# The Mercantile Insurance Co., Inc.

Financial Statements
December 31, 2016 and 2015

and

Independent Auditor's Report

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BOA/PRC Reg. No. 0001,
December 14, 2015, valid until December 31, 2018
SEC Accreditation No. 0012-FR-4 (Group A),
November 10, 2015, valid until November 9, 2018

# INDEPENDENT AUDITOR'S REPORT

The Board of Directors and Stockholders
The Mercantile Insurance Co., Inc.

## Report on the Audit of the Financial Statements

### Opinion

We have audited the financial statements of The Mercantile Insurance Co., Inc. (the Company), which comprise the statements of financial position as at December 31, 2016 and 2015, and the statements of income, the statements of comprehensive income, statements of changes in equity and statements of cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2016 and 2015, and its financial performance and its cash flows for the years then ended in accordance with Philippine Financial Reporting Standards (PFRSs).

### Basis for Opinion

We conducted our audits in accordance with Philippine Standards on Auditing (PSAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the Code of Ethics for Professional Accountants in the Philippines (Code of Ethics) together with the ethical requirements that are relevant to our audit of the financial statements in the Philippines, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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

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

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

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

**Auditor's Responsibilities for the Audit of the Financial Statements**

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

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

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

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

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

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

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

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

**Report on the Supplementary Information Required Under Revenue Regulations 15-2010**

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information required under Revenue Regulations 15-2010 in Note 32 to the financial statements is presented for purposes of filing with the Bureau of Internal Revenue and is not a required part of the basic financial statements. Such information is the responsibility of the management of The Mercantile Insurance Co., Inc. The information has been subjected to the auditing procedures applied in our audit of the basic financial statements. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

SYCIP GORRES VELAYO & CO.

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November 25, 2015, valid until November 24, 2018
PTR No. 5908702, January 3, 2017, Makati City

May 23, 2017

# THE MERCANTILE INSURANCE COMPANY, INC.
## STATEMENTS OF FINANCIAL POSITION

| | December 31 | |
|---|---|---|
| | **2016** | 2015 |
| **ASSETS** | | |
| Cash and cash equivalents (Notes 6 and 27) | **₱260,860,239** | ₱322,565,374 |
| Short-term investments (Notes 7 and 27) | **60,586,358** | – |
| Insurance receivables - net (Notes 8 and 27) | **325,102,976** | 274,124,670 |
| Financial assets (Notes 9 and 27) | | |
| Held-to-maturity investments | **154,751,813** | 119,337,823 |
| Available-for-sale financial assets | **33,617,237** | 26,948,236 |
| Loans and receivables - net | **17,687,074** | 16,458,954 |
| Accrued interest income (Note 27) | **1,231,442** | 539,573 |
| Reinsurance assets (Notes 10 and 15) | **142,564,853** | 145,911,065 |
| Deferred acquisition costs (Note 11) | **78,409,985** | 90,289,492 |
| Property and equipment - net (Note 12) | **187,645,947** | 181,576,572 |
| Investment properties (Note 13) | **149,276,719** | 162,665,235 |
| Net pension asset (Note 24) | **14,115,254** | 15,099,211 |
| Other assets (Note 14) | **11,386,067** | 6,818,270 |
| | **₱1,437,235,964** | ₱1,362,334,475 |

| | | |
|---|---|---|
| **LIABILITIES AND EQUITY** | | |
| **Liabilities** | | |
| Insurance contract liabilities (Notes 15 and 27) | **₱572,877,361** | ₱522,764,259 |
| Insurance payables (Note 16) | **62,991,707** | 40,680,816 |
| Deferred reinsurance commissions (Note 11) | **4,910,590** | 4,602,022 |
| Accounts payable and accrued expenses (Note 18) | **73,564,531** | 69,570,035 |
| Deferred tax liabilities - net (Note 26) | **81,083,618** | 82,364,694 |
| | **795,427,807** | 719,981,826 |
| **Equity** | | |
| Capital stock (Note 19) | **250,000,000** | 250,000,000 |
| Contributed surplus | **92,500** | 92,500 |
| Other comprehensive income (Notes 9, 12 and 24) | **160,956,613** | 149,993,710 |
| Retained earnings | **230,759,044** | 242,266,439 |
| | **641,808,157** | 642,352,649 |
| | **₱1,437,235,964** | ₱1,362,334,475 |

*See accompanying Notes to Financial Statements.*

## THE MERCANTILE INSURANCE COMPANY, INC.
## STATEMENTS OF INCOME

| | Years Ended December 31 | |
|---|---|---|
| | **2016** | 2015 |
| **NET INSURANCE PREMIUMS** (Notes 15 and 20) | | |
| Gross earned premiums on insurance contracts | **₱706,812,263** | ₱495,636,374 |
| Reinsurers' share of premiums earned on insurance contracts | **(185,960,727)** | (128,029,202) |
| | **520,851,536** | 367,607,172 |
| **INVESTMENT AND OTHER INCOME** | | |
| Investment income - net (Note 21) | **12,509,419** | 44,503,852 |
| Commission income (Note 11) | **11,348,661** | 7,451,230 |
| Other income | **556,426** | 271,057 |
| | **24,414,506** | 52,226,139 |
| | **545,266,042** | 419,833,311 |
| **NET INSURANCE BENEFITS AND CLAIMS** (Notes 15 and 22) | | |
| Gross insurance benefits and claims paid | **266,279,191** | 161,208,763 |
| Reinsurers' share of insurance benefits and claims paid | **(48,183,082)** | (4,723,354) |
| Gross change in insurance contract liabilities | **51,676,270** | 65,871,574 |
| Reinsurers' share of change in insurance contract liabilities | **(3,476,334)** | (41,584,447) |
| | **266,296,045** | 180,772,536 |
| **EXPENSES** | | |
| Operating expenses (Note 23) | **87,276,226** | 87,744,726 |
| Commission expense (Note 11) | **204,933,491** | 122,726,031 |
| **TOTAL BENEFITS, CLAIMS AND EXPENSES** | **558,505,762** | 391,243,293 |
| **INCOME (LOSS) BEFORE INCOME TAX** | **(13,239,720)** | 28,590,018 |
| **BENEFIT FROM INCOME TAX** (Note 26) | **(658,807)** | (591,331) |
| **NET INCOME (LOSS)** | **(₱12,580,913)** | ₱29,181,349 |

*See accompanying Notes to Financial Statements*

## THE MERCANTILE INSURANCE COMPANY, INC.
## STATEMENTS OF COMPREHENSIVE INCOME

| | Years Ended December 31 | |
|---|---|---|
| | **2016** | 2015 |
| **NET INCOME (LOSS)** | **(₱12,580,913)** | ₱29,181,349 |
| **OTHER COMPREHENSIVE INCOME** | | |
| *Item that will be reclassified to profit and loss* | | |
| Fair value changes in available-for-sale financial assets (Note 9) | **6,851,782** | (4,220,896) |
| Impairment loss on available-for-sale financial assets (Note 9) | **–** | 194,967 |
| | **6,851,782** | (4,025,929) |
| *Items that will not be reclassified to profit and loss* | | |
| Revaluation increment on property and equipment (Note 12) | **7,188,938** | 5,076,875 |
| Income tax relating to fair value changes in property and equipment (Note 26) | **(2,156,681)** | (1,523,062) |
| | **5,032,257** | 3,553,813 |
| Actuarial gains (losses) on defined benefit plan (Note 24) | **217,688** | (477,751) |
| Income tax relating to actuarial losses (gains) (Note 26) | **(65,306)** | 143,325 |
| | **152,382** | (334,426) |
| | **12,036,421** | (806,542) |
| **TOTAL COMPREHENSIVE INCOME** | **(₱544,492)** | ₱28,347,807 |

*See accompanying Notes to Financial Statements*

# THE MERCANTILE INSURANCE COMPANY, INC.

## STATEMENTS OF CHANGES IN EQUITY

### FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

| | | | Other comprehensive income | | | | |
|---|---|---|---|---|---|---|---|
| | **Capital Stock** (Note 19) | **Contributed Surplus** | **Revaluation Reserve on Available-for-sale Financial Assets** (Note 9) | **Revaluation Reserve on Property and Equipment** (Note 12) | **Actuarial Gain (Loss) on Defined Benefit Plan** (Note 24) | **Retained Earnings** | **Total** |
| As at January 1, 2016 | **₱250,000,000** | **₱92,500** | **₱24,164,754** | **₱112,863,868** | **₱12,965,088** | **₱242,266,439** | **₱642,352,649** |
| Net income for the year | – | – | – | – | – | **(12,580,913)** | **(12,580,913)** |
| Other comprehensive income | – | – | **6,851,782** | **5,032,257** | **152,382** | – | **12,036,421** |
| Total comprehensive income (loss) | – | – | **6,851,782** | **5,032,257** | **152,382** | **(12,580,913)** | **(544,492)** |
| Transfer of depreciation on revaluation increment | – | – | – | **(1,073,518)** | – | **1,073,518** | – |
| **As at December 31, 2016** | **₱250,000,000** | **₱92,500** | **₱31,016,536** | **₱116,822,607** | **₱13,117,470** | **₱230,759,044** | **₱641,808,157** |
| | | | | | | | |
| As at January 1, 2015 | ₱250,000,000 | ₱92,500 | ₱28,190,683 | ₱109,737,311 | ₱13,299,514 | ₱212,657,834 | ₱613,977,842 |
| Net income for the year | – | – | – | – | – | 29,181,349 | 29,181,349 |
| Other comprehensive income (loss) | – | – | (4,025,929) | 3,553,813 | (334,426) | – | (806,542) |
| Total comprehensive income (loss) | – | – | (4,025,929) | 3,553,813 | (334,426) | 29,181,349 | 28,374,807 |
| Transfer of depreciation on revaluation increment | – | – | – | (427,256) | – | 427,256 | – |
| As at December 31, 2015 | ₱250,000,000 | ₱92,500 | ₱24,164,754 | ₱112,863,868 | ₱12,965,088 | ₱242,266,439 | ₱642,352,649 |

