mitigate the effects of these adverse decisions and through the engagement of several qualified legal advisors, as carefully endorsed to and approved by senior management.

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 Compliance Officer. The 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 or the capital adequacy ratio ("CAR"). Risk-weighted assets is the sum of credit risk, market risks, and operational risks, computed 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 shall 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 last 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 unsecured subordinated term debt instruments of other banks/quasi-banks qualifying as Hybrid Tier 1, Upper Tier 2 and Lower Tier 2, in excess of the lower of (i) an aggregate ceiling of 5% of total Tier 1 capital of the bank excluding Hybrid Tier 1; or (ii) 10% of the total outstanding unsecured subordinated term debt issuance of other banks/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 upon 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.

5.2 Minimum Capital Requirement

Under the relevant provisions of the current BSP regulations, the minimum capitalization of the Bank is P4.95 billion. As of March 31, 2009 and 2008, the Bank is in compliance with this regulation.

6. SEGMENT INFORMATION

The Group's main operating businesses are organized and managed separately according to the nature of services provided and the different markets served, with each segment representing a strategic business unit. 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*
Principally 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. Segment revenues and expenses that are directly attributable to primary 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.

Segment information of the Group as of and for the quarters ended March 31, 2009 and 2008 is presented as follows (amounts in millions of Philippine pesos):

March 31, 2009	**Consumer Banking**	**Corporate and Commercial Banking**	**Treasury**	**Headquarters**	**Total**
Results of operations					
Net interest income and other income	P 1,003	P 465	P 889	(P 51)	P 2,306
Other expenses	(642)	(158)	(125)	(505)	1,431
Income before provision for impairmentand income tax	**360**	**P 308**	**P 763**	**(P 556)**	875
Provision for impairment					(171)
Tax expense					(139)
Net income					**P 565**
Segment resources	**P 32, 594**	**P 58,710**	**P 110,655**	**P 13,648**	**P 215,607**
Segment liabilities	**P 105,378**	**P 48,678**	**P 32,665**	**P 1,124**	**P 187,845**

March 31, 2008	**Consumer Banking**	**Corporate and Commercial Banking**	**Treasury**	**Headquarters**	**Total**
Results of operations					
Net interest income and other income	P 944	P 317	P 499	P 151	P 1,911
Other expenses	(502)	(109)	(105)	(397)	(1,113)
Income before provision for					

impairment and income tax	P 442	P 208	P 394	(P 246)	798
Provision for impairment					(100)
Tax expense					(96)
Net income					P 602
Segment resources	P 26,105	P 49,883	P 74,158	P 9,985	P 160,131
Segment liabilities	P 73,689	P 23,215	P 31,251	P 5,502	P 133,657

Notes Payable

The Group's notes payable as of March 31, 2009 and December 31, 2008 of P1,287,100 pertain to the outstanding balance of unsecured subordinated notes (the Notes) issued by the former iBank on March 23, 2006 due on September 24, 2016 and callable on September 23, 2011. Among the significant terms and conditions of the issuance of the Notes are stated below:

a. The Notes shall be issued on the initial issue date at 100% of the face value of the Notes, while the Notes issued on subsequent issue dates will be issued at par, discount or premium depending on market conditions at the time of their 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 bear 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 is not exercised) or the call option date (if the call option is exercised). The interest rate from and including September 23, 2011 up to but excluding September 23, 2016 will be reset and such step-up interest rate shall be payable to the Noteholders beginning on the 12th interest period up to the last interest period in the event that the Parent Company does not exercise the call option;

c. 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;

d. 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,

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

Related Party Transactions

In the ordinary course of business, the Parent Company transacts with its subsidiaries and with certain directors, officers, stockholders and other related interests (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, 70% of which must be secured should not exceed the amount of their respective deposits and book value of their investments in the Parent Company. These limits do not apply to loans secured by assets considered nonrisk as defined in the regulations. In the aggregate, loans to DOSRI should not exceed the total capital funds or 15% of the total loan portfolio of the Parent Company, whichever is lower. As of March 31, 2009 and December 31, 2008, the Parent Company is in compliance with these regulatory requirements.