*See accompanying Notes to Financial Statements.*

## THE MERCANTILE INSURANCE COMPANY, INC.
## STATEMENTS OF CASH FLOWS

| | Years Ended December 31 | |
|---|---|---|
| | **2016** | 2015 |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Income (loss) before income tax | **(₱13,239,720)** | ₱28,590,018 |
| Adjustments for: | | |
| Fair value loss (gain) on investment properties (Note 21) | **12,184,516** | (25,872,192) |
| Depreciation expense (Notes 12 and 23) | **7,772,111** | 8,725,785 |
| Pension expense (Note 24) | **1,852,430** | 1,909,880 |
| Provision for impairment losses on insurance receivables and loans and receivables (Notes 8, 9 and 23) | **401,182** | 4,913,744 |
| Provision for impairment losses on available-for-sale securities (Notes 9 and 21) | **182,781** | 216,641 |
| Dividend income (Note 21) | **(22,234)** | (8,533) |
| Gain on sale of investment property (Note 13) | **(196,000)** | – |
| Gain on foreign exchange (Note 21) | **(1,523,851)** | (385,766) |
| Interest income (Note 21) | **(9,143,271)** | (6,652,632) |
| Operating income (loss) before changes in working capital | **(1,732,056)** | 11,436,945 |
| Decrease (increase) in: | | |
| Insurance receivables | **(51,379,488)** | (62,897,253) |
| Reinsurance assets | **3,346,212** | (53,111,398) |
| Deferred acquisition costs | **11,879,507** | (28,493,404) |
| Loans and receivables | **(1,311,147)** | 2,071,245 |
| Other assets | **(4,567,797)** | 3,858,609 |
| Increase in: | | |
| Insurance contract liabilities | **50,113,102** | 170,603,224 |
| Accounts payable and accrued expenses | **9,787,398** | 7,890,452 |
| Premiums due to reinsurers | **22,310,891** | 26,677,499 |
| Deferred reinsurance commissions | **308,568** | 2,153,172 |
| Net cash flows from operations | **38,755,190** | 80,189,091 |
| Interest received | **7,800,617** | 7,236,859 |
| Income taxes paid | **(8,637,158)** | (8,051,553) |
| Net cash flows from operating activities | **37,918,649** | 79,374,397 |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Proceeds from maturities and disposals of: | | |
| Held-to-maturity investments (Note 9) | **47,175,935** | 34,753,208 |
| Investment properties (Note 13) | **1,400,000** | – |
| Investment in associate (Note 28) | – | 20,000,000 |
| Acquisitions of: | | |
| Short-term investments (Note 7) | **(60,586,358)** | – |
| Held-to-maturity investments (Note 9) | **(82,506,898)** | (34,812,752) |
| Property and equipment (Note 12) | **(6,652,548)** | (6,815,116) |
| Dividends received | **22,234** | 8,533 |
| Net cash flows from (used in) investing activities | **(101,147,635)** | 13,133,873 |

(Forward)

| | Years Ended December 31 | |
|---|---|---|
| | **2016** | 2015 |
| **EFFECTS OF EXCHANGE RATE CHANGES IN CASH AND CASH EQUIVALENTS** | **₱1,523,851** | ₱385,766 |
| **NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS** | **(61,705,135)** | 92,894,036 |
| **CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR** | **322,565,374** | 229,671,338 |
| **CASH AND CASH EQUIVALENTS AT END OF THE YEAR** (Note 6) | **₱260,860,239** | ₱322,565,374 |

*See accompanying Notes to Financial Statements*

# THE MERCANTILE INSURANCE COMPANY, INC.
# NOTES TO FINANCIAL STATEMENTS

## 1. Corporate Information

The Mercantile Insurance Co., Inc. (the Company) was registered with the Philippine Securities and Exchange Commission (SEC) on October 30, 1962 to engage in the business of nonlife insurance, indemnifying others against loss, damage or liability arising from unknown or contingent events and to act as agent to other insurance or surety companies, any of its branches, including life insurance. It includes lines such as health, accident, fire and allied lines, motor vehicle, casualty, marine cargo, marine hull, comprehensive liability insurance and allied risks, and/or such other insurance coverage allied with an incident to aforementioned lines.

On August 26, 2012, the SEC approved the amended Articles of Incorporation of the Company extending its corporate life for another fifty (50) years starting October 29, 2012.

In 2016, Camerton, Inc. (CI or Parent Company) acquired 69.96% ownership of the Company. With the acquisition, CI obtained control of the Company and became the immediate parent company. Carmetheus Holdings, Inc. (CHI) is the ultimate parent of CI. Both CHI and CI are incorporated in the Philippines.

The registered office address of the Company is Mercantile Insurance Building, General Luna corner Beaterio Streets, Intramuros, Manila.

The accompanying financial statements were approved and authorized for issue by the Board of Directors (BOD) on May 23, 2017.

## 2. Basis of Preparation and Statement of Compliance

The financial statements of the Company have been prepared on a historical cost basis, except for available-for-sale (AFS) financial assets and investment properties which have been measured at fair value and property and equipment which has been measured at revalued amounts. The financial statements are presented in Philippine Peso (₱), which is also the Company's functional currency. All values are rounded to the nearest peso unit except when otherwise indicated.

Statement of Compliance

The accompanying financial statements of the Company have been prepared in compliance with Philippine Financial Reporting Standards (PFRS). PFRS include Philippine Financial Reporting Standards, Philippine Accounting Standards and Interpretations issued by the Philippine Interpretations Committee (PIC).

## 3. Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year, except that the Company has adopted the following new accounting pronouncements starting January 1, 2016. Adoption of these pronouncements did not have any significant impact on the Company's financial position or performance unless otherwise indicated. The Company has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

*Effective in 2016*

- Amendments to PFRS 10, PFRS 12 and Philippine Accounting Standards (PAS) 28, *Investment Entities: Applying the Consolidation Exception*
- Amendments to PFRS 11, *Accounting for Acquisitions of Interests in Joint Operations*
- PFRS 14, *Regulatory Deferral Accounts*
- Amendments to PAS 1, *Disclosure Initiative*
- Amendments to PAS 16 and PAS 38, *Clarification of Acceptable Methods of Depreciation and Amortization*
- Amendments to PAS 16 and PAS 41, *Agriculture: Bearer Plants*
- Amendments to PAS 27, *Equity Method in Separate Financial Statements*
- Annual Improvements to PFRSs 2012 - 2014 Cycle
  - Amendment to PFRS 5, *Changes in Methods of Disposal*
  - Amendment to PFRS 7, *Servicing Contracts*
  - Amendment to PFRS 7, *Applicability of the Amendments to PFRS 7 to Condensed Interim Financial Statements*
  - Amendment to PAS 19, *Discount Rate: Regional Market Issue*
  - Amendment to PAS 34, *Disclosure of Information 'Elsewhere in the Interim Financial Report'*

*Future changes in Accounting Policies*
*Effective beginning on or after January 1, 2017*

- Amendment to PFRS 12, *Clarification of the Scope of the Standard* (Part of *Annual Improvements to PFRSs* 2014 - 2016 Cycle)
- Amendments to PAS 7, *Statement of Cash Flows*, *Disclosure Initiative*
- Amendments to PAS 12, *Income Taxes*, *Recognition of Deferred Tax Assets for Unrealized Losses*
- Circular Letter 2016-67, *Valuation Standards for Non-life Insurance Policy Reserves*

  The circular prescribes the new valuation methodology for the non-life insurance companies. Non-life insurance companies will be changing the basis of valuation of their non-life insurance reserves. In addition to the unearned premium reserves, the concept of unexpired risk reserves is also included in the calculation of the premium liability. The incurred but not reported (IBNR) reserves will now be computed using actuarial projection techniques such as but not limited to the chain ladder method, expected loss ratio method and Bornheutter-Ferguson method.

  A margin for adverse deviation is estimated based on standard projection techniques or combination of such techniques, such as but not limited to the Mack Method, Bootstrapping Method, Stochastic Chain Ladder Method to bring the actuarial estimate of the Policy Liabilities at the 75$^{th}$ percentile level of sufficiency. Discount rates to be used shall be current risk-free rates. The rates shall exactly match the duration of the policy and the currency of the cash flows and shall be prescribed by the Insurance Commission.

  The Company will adopt the new valuation standard on the required effective date.

*Effective beginning on or after January 1, 2018*

- Amendments to PFRS 2, *Share-based Payment*, *Classification and Measurement of Share-based Payment Transactions*
- Amendments to PAS 28, *Measuring an Associate or Joint Venture at Fair Value* (Part of *Annual Improvements to PFRSs* 2014 - 2016 Cycle)

- Amendments to PAS 40, *Investment Property*, *Transfers of Investment Property*
- Philippine Interpretation IFRIC-22, *Foreign Currency Transactions and Advance Consideration*
- PFRS 15, *Revenue from Contracts with Customers*
- Amendments to PFRS 4, *Insurance Contracts*, *Applying PFRS 9, Financial Instruments, with PFRS 4*

  The amendments address concerns arising from implementing PFRS 9, the new financial instruments standard before implementing the forthcoming insurance contracts standard. They allow entities to choose between the overlay approach and the deferral approach to deal with the transitional challenges. The overlay approach gives all entities that issue insurance contracts the option to recognize in other comprehensive income, rather than profit or loss, the volatility that could arise when PFRS 9 is applied before the new insurance contracts standard is issued. On the other hand, the deferral approach gives entities whose activities are predominantly connected with insurance an optional temporary exemption from applying PFRS 9 until the application of the forthcoming insurance contracts standard on January 1, 2021.

  The overlay approach and the deferral approach will only be available to an entity if it has not previously applied PFRS 9.

  The Company is assessing which approach it will use and the potential impact of the chosen approach in its financial statements.

- PFRS 9, *Financial Instruments*
  PFRS 9 reflects all phases of the financial instruments project and replaces PAS 39, *Financial Instruments: Recognition and Measurement*, and all previous versions of PFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. PFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early application permitted. Retrospective application is required, but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

  The adoption of PFRS 9 will have an effect on the classification and measurement of the Company's financial assets and impairment methodology for financial assets, but will have no impact on the classification and measurement of the Company's financial liabilities. The adoption will also have an effect on the Company's application of hedge accounting and on the amount of its credit losses. The Company is currently assessing the impact of adopting this standard.

*Effective beginning on or after January 1, 2019*

- PFRS 16, *Leases*
  Under the new standard, lessees will no longer classify their leases as either operating or finance leases in accordance with PAS 17, *Leases*. Rather, lessees will apply the single-asset model. Under this model, lessees will recognize the assets and related liabilities for most leases on their balance sheets, and subsequently, will depreciate the lease assets and recognize interest on the lease liabilities in their profit or loss. Leases with a term of 12 months or less or for which the underlying asset is of low value are exempted from these requirements.

The accounting by lessors is substantially unchanged as the new standard carries forward the principles of lessor accounting under PAS 17. Lessors, however, will be required to disclose more information in their financial statements, particularly on the risk exposure to residual value.

Entities may early adopt PFRS 16 but only if they have also adopted PFRS 15. When adopting PFRS 16, an entity is permitted to use either a full retrospective or a modified retrospective approach, with options to use certain transition reliefs.

The Company is currently assessing the impact of adopting PFRS 16.

*Deferred effectivity*

- Amendments to PFRS 10 and PAS 28, *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*

## 4. Summary of Significant Accounting Policies

Use of Estimates, Assumptions and Judgments
The preparation of the financial statements necessitates the use of estimates, assumptions and judgments. These estimates and assumptions affect the reported amounts of assets and liabilities and contingent liabilities at the end of the reporting period as well as affecting the reported income and expenses for the year. Although the estimates are based on management's best knowledge and judgment of current facts as at the end of the reporting period, the actual outcome may differ from these estimates, possibly significantly. For further information on critical accounting estimates and judgments, refer to Note 5.