Commitments and Contingencies

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 March 31, 2009, 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:

	2009	2008
Trust department accounts	11,798,646	22,896,198
Inward bills for collections	4,720,075	5,118,661
Unused commercial letters of credit	3,160,454	2,135,465
Outstanding guarantees issued	390,287	523,132
Outward bills for collection	66,574	52,109
Late deposits/payments received	36,269	117,746
Unsold travellers' checks	16,152	17,522
Other contingent accounts	2,247	1,889

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.

Financial Performance

The basis of calculation for earnings per share equity attributable to equity holders of the Parent as follows:

		March 31, 2009	March 31, 2008
a.	Net income (annualized for Interim periods, in thousands)	565.179	602,490
b.	Weighted average number of outstanding common Shares Of the Parent Company (in thousands)	641,422	641,422
c.	Basic earnings per share (a/b)	3.52	3.76

Subsequent Events

The Bank's Board of Directors has declared cash dividends of P1.12 per share to all stockholders of record on May 27, 2009 and payment date falls on June 23, 2009 after obtaining prior Bangko Sentral ng Pilipinas approval last May 12, 2009.

Additional Disclosures to Item I – Financial Statements

a) Seasonality or Cyclicality of Interim Operations

Seasonal or cyclical events and/or conditions do not affect the interim operations of the Bank.

b) Unusual Items Affecting Interim Financial Statements

There were no unusual items affecting assets, liabilities, equity, net income, or cash flows because of their nature, size or incidence.

c) Changes in Estimates of Amounts Reported

There were no changes in estimates of amounts reported in prior interim periods of the current financial year or in estimates of amounts reported in prior financial years.

d) Issuances, Repurchases and Repayments of Debt and Equity Securities

As discussed on Notes Payable.

e) Material Events Subsequent to the End of the Interim period Not Reflected in the Financial Statements

There were no material events subsequent to the end of the interim period that have not been reflected in the financial statements for the interim period.

f) Changes in the Composition of the Issuer During the Interim Period

There were no changes in the composition of the issuer including business combinations, acquisition or disposal of subsidiaries and long-term investments, restructurings, and discontinuing operations during the interim period.

ANNEX "6"

UNIONBANK OF THE PHILIPPINES
SEC FORM 17-Q
FOR THE PERIOD ENDED MARCH 31, 2009

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

<u>Statement of Income for the Period Ended 31 March 2009 vs. Same Period 2008</u>

The Bank recorded a net income of Php0.57 billion for the first quarter of 2009, 6.19% lower than Php0.60 billion the Bank earned for the same period last year, due primarily on higher interest expense on increased deposit levels.

Interest income amounted to Php3.02 billion for the first three months of 2009, 44.56% higher than Php2.09 billion for the same period last year, as increases in interest income from loans and other receivables, investments and trading securities, and deposits with other banks more than offset the decrease in interest income from interbank loans receivables. Interest income on loans and other receivables grew by 48.55%, to Php1.72 billion this year from Php1.16 billion last year, with the average daily balance (ADB) expansion of the Bank's loan portfolio inclusive of unquoted debt securities classified as loans. Interest income on investments and trading securities likewise increased by 43.04%, to Php0.99 billion this year from Php0.69 billion last year, driven primarily by higher average levels on these investments. Higher ADB levels, coupled with higher yields on deposits with other banks, resulted in 278.68% increase in interest income on these investments, to Php0.31 billion this year from Php0.08 billion last year. On the other hand, interest income on interbank loans receivables declined by 97.11%, to Php0.005 billion this year from Php0.16 billion last year, due to lower average levels and yields on these investments.

Interest expense amounted to Php1.58 billion for the period ending March 31, 2009, 88.71% higher than Php0.83 billion for the same period last year, mainly due to the 127.96% increase in interest expense on deposit liabilities driven by higher average deposit levels and cost. Interest expense on bills payable and other liabilities declined by 70.75%, to Php.05 billion this year from Php0.16 billion last year as a result of lower borrowing cost and decreased average borrowing levels.

As a result of the foregoing, net interest income rose by 15.18%, to Php1.45 billion this year from Php1.25 billion last year.

The Bank continues to build up its provision for impairment losses, setting up an additional Php0.17 billion in the first quarter of the year, 71.00% higher than Php0.10 billion booked in the same period last year, notwithstanding that the Bank has no exposure to financial institutions which were adversely affected by the financial crisis.