Product Classification
Insurance contracts are defined as those contracts under which the Company (the insurer) accepts significant insurance risk from another party (the policyholders) by agreeing to compensate the policyholders if a specified uncertain future event (the insured event) adversely affects the policyholder. As a general guideline, the Company defines significant insurance risk, by comparing benefits paid with benefits payable if the insured event did not occur. Insurance contracts can also transfer financial risk. Financial risk is the risk of a possible future change in one or more of a specified interest rate, security price, commodity price, foreign exchange rate, index of price or rates, a credit rating or credit index or other variable.

Investment contracts mainly transfer financial risk but can also transfer insignificant insurance risk.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period, unless all rights and obligations are extinguished or has expired. Investment contracts can however be reclassified as insurance contracts after inception if the insurance risk becomes significant.

Fair Value Measurement
The Company measures financial instrument and non-financial assets such as property and equipment, at fair value at each reporting period. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 27.

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

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

The principal or the most advantageous market must be accessible to by the Company.
The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

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

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

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

- *Level 1* - Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- *Level 2* - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- *Level 3* - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

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

<u>Cash and Cash Equivalents</u>
Cash includes cash on hand, cash in banks and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three (3) months or less from dates of placement and that are subject to an insignificant risk of changes in value.

<u>Short-term Investments</u>
These are placements in time deposits and other money market instruments with original maturities of more than three months but less than one year and which are not restricted as to use.

Insurance Receivables
Insurance receivables are recognized on policy inception dates and measured on initial recognition at the fair value of the consideration receivable for the period of coverage. Subsequent to initial recognition, insurance receivables are measured at amortized cost. The carrying value of insurance receivables is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in profit or loss.

Insurance receivables are derecognized under the derecognition criteria of financial assets.

Financial Instruments
*Date of recognition*
Financial instruments are recognized in the statement of financial position when the Company becomes a party to the contractual provisions of the instrument. Purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace are recognized on the trade date.

*Initial recognition of financial instruments*
Financial instruments are initially recognized at fair value of the consideration given (in case of an asset) or received (in case of a liability). Except for financial instruments at fair value through profit or loss (FVPL), the initial measurement of financial assets includes transaction costs. The Company classifies its financial assets in the following categories: held-to-maturity (HTM) investments, AFS financial assets, FVPL investments and loans and receivables. The Company classifies its financial liabilities into financial liabilities at FVPL and other financial liabilities. The classification depends on the purpose for which the investments were acquired and whether they are quoted in an active market. Management determines the classification of its investments at initial recognition and, where allowed and appropriate, re-evaluates such designation at every end of the reporting period.

As of December 31, 2016 and 2015, the Company's financial instruments are in the nature of AFS financial assets, HTM financial assets, loans and receivables and other financial liabilities.

*Day 1 difference*
Where the transaction price in a non-active market is different from the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the Company recognizes the difference between the transaction price and fair value (a 'Day 1' difference) in profit or loss unless it qualifies for recognition as some other type of asset. In cases where an observable data is used, the difference between the transaction price and model value is only recognized in profit or loss when the inputs become observable or when the instrument is derecognized. For each transaction, the Company determines the appropriate method of recognizing the 'Day 1' difference amount.

*Loans and receivables*
Loans and receivables are financial assets with fixed or determinable payments and fixed maturities that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as financial assets held for trading, designated as AFS or FVPL. This accounting policy relates to the statement of financial position captions: (a) "Cash and cash equivalents," (b) "Short-term investments," (c) "Insurance receivables" and (d) "Loans and receivables."

After initial measurement, the loans and receivables are subsequently measured at amortized cost using the effective interest rate method, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortization is included in the "Interest income" in profit or loss. The losses arising from impairment of such loans and receivables are recognized in profit or loss.

*AFS financial assets*
AFS financial assets are those which are designated as such or do not qualify to be classified as designated at FVPL, HTM or loans and receivables. They are purchased and held indefinitely, and may be sold in response to liquidity requirements or changes in market conditions.

After initial measurement, AFS financial assets are subsequently measured at fair value. The effective yield component of AFS debt securities, as well as the impact of restatement on foreign currency-denominated AFS debt securities, is reported in earnings. Interest earned on holding AFS debt investments are reported as interest income using the effective interest rate. Dividends earned on holding AFS equity investments are recognized in profit or loss when the right to receive the payment has been established. The unrealized gains and losses arising from the fair valuation of AFS investments are reported as "Revaluation reserve on available-for-sale financial assets" in equity. The losses arising from impairment of such investments are recognized in profit or loss. When the security is disposed of, the cumulative gain or loss previously recognized in equity is recognized as realized gains or losses in profit or loss. When the Company holds more than one investment in the same security, the cost is determined using the weighted average method.

When the fair value of AFS financial assets cannot be measured reliably because of lack of reliable estimates of future cash flows and discount rates necessary to calculate the fair value of unquoted equity instruments, these investments are carried at cost.

*Other financial liabilities*
Issued financial instruments or their components, which are not designated at FVPL are classified as other financial liabilities, where the substance of the contractual arrangement results in the Company having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

After initial measurement, other financial liabilities are subsequently measured at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any discount or premium on the issue and fees that are an integral part of the effective interest rate. Any effects of restatement of foreign currency-denominated liabilities are recognized in the statement of comprehensive income.

This accounting policy applies primarily to the Company's provision for claims reported by policyholders and IBNR (included in insurance contract liabilities), insurance payables and accounts payable and accrued expenses that meet the above definition (other than liabilities covered by other accounting standards, such as retirement benefit obligation and income tax payable).

Offsetting
Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

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

*Financial assets carried at amortized cost*
For financial assets carried at amortized cost (e.g., loans and receivables), the Company first assesses whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Company determines that no objective evidence of impairment exists for individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be recognized, are not included in a collective assessment for impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows. The carrying amount of the asset is reduced through the use of an allowance account and the amount of loss is charged against profit or loss. If, in a subsequent period, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed. Any subsequent reversal of an impairment loss is recognized in profit or loss, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. Time value is generally not considered when the effect of discounting is not material. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate, adjusted for the original credit risk premium. 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 credit risk characteristics such as past-due status and term.

*AFS investments carried at fair value*
In case of equity investments classified as AFS, impairment indicators would include a significant or prolonged decline in the fair value of the investments below its cost. When a decline in the fair value of an AFS financial asset has been recognized in other comprehensive income, and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment even though the financial asset has not been derecognized. Impairment losses on equity investments are not reversed through profit or loss. Increases in fair value after impairment are recognized directly in other comprehensive income.

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

*AFS investments carried at cost*
If there is an objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such unquoted equity instrument 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 discounted at the current market rate of return for a similar financial asset.

Derecognition of Financial Assets and Liabilities
*Financial asset*
A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized where:

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

Where the Company has transferred its right to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Company's continuing involvement in the asset.

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

Reinsurance
The Company cedes insurance risk in the normal course of business. Reinsurance assets represent balances due from reinsurance companies. Recoverable amounts are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contract.

Reinsurance assets are reviewed for impairment at each end of the reporting period or more frequently when an indication of impairment arises during the reporting year. Impairment occurs when objective evidence exists that the Company may not recover outstanding amounts under the terms of the contract and when the impact on the amounts that the Company will receive from the reinsurer can be measured reliably. The impairment loss is recorded in profit or loss. Ceded reinsurance arrangements do not relieve the Company from its obligations to policyholders.

The Company also assumes reinsurance risk in the normal course of business for insurance contracts. Premiums and claims on assumed reinsurance are recognized in profit or loss as income and expenses in the same manner as they would be if the reinsurance were considered direct business, taking into account the product classification of the reinsured business. Reinsurance liabilities represent balances due to reinsurance companies. Amounts payable are estimated in a manner consistent with the associated reinsurance contract.

Premiums and claims are presented on a gross basis for both ceded and assumed reinsurance.

Reinsurance assets or liabilities are derecognized when the contractual rights are extinguished or expired or when the contract is transferred to another party.

Deferred Acquisition Costs (DAC)
Commissions and other acquisition costs incurred during the financial period that vary with and are related to securing new insurance contracts and or renewing existing insurance contracts, but which relates to subsequent financial periods, are deferred to the extent that they are recoverable out of future revenue margins. All other acquisition costs are recognized as expense when incurred.

Subsequent to initial recognition, these costs are amortized on a straight-line basis using the 24th method over the life of the contract except for marine cargo where commissions for the last two months of the year are recognized as expense the following year. Amortization is charged against profit or loss. The unamortized acquisition costs are shown as “Deferred acquisition costs” in the assets section of the statement of financial position.

An impairment review is performed at each end of the reporting period or more frequently when an indication of impairment arises. The carrying value is written down to the recoverable amount. The impairment loss is charged to profit or loss. DAC is also considered in the liability adequacy test for each end of the reporting period.

Property and Equipment
Land and buildings and building improvements are stated at appraised value determined by an independent firm of appraisers, less accumulated depreciation. The net appraisal increment resulting from the revaluation is credited to revaluation increment on property and equipment included under "Other Comprehensive Income" in the Statements of Financial Position. Accumulated depreciation on the revalued property and equipment is eliminated against the gross carrying value of the asset and the net amount restated to the revalued amount of the asset.

A revaluation surplus is recorded in OCI and credited to the revaluation reserve in equity. However, to the extent that it reverses a revaluation deficit of the same asset previously recognized in profit or loss, the increase is recognized in profit or loss. A revaluation deficit is recognized in profit or loss, except to the extent that it offsets an existing surplus on the same asset recognized in the asset revaluation reserve.

Property and equipment, other than land and buildings and building improvements, are carried at cost less accumulated depreciation, and any impairment in value.

The initial cost of property and equipment comprises its purchase price, including any directly attributable costs of bringing the asset to its working condition and location for its intended use. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance expenses are charged to profit or loss during the financial period in which they are incurred.

Depreciation of property and equipment commence once the property and equipment are available for use and is computed using the straight-line method over the estimated useful lives (EUL) of the assets regardless of the utilization.

The EUL of the Company's property and equipment follows:

| | Years |
|---|---|
| Building and building improvements | 40 |
| Office furniture, fixtures and equipment | 5 |
| Transportation equipment | 4 |

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

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

Investment Properties
Property held for long term rental yields or for capital appreciation or for both, is classified as investment property. These properties are initially measured at cost, which includes transaction cost, but excludes day to day servicing cost. Replacement cost is capitalized if it is probable that future economic benefits associated with the item will flow to the entity and the cost of the item can be reliably measured. Subsequent to initial recognition, investment properties are stated at fair

values determined by an independent firm of appraisers. Gains or losses arising from changes in the fair values of investment properties are included in the profit or loss for the period in which they arise, including the corresponding tax effect.

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

Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner occupation or commencement of development with a view to sale.

Investment property is derecognized when it has been disposed of or when permanently withdrawn from use and no future benefit is expected from its disposal. Any gain or loss on the retirement or disposal of investment properties are recognized in profit or loss in the year of derecognition.

Impairment of Non-financial Assets

The Company assesses at each end of the reporting period whether there is an indication that an asset may be impaired. If any such indication exists or when annual impairment testing for an asset is required, the Company makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses of continuing operations are recognized in profit or loss in those expense categories consistent with the function of the impaired asset.

For assets excluding goodwill, an assessment is made at each end of the reporting period as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If any such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized. If such is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation and amortization, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the statement of income unless the asset is carried at revalued amount, in which case, the reversal is treated as a revaluation increase. After such reversal, the depreciation and amortization charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining estimated useful life.

Insurance Contract Liabilities

Insurance contract liabilities are recognized when contracts are entered into and premiums are charged.

*Provision for Unearned Premiums*
The proportion of written premiums, gross of commissions payable to intermediaries, attributable to subsequent periods or to risks that have not yet expired is deferred as provision for unearned premiums as part of "Insurance contract liabilities" and presented in the liabilities section of the statement of financial position. Premiums from short-duration insurance contracts are recognized as revenue over the period of the contracts using the 24th method except for the marine cargo where premiums for the last two months are considered earned the following year. The portion of the premiums written that relate to the unexpired periods of the policies at end of the reporting period are accounted for as Provision for unearned premiums as part of "Insurance contract liabilities" and presented in the liabilities section of the statement of financial position. The change in the provision for unearned premiums is taken to profit or loss in order that revenue is recognized over the period of risk. Further provisions are made to cover claims under unexpired insurance contracts which may exceed the unearned premiums and the premiums due in respect of these contracts.

*Claims Provision and Incurred But Not Reported (IBNR) Losses*
These liabilities are based on the estimated ultimate cost of all claims incurred but not settled at the end of the reporting period together with related claims handling costs and reduction for the expected value of salvage and other recoveries. Delays can be experienced in the notification and settlement of certain types of claims, therefore the ultimate cost of which cannot be known with certainty at the end of the reporting period. The liability is not discounted for the time value of money and includes provision for IBNR losses. The liability is derecognized when the contract is discharged, cancelled or has expired.

*Liability Adequacy Test*
At each end of the reporting period, liability adequacy tests are performed to ensure the adequacy of insurance contract liabilities, net of the related DAC assets. In performing the test, current best estimates of future cash flows, claims handling and policy administration expenses are used. Changes in expected claims that have occurred, but which have not been settled, are reflected by adjusting the liability for claims and future benefits. Any inadequacy is immediately charged to the statement of comprehensive income by establishing an unexpired risk provision for losses arising from the liability adequacy tests. The provision for unearned premiums is increased to the extent that the future claims and expenses in respect of current insurance contracts exceed future premiums plus the current provision for unearned premiums.

Pension Cost
The net defined benefit liability or asset is the aggregate of the present value of the defined benefit obligation at the end of the reporting period reduced by the fair value of plan assets (if any), adjusted for any effect of limiting a net defined benefit asset to the asset ceiling. The asset ceiling is the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.
The cost of providing benefits under the defined benefit plan is actuarially determined using the projected unit credit method.

Defined benefit cost comprises the following:
- Service cost
- Net interest on the net defined benefit liability or asset
- Remeasurement of net defined benefit liability or asset

Service cost includes current service cost, past service cost and gain or loss on non-routine settlements and is recognized as expense in profit or loss. Past service cost is recognized when plan amendment or curtailment occurs. These amounts are calculated periodically by independent qualified actuaries.

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

Remeasurements comprising actuarial gains and losses, return on plan assets and any change in the effect of the asset ceiling (excluding net interest on defined benefit liability) are recognized immediately in other comprehensive income in the period in which they arise. Remeasurements are not reclassified to profit or loss in subsequent periods.

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

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

Equity

*Capital stock*

Capital stock is recognized as issued when the stock is paid for or subscribed under a binding subscription agreement and is measured at par value. When the shares are sold at a premium, the difference between the proceeds and the par value is credited to additional paid-in capital. Share issuance costs incurred as necessary part of completing an equity transaction are accounted for as part of that transaction and are treated as a deduction from additional paid-in capital from previous share issuance. If the additional paid-in capital account is not sufficient, the excess is deducted from retained earnings.

*Contributed surplus*

Contributed Surplus represents contributions of the stockholders to cover any unexpected deficiency in the Margin of Solvency (MOS) and Risk-Based Capital (RBC) as required under the Insurance Code and can be withdrawn upon the approval of the IC.

*Additional paid-in capital*

Additional paid-in capital includes any premiums received in excess of par value on the issuance of capital stock. Any transaction costs associated with the issuance of shares are deducted from additional paid-in capital.

*Retained earnings (Deficit)*
Retained earnings (deficit) include all the accumulated earnings (losses) of the Company, less any amount of dividends declared.

Revenue
Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

*Premiums revenue*
Gross insurance written premiums comprise the total premiums receivable for the whole period of cover provided by contracts entered into during the accounting period and are recognized on the date on which the policy incepts. Premiums include any adjustments arising in the accounting period for premiums receivable in respect of business written in prior periods.

Premiums from short-duration insurance contracts are recognized as revenue over the period of the contracts using the 24th method except for marine cargo where premiums for the last two months are considered earned the following year. The portion of the premiums written that relate to the unexpired periods of the policies at end of the reporting period are accounted for as Provision for unearned premiums and shown as part of “Insurance contract liabilities” presented in the liabilities section of the statements of financial position. The related reinsurance premiums ceded that pertain to the unexpired periods at end of the reporting period are accounted for as Deferred reinsurance premiums and shown as part of “Reinsurance assets” in the statements of financial position. The net changes in these accounts between each end of reporting period are recognized in profit or loss.

*Reinsurance commissions*
Commissions earned from short-duration insurance contracts are recognized as revenue over the period of the contracts using the 24th method except for marine cargo where the deferred reinsurance commissions for the last two months of the year are considered earned the following year. The portion of the commissions that relate to the unexpired periods of the policies at end of the reporting period are accounted for as “Deferred reinsurance commissions” and presented in the liabilities section of the statement of financial position.

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

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the original effective interest rate applied to the new carrying amount.

*Commission expense and other underwriting expenses*
Commissions are recognized when the insurance contracts are entered and the corresponding premiums are recognized.

*Dividend income*
Dividend income is recognized when the shareholders' right to receive the payment is established.

*Benefits and claims*
Benefits and claims consist of benefits and claims paid to policyholders, which include changes in the valuation of Insurance contract liabilities, except for changes in the provision for unearned premiums which are recorded in insurance revenue. It further includes internal and external claims handling costs that are directly related to the processing and settlement of claims. Amounts receivable in respect of salvage and subrogation are also considered. General insurance claims are recorded on the basis of notifications received.

*Operating expense*
Operating expenses, except for lease expenses, are recognized as expense as they are incurred.

*Interest expense*
Interest expense is charged against operations and is calculated using the effective interest method.

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

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

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

Leases where the lessor does not transfer substantially all the risks and benefits of ownership of the assets are classified as operating leases. Lease payments on operating leases are recognized on a straight-line basis over the lease term.

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

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

Income Tax

*Current tax*

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that have been enacted or substantively enacted at the end of the reporting period.

*Deferred income tax*

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

Deferred income tax liabilities are recognized for all taxable temporary differences, including asset revaluations. Deferred income tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits from the excess of minimum corporate income tax (MCIT) over the regular income tax, and unused net operating loss carryover (NOLCO), to the extent that it is probable that sufficient taxable profit will be available against which the deductible temporary differences and carry forward of unused tax credits from MCIT and unused NOLCO can be utilized. Deferred income tax, however, is not recognized on temporary differences that arise from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting income nor taxable income or loss.

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

Deferred tax assets and liabilities are measured at the tax rates that are applicable to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the end of the reporting period. Movements in the deferred income tax assets and liabilities arising from changes in tax rates are charged against or credited to income for the period.

Current tax and deferred tax relating to items recognized as other comprehensive income is also recognized in the statement of comprehensive income.

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

Value-added tax (VAT)
Revenue, expenses and assets are recognized net of the amount of sales tax except:

- where the tax incurred on a purchase of assets or services is not recoverable from the tax authority, in which case the tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and,
- receivables and payables that are stated with the amount of tax included.

Events after the Reporting Period
Any post year-end events that provide additional information about the Company's position at the end of the reporting period (adjusting event) are reflected in the financial statements. Post year-end events that are not adjusting events, if any, are disclosed in the financial statements when material.

## 5. Significant Accounting Judgments and Estimates

The preparation of the Company's financial statements in accordance with PFRS required management to make judgments, estimates and assumptions that affect the amounts reported in the financial statements and related notes. Future events may occur which will cause the assumptions used in arriving at the estimates to change. The effects of any change in estimates are reflected in the financial statements as they become reasonably determinable.

Judgments, estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual outcome can differ from these estimates.

Judgments
In the process of applying the Company's accounting policies, management has made the following judgments, apart from those involving estimates and assumptions, which have the most significant effect on the amounts recognized in the financial statements.

*Distinction between investment properties and owner occupied properties*
The Company determines whether a property qualifies as investment property or owner-occupied property. In making its judgment, the Company considers whether the property generated cash flows largely independently of the other assets held by an entity or for capital appreciation or to earn rentals. Owner-occupied properties generate cash flows that are attributable not only to the property but also to the other assets used in the supply of services or for administrative purposes.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the supply of services or for administrative purposes. If these portions cannot be sold or leased out separately under a finance lease as of the reporting date, the property is accounted for as investment property only if an insignificant portion is held for use in the supply of services or for administrative purposes. Judgment is applied in determining whether ancilliary services are so significant that a property does not qualify as investment property. The Company considers each property separately in making its judgment.

The disclosures on the Company's property and equipment and investment properties are presented in Notes 12 and 13, respectively.

*Operating leases - Company as a lessee*
The Company has entered into property leases. Substantially, all the risk and benefits incidental to ownership of the leased item are not transferred to the Company. The future minimum rentals under non-cancellable operating lease amounted to ₱1.85 million and ₱1.71 million in 2016 and 2015, respectively (see Note 30).

*Operating leases - Company as a lessor*
The Company has entered into property leases on its investment property portfolio. The Company has determined that it retains all the significant risks and rewards of ownership of these properties which are leased out on operating leases. The future minimum rentals under non-cancellable operating leases amounted to ₱6.15 million and ₱4.52 million in 2016 and 2015, respectively (see Note 30).

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

The Company carries certain financial assets at fair value, which requires extensive use of accounting estimates and judgments. Fair value determinations for financial assets and liabilities are based generally on listed or quoted market prices. If prices are not readily determinable or if liquidating the positions is reasonably expected to affect market prices, fair value is based on either internal valuation models or management's estimate of amounts that could be realized under current market conditions, assuming an orderly liquidation over a reasonable period of time. While significant components of fair value were determined using verifiable objective evidence (i.e., foreign exchange rates, interest rates, volatility rates), the amount of changes in fair value of these financial assets and liabilities would affect profit or loss and OCI.