Total other income amounted to Php0.86 billion for the quarter-end March 2009, 31.00% higher than Php0.66 billion for the same period last year, driven primarily by the 55.83% increase in miscellaneous income. Miscellaneous income amounted to Php0.54 billion this year from Php0.34 billion last year due primarily to foreign exchange gains on foreign currency denominated assets and higher gains from sale of foreclosed assets. Income from trading increased by 16.48%, to Php0.14 billion this year from Php0.12 billion last year, with the disposal of available-for-sale securities.

Total other expenses grew by 28.55%, to Php1.43 billion for the first three months of 2009, from Php1.11 billion for the same period last year, driven primarily by the 63.02% increase in miscellaneous expenses. Miscellaneous expenses amounted to Php0.56 billion this year from Php0.34 billion last year, as trust fund contribution of the Bank increased with higher pre-need plan sales of First Union Plans. PDIC insurance expense likewise increased due to higher average deposit level. Taxes and licenses amounted to Php0.18 billion this year, 28.06% higher than Php0.14 billion last year due to more gross receipts tax paid on increased interest income on loans. Occupancy cost also increased by 20.38%, to Php0.11 billion this year from Php0.09 billion last year due to annual rent increases and higher utility expenses. Depreciation and amortization was 16.08% higher at Php0.11 billion this year from Php0.09 billion last year, on additional booking of depreciation on acquired assets. Salaries and employee benefits grew by 6.70% this year, to Php0.48 billion from Php0.45 billion last year, as a result of annual salary increases and higher contribution to employees' retirement fund. Provision for income tax increased by 44.26%, to Php0.14 billion this year from Php0.10 billion last year, mainly due to higher final taxes on increased levels of investment securities.

Statement of Condition as of March 31, 2009 vs. December 31, 2008

The Bank's total resources reached Php215.61 billion as of March 31, 2009, 5.74% higher than Php203.90 billion as of end-2008.

Cash and other cash items dropped by 22.73%, to Php3.00 billion as of the first quarter of 2009, from Php3.88 billion end-2008 levels as larger cash inventories are maintained to support clients' higher cash requirements during the holiday season. Due from Other Banks likewise decreased by 62.82%, to Php1.95 billion from Php5.24 billion as a result of the payment of dollar-denominated interbank borrowings and purchase of dollar-denominated investment securities. Interbank loans receivables rose 397.88% to Php19.17 billion from Php3.85 billion, as excess funds were shifted to this asset to maximize earnings through overnight placements.

The Bank purchased additional investments in both available-for-sale investments and held-to maturity investments which grew by 39.35% and 11.38%, respectively.

Loans and receivables dropped 14.24%, to Php77.81 billion as of end of the first quarter of 2009, from Php90.73 billion at end-2008 levels, due to decreased levels of bills purchased, payment of time loans, and shift from reverse repurchase agreements to higher-yielding investments.

Assets held for sale was lower by 45.60%, to Php0.14 billion as of end-March 2009, from Php0.26 billion end-2008 levels, driven by the reclassification of certain assets held for sale to other resources.

Other resources increased by 36.12%, to Php4.98 billion as of the first three months of 2009, from Php3.66 billion end-2008 levels, mainly due to increased levels of returned checks and other cash items and prepaid expenses.

Total liabilities amounted to Php187.84 billion as of end-March 2009, 6.20% higher than Php176.88 billion as of end-2008, mainly due to the increase in the Bank's deposit base, which grew by 4.62% to Php168.88 billion as of the first three months of 2009, from Php161.42 billion end-2008 levels. Demand, savings and time deposits grew by 4.21%, 6.84% and 4.70%, respectively, in line with the bank's thrust to generate more deposits.

Bills and acceptances payable increased by 314.31%, to Php8.93 billion from Php2.16 billion, in view of higher interbank borrowings to fund investment opportunities. On the other hand, other liabilities decreased by 27.24%, to Php8.75 billion from Php12.02 billion, as a result of lower levels of bills purchased, decline in funds held by the Bank for remittance to BIR, and drop in accounts payable.

Net unrealized losses on available-for-sale investments declined by 21.90%, to Php0.64 billion from Php0.82 billion due to favorable market conditions affecting the Bank's mark-to-market of investment securities.