The carrying value of AFS financial assets is ₱33.62 million and ₱26.95 million as of December 31, 2016 and 2015, respectively (see Notes 9 and 27).

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

*HTM investments*
The Company classifies non-derivative financial assets with fixed or determinable payments and fixed maturity as HTM investment. This classification requires significant judgment. In making this judgment, the Company evaluates its intention and ability to hold such investments to maturity. If the Company fails to keep these investments to maturity other than in certain specific circumstances - for example, sales that are so close to maturity - it will be required to reclassify the entire portfolio as AFS financial assets. The investment would therefore be measured at fair value and not as amortized cost. HTM investments amounted to ₱154.75 million and ₱119.34 million as of December 31, 2016 and 2015, respectively (see Notes 9 and 27).

Estimates

*Claims liability arising from insurance contracts*

For nonlife insurance contracts, estimates have to be made both for the expected ultimate cost of claims reported at the reporting date and for the expected ultimate cost of the claims IBNR at the reporting date. It can take a significant period of time before the ultimate claim costs can be established with certainty and for some type of policies, IBNR claims form the majority of the statement of financial position claims provision. The primary technique adopted by management in estimating the cost of notified and IBNR claims, is that of using past claims settlement trends to predict future claims settlement trends. At each reporting date, prior year claims estimates are assessed for adequacy and changes made are charged to provision. Nonlife insurance claims provisions are not discounted for the time value of money.

The main assumption underlying the estimation of the claims provision is that a Company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios. Historical claims development is mainly analyzed by accident years, but can also be further analyzed by geographical area, as well as by significant business lines and claim types. Large claims are usually addressed separately, either by being reserved at the face value of loss adjuster estimates or separately projected in order to reflect their future development. In most cases, no explicit assumptions are made regarding future rates of claims inflation or loss ratios. Instead, the assumptions used are those implicit in the historic claims development data on which the projections are based. Additional qualitative judgment is used to assess the extent to which past trends may not apply in the future, (i.e., for example to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy conditions and claims handling procedures) in order to arrive at the estimated ultimate cost of claims that present the likely outcome from the range of possible outcomes, taking account of all the uncertainties involved.

The carrying value of total provision for outstanding claims, IBNR and reserve for unearned premiums amounted to ₱572.87 million and ₱522.76 million as of December 31, 2016 and 2015, respectively (see Note 15).

*Impairment of financial assets*

The Company treats AFS equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment. The Company treats 'significant' generally as 20% or more and 'prolonged' greater than six (6) months. In addition, the Company evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for unquoted equities. Impairment may be appropriate also when there is evidence of deterioration in the financial health of the investee, the industry and sector performance, changes in technology and operational and financing cash flows.

The Company assesses at the end of each reporting period whether there is any objective evidence that its HTM investments are impaired. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the holder of the asset about the following loss events:

(a) significant financial difficulty of the issuer or obligor;
(b) a breach of contract, such as a default or delinquency in interest or principal payments;

(c) the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
(d) it becoming probable that the borrower will enter bankruptcy or other financial reorganization;
(e) the disappearance of an active market for that financial asset because of financial difficulties; or
(f) 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, including:

    (i) adverse changes in the payment status of borrowers in the group (e.g. an increased number of delayed payments or an increased number of credit card borrowers who have reached their credit limit and are paying the minimum monthly amount); or
    (ii) national or local economic conditions that correlate with defaults on the assets in the group (e.g. an increase in the unemployment rate in the geographical area of the borrowers, a decrease in property prices for mortgages in the relevant area, a decrease in oil prices for loan assets to oil producers, or adverse changes in industry conditions that affect the borrowers in the group).

The Company reviews its loans and receivables at each reporting date to assess whether an allowance for impairment should be recorded in profit or loss. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of allowance required. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance. The level of this allowance is evaluated by management on the basis of factors that affect the collectability of the accounts. These factors include, but are not limited to, age of balances, financial status of counterparties, payment behavior and known market factors. The Company reviews the age and status of receivables and identifies accounts that are to be provided with allowance on a regular basis.

In addition to specific allowance against individually significant loans and receivables, the Company also makes a collective impairment allowance against exposures which, although not specifically identified as requiring a specific allowance, have a greater risk of default than when originally granted. This collective allowance is based on any deterioration in the internal rating of the loan or investment since it was granted or acquired. These internal ratings take into consideration factors such as any deterioration in country risk, industry and technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows.

The amount and timing of recorded expenses for any period would differ if the Company made different judgments or utilized different estimates. An increase in allowance for impairment losses would increase recorded expenses and decrease net income. Allowance for impairment losses amounted to ₱1.27 as of December 31, 2016 and 2015. Insurance receivables, net of allowance for impairment losses, amounted to ₱325.10 million and ₱274.12 million as of December 31, 2016 and 2015, respectively (see Note 8).

The carrying values of financial assets follow (see Note 9):

| | **2016** | 2015 |
|---|---|---|
| HTM investments | **₱154,751,813** | ₱119,337,823 |
| AFS financial assets | **33,617,237** | 26,948,235 |
| Loans and receivables | **17,687,074** | 16,458,954 |

*EUL of property and equipment and investment properties*
The Company reviews annually the EUL of property and equipment and investment properties based on the period over which the assets are expected to be available for use. It is possible that future results of operations could be materially affected by changes in these estimates. A reduction in the EUL of property and equipment and investment properties would increase recorded depreciation expense and decrease the related asset accounts.

The related balances follow:

| | **2016** | 2015 |
|---|---|---|
| Property and equipment - net (Note 12) | **₱187,645,947** | ₱181,576,572 |
| Investment properties (Note 13) | **149,276,719** | 162,665,235 |

*Impairment of nonfinancial assets*
The Company assesses impairment on assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The factors that the Company considers important which could trigger an impairment review include the following:
- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the manner of use of the acquired assets or the strategy for overall business; and
- significant negative industry or economic trends.

The Company recognizes an impairment loss whenever the carrying amount of an asset exceeds its recoverable amount. The recoverable amount is computed using the value in use approach. Recoverable amounts are estimated for individual assets or, if it is not possible, for the cash-generating unit to which the asset belongs.

As of December 31, 2016 and 2015, the Company has determined that there are no indications that its property and equipment, and investment properties may be impaired.

The related balances follow:

| | **2016** | 2015 |
|---|---|---|
| Property and equipment - net (Note 12) | **₱187,645,947** | ₱181,576,572 |
| Investment properties (Note 13) | **149,276,719** | 162,665,235 |

*Pension and other employee benefits*
The determination of the obligation and cost of pension is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions, which include, among others, discount rate and salary increase rate, are described in Note 24. While the Company believes that the assumptions are reasonable and appropriate, significant differences in the actual experience or significant changes in the assumptions may materially affect the pension obligation. Please refer to Note 24 for the related balances.

*Recognition of deferred tax assets*
Deferred tax assets are recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which these can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized. These assets are periodically reviewed for realization. Periodic reviews cover the nature and amount of deferred income and expense items, expected timing when assets will be

used or liabilities will be required to be reported, reliability of historical profitability of businesses expected to provide future earnings and tax planning strategies which can be utilized to increase the likelihood that tax assets will be realized.

As of December 31, 2016 and 2015, the Company recognized deferred tax asset amounting to ₱21.96 million and ₱25.75 million, respectively, since based on the Company's estimate, the Company will generate sufficient taxable income in the future when these temporary differences will be utilized.

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

## 6. Cash and Cash Equivalents

This account consists of:

| | **2016** | 2015 |
|---|---|---|
| Cash on hand | **₱71,700** | ₱71,700 |
| Cash in banks | **192,055,640** | 268,135,155 |
| Cash equivalents | **68,732,899** | 54,358,519 |
| | **₱260,860,239** | ₱322,565,374 |

Cash in banks earns interest at the prevailing bank deposit rates which ranged from 0.25% to 1.25% in 2016 and 2015. Cash equivalents are short-term deposits made for varying periods of up to three (3) months depending on the immediate cash requirements of the Company and earn interest at the respective short-term deposit rates that ranged from 0.08% to 1.75% and 0.80% to 1.60% in 2016 and 2015, respectively.

Interest income earned on cash and cash equivalents amounted to ₱2.87 million and ₱2.00 million in 2016 and 2015, respectively (see Note 21).

## 7. Short-term Investments

Short-term investments consist of money market placements made for varying periods of more than three (3) months to twelve (12) months and earn interest ranging from 0.88% to 2.25% in 2016. Interest income on these short-term investments amounted to ₱0.28 million 2016 (see Note 21).

## 8. Insurance Receivables

This account consists of:

| | 2016 | 2015 |
|---|---|---|
| Premiums receivable | **₱169,454,481** | ₱116,864,357 |
| Reinsurance recoverable on paid losses | **86,069,973** | 91,309,664 |
| Taxes receivable | **49,141,800** | 29,220,291 |
| Due from reinsurers | **23,315,942** | 37,999,398 |
| | **327,982,196** | 275,393,710 |
| Less allowance for impairment losses | **2,879,220** | 1,269,040 |
| | **₱325,102,976** | ₱274,124,670 |

Premiums receivable represent unpaid premiums on written insurance policies which are collectible from policyholders within the Company's usual grace period of ninety (90) days.

Reinsurance recoverable on paid losses pertains to amounts recoverable from the reinsurers in respect of claims already paid by the Company.

Taxes receivable includes receivables from policyholders for documentary stamp tax (DST), value-added tax (VAT), fire service tax, local government tax and premium tax.

Due from reinsurers pertains to premiums collectible from ceding companies with respect to assumed policies.

The allowance for impairment losses on insurance receivables as at December 31, 2016 and 2015 follows:

| | Premiums receivable | Due from reinsurers | Reinsurance recoverable on paid losses | Total |
|---|---|---|---|---|
| At January 1, 2015 | ₱– | ₱8,276,368 | ₱12,421,570 | ₱20,697,938 |
| Provision for the year (Note 23) | – | 1,107,037 | 3,806,707 | 4,913,744 |
| Write-off | – | (8,368,149) | (15,974,493) | (24,342,642) |
| At December 31, 2015 | ₱– | ₱1,015,256 | ₱253,784 | ₱1,269,040 |
| Reclassification of allowance for impairment losses (Note 9) | 1,610,180 | – | – | 1,610,180 |
| **At December 31, 2016** | **₱1,610,180** | **₱1,015,256** | **₱253,784** | **₱2,879,220** |

## 9. Financial Assets

The Company's financial assets are summarized by measurement categories as follows:

| | 2016 | 2015 |
|---|---|---|
| HTM investments | **₱154,751,813** | ₱119,337,823 |
| AFS financial assets | **33,617,237** | 26,948,236 |
| Loans and receivables - net | **17,687,074** | 16,458,954 |
| | **₱206,056,124** | ₱162,745,013 |

The assets included in each of the categories above are discussed below:

a) *HTM investments*

The Company's HTM investments consist of investments in Philippine peso-denominated government securities that earned annual interest ranging from 1.63% to 9.13% in 2016 and 1.63% to 9.13% in 2015. Interest income earned from HTM investments amounted to ₱5.06 million and ₱3.64 million in 2016 and 2015, respectively (see Note 21). As of December 31, 2016 and 2015, the fair value of these investments amounted to ₱195.32 million and ₱119.86 million, respectively (see Note 27).

The Company deposited government securities in the IC amounting to ₱137.50 million and ₱91.86 million as of December 31, 2016 and 2015, respectively, in accordance with the provision of the Insurance Code (the Code) as security for the benefit of policyholders and creditors of the Company.

b) *AFS financial assets*

| | 2016 | 2015 |
|---|---|---|
| **Traded securities** | | |
| Listed common shares | **₱25,446,937** | ₱19,737,936 |
| Club shares | **8,150,000** | 5,650,000 |
| | **33,596,937** | 25,387,936 |
| **Nontraded securities** | | |
| Unlisted common shares | **20,300** | 1,560,300 |
| **Total AFS financial assets recognized in the statements of financial position** | **₱33,617,237** | ₱26,948,236 |

The acquisition costs of the AFS financial assets follow:

| | 2016 | 2015 |
|---|---|---|
| Listed common shares | **₱1,102,901** | ₱1,145,682 |
| Club shares | **1,477,500** | 1,617,500 |
| Unlisted common shares | **20,300** | 20,300 |
| | **₱2,600,701** | ₱2,783,482 |

The rollforward analysis of reserve for fluctuation on AFS financial assets follows:

| | 2016 | 2015 |
|---|---|---|
| At January 1 | **₱24,164,754** | ₱28,190,683 |
| OCI | | |
| Changes in fair value of AFS financial assets | **6,851,782** | (4,220,896) |
| Transferred to profit of loss | | |
| Provision for impairment losses | – | 194,967 |
| At December 31 | **₱31,016,536** | ₱24,164,754 |

Dividend income earned from the Company's AFS financial assets amounted to ₱22,234 and ₱8,533 in 2016 and 2015, respectively (see Note 21).

The carrying values of financial assets have been determined as follows:

| | HTM | AFS |
|---|---|---|
| At January 1, 2015 | ₱119,305,036 | ₱31,190,806 |
| Additions | 34,812,752 | – |
| Maturities and disposals | (34,753,208) | – |
| Amortization of premium - net | (26,757) | – |
| Fair value change during the year | – | (4,025,929) |
| Impairment loss (Note 23) | – | (216,641) |
| At December 31, 2015 | 119,337,823 | 26,948,236 |
| Additions | 82,506,898 | – |
| Maturities and disposals | (47,175,935) | – |
| Amortization of premium - net | 83,027 | – |
| Fair value gains added on other comprehensive income | – | 6,851,782 |
| Impairment loss (Note 23) | – | (182,781) |
| At December 31, 2016 | ₱154,751,813 | ₱33,617,237 |

c) *Loans and receivables*

| | **2016** | 2015 |
|---|---|---|
| Bond loss recoverable | **₱9,248,542** | ₱9,248,542 |
| Advances | **4,557,602** | 5,643,823 |
| Notes receivable | **2,955,507** | 3,046,861 |
| Accrued rent receivable | **1,326,605** | 111,514 |
| Receivable from tenants | – | 18,394 |
| | **18,088,256** | 18,069,134 |
| Less allowance for impairment losses | **401,182** | 1,610,180 |
| | **₱17,687,074** | ₱16,458,954 |

Bond loss recoverable pertains to the amount paid by the Company under an issued callable surety bond. It is a contract wherein the Company (the surety) guaranteed the performance of certain obligations of a second party (the principal) to a third party (the obligee). It is the amount paid by the Company to the obligee recoverable from the principal.

Advances represent notarial fee charges and unpaid service charges billed on bond enrollments.

Notes receivable represent secured notes from employees with interest rates ranging from 6% to 12% per annum payable up to 4 years. Interest income amounted to ₱0.28 million and ₱0.23 million in 2016 and 2015, respectively (see Note 21).

Accrued rent receivable pertains to amount owed by the tenants to the Company for rental of the Company's premises.

Receivable from tenants pertains to reimbursable expenses incurred for utilities paid by the Company on their behalf.

The rollforward analysis of allowance for impairment losses on loans and receivables follows:

| | **2016** | 2015 |
|---|---|---|
| At January 1 | **₱1,610,180** | ₱1,610,180 |
| Provision for the year (Note 23) | **401,182** | – |
| Reclassification of allowance for impairment losses (Note 9) | **(1,610,180)** | – |
| At December 31 | **₱401,182** | ₱1,610,180 |

10. **Reinsurance Assets**

This account consists of (Note 15):

| | **2016** | 2015 |
|---|---|---|
| Reinsurance recoverable on unpaid losses | **₱124,206,166** | ₱120,729,832 |
| Deferred reinsurance premiums | **18,358,687** | 25,181,233 |
| | **₱142,564,853** | ₱145,911,065 |

The reinsurance recoverable on unpaid losses pertains to amounts recoverable from the reinsurers in respect of claims not yet paid by the Company.

The deferred reinsurance premiums refer to the unrealized portion of the premiums ceded out.

11. **Deferred Acquisition Costs and Deferred Reinsurance Commissions**

The rollforward analyses of these accounts follow:

*Deferred acquisition costs*

| | **2016** | 2015 |
|---|---|---|
| At January 1 | **₱90,289,492** | ₱61,796,088 |
| Costs deferred during the year | **193,053,984** | 151,219,435 |
| Amortization during the year recognized under "Commission expense" | **(204,933,491)** | (122,726,031) |
| At December 31 | **₱78,409,985** | ₱90,289,492 |

*Deferred reinsurance commissions*

| | **2016** | 2015 |
|---|---|---|
| At January 1 | **₱4,602,022** | ₱2,448,850 |
| Income deferred during the year | **11,657,229** | 9,604,402 |
| Amortization during the year recognized under "Commission income" | **(11,348,661)** | (7,451,230) |
| At December 31 | **₱4,910,590** | ₱4,602,022 |

## 12. **Property and Equipment** - net

The movements in this account for property and equipment carried at cost follow:

| | **2016** | | |
|---|---|---|---|
| | **Office furniture, fixtures and equipment** | **Transportation equipment** | **Total** |
| **Cost** | | | |
| At January 1 | **₱38,473,562** | **₱20,069,579** | **₱58,543,141** |
| Additions | **4,914,548** | **1,738,000** | **6,652,548** |
| At December 31 | **43,388,110** | **21,807,579** | **65,195,689** |
| **Accumulated depreciation** | | | |
| At January 1 | **28,223,123** | **15,631,475** | **43,854,598** |
| Depreciation (Note 23) | **3,897,500** | **2,197,925** | **6,095,425** |
| At December 31 | **32,120,623** | **17,829,400** | **49,950,023** |
| **Net book value** | **₱11,267,487** | **₱3,978,179** | **₱15,245,666** |

| | 2015 | | |
|---|---|---|---|
| | Office furniture, fixtures and equipment | Transportation equipment | Total |
| **Cost** | | | |
| At January 1 | ₱33,407,946 | ₱18,320,079 | ₱51,728,025 |
| Additions | 5,065,616 | 1,749,500 | 6,815,116 |
| At December 31 | 38,473,562 | 20,069,579 | 58,543,141 |
| **Accumulated depreciation** | | | |
| At January 1 | 24,608,236 | 13,821,120 | 38,429,356 |
| Depreciation (Note 23) | 3,614,887 | 1,810,355 | 5,425,242 |
| At December 31 | 28,223,123 | 15,631,475 | 43,854,598 |
| **Net book value** | ₱10,250,439 | ₱4,438,104 | ₱14,688,543 |

The movements in property and equipment carried at revalued amounts follow:

| | **2016** | | |
|---|---|---|---|
| | **Land** | **Building and Building Improvements** | **Total** |
| **Revalued amount** | | | |
| At January 1 | **₱135,031,001** | **₱31,857,028** | **₱166,888,029** |
| Increase (decrease) in fair value | **5,745,999** | **(233,747)** | **5,512,252** |
| At December 31 | **140,777,000** | **31,623,281** | **172,400,281** |
| **Accumulated depreciation** | | | |
| At January 1 | – | – | – |
| Depreciation (Note 23) | – | **1,676,686** | **1,676,686** |
| Decrease (increase) in fair value | – | **(1,676,686)** | **(1,676,686)** |
| At December 31 | – | – | – |
| **Net book value** | **₱140,777,000** | **₱31,623,281** | **₱172,400,281** |

| | 2015 | | |
|---|---|---|---|
| | Land | Building and Building Improvements | Total |
| **Revalued amount** | | | |
| At January 1 | ₱132,158,001 | ₱32,953,696 | ₱165,111,697 |
| Additions | – | – | – |
| Increase (decrease) in fair value | 2,873,000 | (1,096,668) | 1,776,332 |
| At December 31 | 135,031,001 | 31,857,028 | 166,888,029 |
| **Accumulated depreciation** | | | |
| At January 1 | – | – | – |
| Depreciation (Note 23) | – | 3,300,543 | 3,300,543 |
| Decrease (increase) in fair value | – | (3,300,543) | (3,300,543) |
| 44,At December 31 | – | – | – |
| **Net book value** | ₱135,031,001 | ₱31,857,028 | ₱166,888,029 |

If land and building and building improvements were carried at cost less accumulated depreciation, the amounts would be as follows:

| | **2016** | | |
|---|---|---|---|
| | **Land** | **Building and Building Improvements** | **Total** |
| Cost | **₱1,181,816** | **₱8,973,255** | **₱10,155,071** |
| Accumulated depreciation | **–** | **(4,644,229)** | **(4,644,229)** |
| **Net book value** | **₱1,181,816** | **₱4,329,026** | **₱5,510,842** |

| | 2015 | | |
|---|---|---|---|
| | Land | Building and Building Improvements | Total |
| Cost | ₱1,181,816 | ₱8,973,255 | ₱10,155,071 |
| Accumulated depreciation | – | (4,501,139) | (4,501,139) |
| **Net book value** | ₱1,181,816 | ₱4,472,116 | ₱5,653,932 |

The Company's building and building improvements are carried at revalued amount as of December 31, 2016 and 2015. The Company uses the elimination method in revaluing its building and building improvements.

On September 7, 2016 and January 25. 2017, the Company obtained appraisal of its investment property from Aviso Valuation & Advisory Corporation (formerly CCGA Realty Corporation), an independent firm of appraisers, for the revalued amount of its property and equipment as of December 31, 2016 and 2015, respectively. The revalued amount of property and equipment was arrived at using the Fair Value Approach. In this approach, the value of the land and condominium units is based on sales and listings of comparable property registered within the vicinity. The technique of this approach requires the establishment of comparable property by reducing reasonable comparative sales and listings to a common denominator. This is done by adjusting the differences between the subject property and those actual sales and listings regarded as comparable. The properties used as basis of comparison are situated within the immediate vicinity of the subject property. Estimated price per square meter based on this approach is the unobservable input. Significant increases (decreases) in estimated price per square meter would result in a significantly higher (lower) fair value of the properties.