The Bank's annualized return on average equity (ROE) and annualized return on average assets (ROA) as of March 31, 2009 are 8.3% and 1.1%, respectively. The Bank's ratio of non-performing loans to total loans (inclusive of interbank loans receivables) is higher at 7.9% as of end-March 2009 from 5.9% as of the same period last year as a result of writing back, in June 2008, fully reserved NPLs of the former iBank which were previously excluded from the ratio when the assets of that bank were recognized in the books of UnionBank at fair value upon merger of the two banks. NPL cover was higher at 90.7% as of end-March 2009 from 60.4% a year ago. Cost-to-income ratio in the current period was higher at 62.1% compared to 58.2% as of the same period last year, due to operating expense growing at a higher rate than operating income. Annualized earnings per share declined to Php3.52 for the period ended March 2009, from Php3.76 a year ago on lower income. The Bank's capital adequacy ratio was reduced to 10.8% as of balance sheet date from 14.6% a year ago, due to higher risk-weighted assets with the expansion of the Bank's loan and investment securities portfolio, and the application of higher risk weights on ROPs for 2009 in line with the requirements of Basel II.

Key performance indicators of the Bank are as follows:

	Mar. 2009	Dec. 2008
Capital to Risk Assets	10.8%	12.9%
Return on Average Assets	1.1%	1.1%
Return on Average Equity	8.3%	8.0%
Non-Performing Loan Ratio	7.9%	7.9%
Non-Performing Loan Cover	90.7%	85.7%
Cost-Income Ratio	62.1%	57.6%

The manner by which the Bank calculates the above indicators is as follows:

Return on Average Assets:	Net income divided by average total resources for the period indicated
Return on Average Equity:	Net income divided by average total capital funds for the period indicated
Non-Performing Loan Ratio:	Total non-performing loans divided by total loans (inclusive of interbank loans receivables)
Non-Performing Loan Cover:	Total allowance for probable loan losses divided by total non-performing loans
Capital Adequacy Ratio:	Total capital divided by total risk-weighted assets (inclusive of credit, market and operational risk charge)
Cost-Income Ratio:	Total operating expenses divided by the sum of net interest income and other income

As to material event/s and uncertainties, the Bank has nothing to disclose on the following apart from those already disclosed or presented in the accompanying unaudited financial statements:

- Any known trends, demands, commitments, events or uncertainties that will have a material impact on the issuer's liquidity.
- Any events that will trigger direct or contingent financial obligation, including any default or acceleration of an obligation.
- Any material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the company
- Any material commitments for capital expenditures, the general purpose of such commitments and the expected sources of funds for such expenditures.
- Any known trends, events or uncertainties that have had or that are reasonably expected` to have a material favorable or unfavorable impact on net sales/revenues/income from continuing operations.
- Any significant elements of income or loss that did not arise from the issuer's continuing operations.
- Any seasonal aspects that had a material effect on the financial condition or results of operations.

UNIONBANK OF THE PHILIPPINES
Aging of Accounts Receivable
As of March 31, 2009

Type of Accounts Receivable	Total	Current	90 days or less	91 to 180 days	181 days to 1 year	more than 1 year
a) Trade Receivables						
1) Interbank Loans Receivable	19,168,250	19,168,250				
2) Loans	80,225,056	61,945,008	12,945,812	602,841	2,118,842	2,612,553
3) Accrued Interest Receivable	1,966,610	1,662,732	53,524	33,788	43,120	173,446
4) Sales Contract Receivable	1,176,642	1,032,249	117,277	27,116	-	-
5) Installment Contract Receivable	11,901	297	-	-	-	11,604
Less: Allow. For Doubtful Account	5,907,959					
Unearned Discounts	368,496					
SUB-TOTAL	96,272,004	83,808,536	13,116,613	663,745	2,161,962	2,797,603
b) Non-Trade Receivables						
1) Accounts Receivable	1,052,015	772,692	9,821	2,945	11,188	255,369
Less: Allow for Doubtful Account	345,725					
SUB-TOTAL	706,290	772,692	9,821	2,945	11,188	255,369
Net Receivables (a + b)	96,978,294	84,581,228	13,126,434	666,690	2,173,150	3,052,972