Depreciation expense charged to operations amounted to ₱7.77 million and ₱8.73 million in 2016 and 2015, respectively (see Note 23). The amount of revaluation increment absorbed through depreciation, net of tax, transferred to retained earnings amounted to ₱1.07 million and ₱0.43 million in 2016 and 2015, respectively.

The cost of fully depreciated property and equipment still in use as of December 31, 2016 and 2015 amounted to ₱22.41 million and ₱25.50 million, respectively.

## 13. **Investment Properties**

The rollforward analysis of this account follows:

| | **2016** | | |
|---|---|---|---|
| | **Land** | **Building and building improvements** | **Total** |
| At January 1, 2015 | **₱62,014,000** | **₱100,651,235** | **₱162,665,235** |
| Disposal | **(1,204,000)** | **–** | **(1,204,000)** |
| Fair value loss (Note 21) | **(11,284,000)** | **(900,516)** | **(12,184,516)** |
| **At December 31, 2015** | **₱49,526,000** | **₱99,750,719** | **₱149,276,719** |

| | 2015 | | |
|---|---|---|---|
| | Land | Building and building improvements | Total |
| At January 1, 2015 | ₱– | ₱103,947,304 | ₱103,947,304 |
| Transfers from asset held-for-sale (Note 8) | 32,845,739 | – | 32,845,739 |
| Fair value gain (loss) (Note 21) | 29,168,261 | (3,296,069) | 25,872,192 |
| At December 31, 2015 | ₱62,014,000 | ₱100,651,235 | ₱162,665,235 |

In 2016, the Company sold a piece of land with book value of ₱1.20 million which resulted in a gain of ₱0.20 million which is included “Other Income” in the Company’s statement of income.

As of December 31, 2016 and 2015, the aggregate fair value of the Company’s investment property amounted to ₱149.28 million and ₱162.67 million, respectively. The fair value represents the amount at which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm’s length transaction at the date of valuation.

On September 7, 2016 and January 25. 2017, the Company obtained appraisal of its investment from Aviso Valuation & Advisory Corporation (formerly CCGA Realty Corporation), an independent firm of appraisers, for the fair value of its investment property as of December 31, 2016 and 2015, respectively. The value of investment properties was arrived at using the Fair Value Approach. In this approach, the value of the land and condominium units is based on sales and listings of comparable property registered within the vicinity. The technique of this approach requires the establishment of comparable property by reducing reasonable comparative sales and listings to a common denominator. This is done by adjusting the differences between the subject property and those actual sales and listings regarded as comparable. The properties used as basis of comparison are situated within the immediate vicinity of the subject property. Estimated price per square meter based on this approach is the unobservable input. Significant increases (decreases) in estimated price per square meter would result in a significantly higher (lower) fair value of the properties.

No depreciation was recognized in 2016 and 2015 since the Company uses fair value method in measuring investment properties. Rental income earned from investment properties amounted ₱14.19 million and ₱11.80 million in 2016 and 2015, respectively, which is included in investment income (see Note 21).

## 14. **Other Assets**

This account consists of:

| | **2016** | 2015 |
|---|---|---|
| Prepaid expenses | **₱4,409,964** | ₱3,057,906 |
| Input VAT | **3,469,323** | 680,998 |
| Creditable withholding taxes | **3,454,807** | 2,757,093 |
| Security deposit | **51,973** | – |
| Deferred input VAT | **–** | 322,273 |
| | **₱11,386,067** | ₱6,818,270 |

Prepaid expenses are composed of advance payment of certificate of cover (COC) of VAT and DST. This account is a wallet load paid to CIS bayad center where the COC for VAT and DST is being deducted.

Input VAT pertains to VAT on domestic purchases or payments for services. This will be applied against future output VAT.

Creditable withholding taxes are unapplied taxes withheld by the Company's customers on income payments and are creditable against income tax due. As of December 31, 2016, the Company's creditable withholding taxes are considered recoverable and can be applied against future income tax.

Security deposit pertains to rental deposit.

## 15. **Insurance Contract Liabilities**

Insurance contract liabilities may be analyzed as follows:

| | **2016** | | | 2015 | | |
|---|---|---|---|---|---|---|
| | **Insurance Contract liabilities** | **Reinsurers' share of liabilities (Note 10)** | **Net** | Insurance Contract liabilities | Reinsurers' share of liabilities (Note 10) | Net |
| Provision for claims reported and loss adjustment expenses | **₱239,401,579** | **₱124,189,311** | **₱115,212,268** | ₱215,500,391 | ₱120,729,832 | ₱94,770,559 |
| Provision for IBNR claims | **30,409,842** | **16,855** | **30,392,987** | 2,634,760 | – | 2,634,760 |
| Total claims reported and IBNR claims | **269,811,421** | **124,206,166** | **145,605,255** | 218,135,151 | 120,729,832 | 97,405,319 |
| Provision for unearned premiums | **303,065,940** | **18,358,687** | **284,707,253** | 304,629,108 | 25,181,233 | 279,447,875 |
| Insurance contract liabilities | **₱572,877,361** | **₱142,564,853** | **₱430,312,508** | ₱522,764,259 | ₱145,911,065 | ₱376,853,194 |

Provisions for claims reported by policyholders and IBNR may be analyzed as follows:

| | **2016** | | | 2015 | | |
|---|---|---|---|---|---|---|
| | **Insurance Contract liabilities** | **Reinsurers' share of liabilities (Note 10)** | **Net** | Insurance Contract liabilities | Reinsurers' share of liabilities (Note 10) | Net |
| At January 1 | **₱218,135,151** | **₱120,729,832** | **₱97,405,319** | ₱152,263,577 | ₱79,145,385 | ₱72,767,961 |
| Claims incurred during the year | **290,180,379** | **51,642,561** | **238,537,818** | 226,730,106 | 46,307,801 | 180,772,536 |
| Claims paid during the year net of recoveries (Note 22) | **(266,279,191)** | **(48,183,082)** | **(218,096,109)** | (161,208,763) | (4,723,354) | (156,485,409) |
| Increase in IBNR | **27,775,082** | **16,855** | **27,758,227** | 350,231 | – | 350,231 |
| **At December 31** | **₱269,811,421** | **₱124,206,166** | **₱145,605,255** | ₱218,135,151 | ₱120,729,832 | ₱97,405,319 |

Provision for unearned premiums may be analyzed as follows:

| | **2016** | | | 2015 | | |
|---|---|---|---|---|---|---|
| | **Insurance contract liabilities** | **Reinsurers' share of liabilities** (Note 10) | **Net** | Insurance contract liabilities | Reinsurers' share of liabilities (Note 10) | Net |
| At January 1 | **₱304,629,108** | **₱25,181,233** | **₱279,447,875** | ₱199,897,458 | ₱13,654,282 | ₱186,243,176 |
| New policies written during the year (Note 20) | **705,249,095** | **179,138,181** | **526,110,914** | 600,368,024 | 139,556,153 | 460,811,871 |
| Premiums earned during the year (Note 20) | **(706,812,263)** | **(185,960,727)** | **(520,851,536)** | (495,636,374) | (128,029,202) | (367,607,172) |
| **At December 31** | **₱303,065,940** | **₱18,358,687** | **₱284,707,253** | ₱304,629,108 | ₱25,181,233 | ₱279,447,875 |

## 16. Insurance Payables

The rollforward analysis of insurance payables follows:

| | **2016** | 2015 |
|---|---|---|
| At January 1 | **₱40,680,816** | ₱14,003,317 |
| Arising during the year (Note 20) | **179,138,181** | 139,556,153 |
| Paid during the year | **(156,827,290)** | (112,878,654) |
| At December 31 | **₱62,991,707** | ₱40,680,816 |

## 17. Insurance Contract Liabilities and Reinsurance Assets - Terms, Assumptions and Sensitivities

*Terms and Conditions*
The major classes of general insurance written by the Company include motor, property, casualty, marine and engineering. Risks under these policies usually cover a twelve (12) month duration.

For general insurance contracts, claims provisions (comprising provisions for claims reported by policyholders and IBNR claims) are established to cover the ultimate cost of settling the liabilities in respect of claims that have occurred and are estimated based on known facts at the reporting date.

The provisions are refined as part of a regular ongoing process as claims experience develops, certain claims are settled and further claims are reported. Outstanding claims provisions are not discounted for the time value of money.

The measurement process primarily includes projections of future claims through use of historical experience statistics. In certain cases, where there is a lack of reliable historical data on which to estimate claims development, relevant benchmarks of similar business are used in developing claims estimates. Claims provisions are separately analyzed by geographical area and class of business. In addition, claims are usually assessed by loss adjusters. The claims projection assumptions are generally intended to provide a best estimate of the most likely or expected outcome.

*Assumptions*
The principal assumption underlying the estimates is the Company's past claims development experience. This includes assumptions in respect of average claim costs and claim numbers for each accident year. Judgment is used to assess the extent to which external factors such as judicial decisions and government legislation affect the estimates.

Other key assumptions include variation in interest and delays in settlement.

*Sensitivities*
The general insurance claims provision is sensitive to the above key assumptions. The sensitivity of certain variables such as legislative change and uncertainty in the estimation process, is not possible to quantify. Furthermore, because of delays that arise between occurrence of a claim and its subsequent notification and eventual settlement, the outstanding claim provisions are not known with certainty at the reporting date.

Consequently, the ultimate liabilities will vary as a result of subsequent developments. Differences resulting from reassessments of the ultimate liabilities are recognized in subsequent financial statements.

The analysis below is performed for a reasonably possible movement in key assumptions with all other assumptions held constant, on the statements of comprehensive income.

| | **2016** | | | |
|---|---|---|---|---|
| | **Change in Assumptions** | **Impact on gross insurance contract liabilities** | **Impact on net insurance contract liabilities** | **Impact on income before income tax** |
| **Average claim costs** | **-26.71%decrease** | **(₱73,474,082)** | **(₱59,534,383)** | **(₱59,534,383)** |
| **Average number of claims** | **48.52%increase** | **133,437,656** | **108,121,507** | **108,121,507** |

| | 2015 | | | |
|---|---|---|---|---|
| | Change in Assumptions | Impact on gross insurance contract liabilities | Impact on net insurance contract liabilities | Impact on income before income tax |
| Average claim costs | 56.11% increase | ₱152,050,414 | ₱87,173,025 | ₱87,173,025 |
| Average number of claims | 16.53% increase | 44,777,927 | 25,671,928 | 25,671,928 |

The average claim costs and number of claims were based on the Company's claims development experience for the past five years.

*Claims Development Table*
Reproduced below is an exhibit that shows the development of claims over a period of time on a gross and net reinsurance basis:

At Gross

| Accident year | 2012 and prior years | 2013 | 2014 | 2015 | 2016 | TOTAL |
|---|---|---|---|---|---|---|
| **Estimate of ultimate claim costs:** | | | | | | |
| At the end of accident year | ₱383,249,982 | ₱164,629,183 | ₱144,478,145 | ₱270,966,548 | ₱275,032,056 | ₱275,032,056 |
| One year later | 322,339,717 | 115,743,928 | 50,559,644 | 182,424,861 | – | 182,424,861 |
| Two years later | 223,687,605 | 48,514,094 | 21,468,046 | – | – | 21,468,046 |
| Three years later | 135,468,587 | 18,707,592 | – | – | – | 18,707,592 |
| Four years later | 16,551,951 | – | – | – | – | 16,551,951 |
| Current estimate of cumulative claims | 16,551,951 | 18,707,592 | 21,468,046 | 182,424,861 | 275,032,056 | 514,184,505 |
| Cumulative payments to date | 2,944,153 | 3,996,487 | 16,112,206 | 97,585,766 | 123,734,472 | 244,373,084 |
| **Total gross insurance liability in the statement of financial position** | ₱13,607,797 | ₱14,711,105 | ₱ 5,355,840 | ₱84,839,094 | ₱151,297,584 | ₱269,811,421 |

At Net

| | 2012 and prior years | 2013 | 2014 | 2015 | 2016 | Total |
|---|---|---|---|---|---|---|
| **Estimate of ultimate claim costs:** | | | | | | |
| At the end of accident year | ₱329,970,377 | ₱116,999,324 | ₱231,409,209 | ₱155,349,618 | ₱222,852,239 | ₱222,852,239 |
| One year later | 239,770,842 | 55,329,123 | 48,449,568 | 82,610,995 | | 82,610,995 |
| Two years later | 161,658,287 | 32,582,966 | 10,913,257 | | | 10,913,257 |
| Three years later | 120,121,942 | 13,564,399 | | | | 13,564,399 |
| Four years later | 16,309,438 | | | | | 16,309,438 |
| Current estimate of cumulative claims | 16,309,438 | 13,564,399 | 10,913,257 | 82,610,995 | 222,852,239 | 346,250,328 |
| Cumulative payments to date | 2,895,528 | 3,730,772 | 5,696,052 | 71,959,241 | 116,363,480 | 200,645,073 |
| **Total gross insurance liability in the statement of financial position** | ₱13,413,910 | ₱9,833,628 | ₱5,217,206 | ₱10,651,753 | ₱106,488,759 | ₱145,605,255 |

## 18. Accounts Payable and Accrued Expenses

This account consists of:

| | **2016** | 2015 |
|---|---|---|
| Payable to government agencies | **₱46,047,093** | ₱46,416,213 |
| Commissions payable | **14,501,654** | 11,037,482 |
| Customers' deposits | **9,597,938** | 8,643,645 |
| Rental deposits | **3,417,846** | 3,472,695 |
| | **₱73,564,531** | ₱69,570,035 |

Payable to government agencies consists of output VAT, withholding tax, unpaid previous years' taxes, premium tax and local government tax, such as fire service tax.

Commissions payable consist of amounts payable to agents which are non-interest-bearing and calculated based on the average commission rates approve by management.

Customers' deposits pertain to cash received as collateral for bond policies.

Rental deposits represent two months deposit on leased premises. These rent deposits are refundable at the end of the lease contract or applied against the remaining lease term depending on the agreement of the contracting parties. Lease contracts are renewable every year.

## 19. Equity

The Company's capital stock consists of:

| | 2016 | | 2015 | |
|---|---|---|---|---|
| | **Shares** | **Amount** | Shares | Amount |
| Authorized shares at ₱100 par value | **5,000,000** | **₱500,000,000** | 5,000,000 | ₱500,000,000 |
| Issued and outstanding | | | | |
| at beginning and end of year | **2,500,000** | **250,000,000** | 2,500,000 | 250,000,000 |
| | **2,500,000** | **₱250,000,000** | 2,500,000 | ₱250,000,000 |

## 20. Net Insurance Premiums

This account consists of:

| | 2016 | 2015 |
|---|---|---|
| Gross earned premiums on insurance contracts: | | |
| Direct insurance | **₱667,812,933** | ₱557,144,111 |
| Assumed reinsurance | **37,436,162** | 43,223,913 |
| Total insurance contract premiums revenue | **705,249,095** | 600,368,024 |
| Gross change in provision for unearned premiums | **1,563,168** | (104,731,650) |
| **Total gross earned premiums on insurance** (Note 15) | **706,812,263** | 495,636,374 |
| Reinsurer's share of gross earned premiums on insurance contracts | **179,138,181** | 139,556,153 |
| Reinsurer's share of gross change in deferred reinsurance premiums | **6,822,546** | (11,526,951) |
| **Total reinsurers' share of gross earned premiums on insurance** (Note 15) | **185,960,727** | 128,029,202 |
| Net insurance premiums | **₱520,851,536** | ₱367,607,172 |

## 21. Investment Income - net

This account consists of:

| | 2016 | 2015 |
|---|---|---|
| Interest income on: | | |
| HTM investments (Note 9) | **₱5,061,928** | ₱3,641,803 |
| Cash and cash equivalents (Note 6) | **2,865,947** | 1,996,904 |
| Short-term investments (Note 7) | **281,751** | – |
| Net pension asset (Note 24) | **650,785** | 786,133 |
| Loans and receivables (Note 9) | **282,860** | 227,792 |
| Rental income (Notes 13 and 30) | **14,187,360** | 11,801,370 |
| Gain on foreign exchange | **1,523,851** | 385,766 |
| Dividend income (Note 9) | **22,234** | 8,533 |
| Impairment loss on available-for-sale securities (Notes 9 and 23) | **(182,781)** | (216,641) |
| Fair value gain (loss) on investment properties - net (Note 13) | **(12,184,516)** | 25,872,192 |
| | **₱12,509,419** | ₱44,503,852 |

## 22. Net Insurance Benefits and Claims

Gross insurance contract benefits and claims paid:

| | **2016** | 2015 |
|---|---|---|
| Insurance contract benefits and claims paid (Note 15): | | |
| Direct insurance | **₱258,469,877** | ₱154,385,661 |
| Assumed reinsurance | **7,809,314** | 6,823,102 |
| Total insurance contract benefits and claims paid | **₱266,279,191** | ₱161,208,763 |

Gross change in insurance contract liabilities:

| | **2016** | 2015 |
|---|---|---|
| Increase in insurance contract liabilities (Note 15): | | |
| Direct insurance | **₱20,441,709** | ₱37,584,447 |
| Assumed reinsurance | **3,459,479** | 27,936,896 |
| Provision for IBNR | **27,775,082** | 350,231 |
| Total change in insurance contract liabilities | **₱51,676,270** | ₱65,871,574 |

## 23. Operating Expenses

This account consists of:

| | **2016** | 2015 |
|---|---|---|
| Personnel expenses (Note 25) | **₱36,326,653** | ₱33,973,876 |
| Depreciation (Note 12) | **7,772,111** | 8,725,785 |
| Transportation expenses | **5,319,608** | 4,196,847 |
| Taxes and licenses | **4,912,357** | 3,607,985 |
| Postage, telephone and telegraph | **4,390,623** | 4,069,620 |
| Contracted services | **4,030,371** | 4,202,206 |
| Professional fees | **3,577,683** | 1,410,404 |
| Stationery, printing and supplies | **2,812,158** | 3,715,263 |
| Entertainment, amusement and recreation | **2,607,277** | 1,761,743 |
| Light and water | **2,328,346** | 2,259,650 |
| Agency, seminar and training | **2,127,547** | 1,832,655 |
| Rent expense (Note 30) | **1,846,605** | 1,711,685 |
| Advertising and promotion | **1,298,047** | 1,442,229 |
| Repairs and maintenance | **815,258** | 2,586,183 |
| Association dues and fees | **726,634** | 699,683 |
| Provision for impairment losses (Notes 8 and 9) | **401,182** | 6,129,235 |
| Insurance | **181,140** | 138,207 |
| Miscellaneous | **5,802,626** | 5,281,470 |
| | **₱87,276,226** | ₱87,744,726 |

Miscellaneous expenses include sports and social affairs, donation and contribution, impairment loss on AFS, bank charges and books and subscription.

## 24. **Retirement Costs**

The Company has a funded, tax qualified, noncontributory, defined benefit pension plan covering substantially all of its regular employees. The benefits are based on years of service and compensation on the last year of employment.

The Company's annual contribution to the plan consists principally of payments which covers the current service cost for the year and the required funding relative to the guaranteed minimum benefits as applicable. The fund is administered by the Trustee under the supervision of the Board of Trustees (BOT) of the plan which delegates the implementation of the investment policy to the Trustee. This fund is subject to the investment objectives and guidelines established by the Trustee and rules and regulations issued by Bangko Sentral ng Pilipinas covering assets under trust and fiduciary agreements. The Trustee is responsible for the investment strategy of the plan.

The latest actuarial valuation date of the Company's retirement plan is December 31, 2016.

The fund is administered by a trustee bank under the supervision of the Board of Trustees of the plan. The Board of Trustees is responsible for investment of the assets. It defines the investment strategy as often as necessary, at least annually, especially in the case of significant market developments or changes to the structure of the plan participants. When defining the investment strategy, it takes account of the plans' objectives, benefit obligations and risk capacity. The investment strategy is defined in the form of a long-term target structure (investment policy). The Board of Trustees delegates the implementation of the investment policy in accordance with the investment strategy as well as various principles and objectives to an Investment Committee, which also consists of members of the Board of Trustees, a Director and a Controller. The Controller oversees the entire investment process.

Republic Act 7641, *The New Retirement Law*, requires a provision for retirement pay to qualified private sector employees in the absence of any retirement plan in the entity. The law does not require minimum funding of the plan.

The following tables summarize the components of the "Current service" and "Net interest income" recognized in profit or loss under "Operating expenses" and "Investment income", respectively, and the funded status and amounts recognized in the statements of financial position for the plan:

**2016**

| | **Present value of defined benefit obligation** | **Fair value of plan assets** | **Restrictions on asset recognized** | **Net pension asset** |
|---|---|---|---|---|
| At January 1 | **₱41,156,081** | **(₱60,469,658)** | **₱4,214,366** | **(₱15,099,211)** |
| *Benefit cost in profit or loss* | | | | |
| Current service cost | **1,852,430** | **–** | **–** | **1,852,430** |
| Net interest income (Note 21) | **2,057,804** | **(2,919,307)** | **210,718** | **(650,785)** |
| *Remeasurements in OCI* | | | | |
| Actuarial loss on plan assets | **–** | **2,280,536** | **–** | **2,280,536** |
| Actuarial gain (loss) on defined benefit obligation | | | | |
| Financial assumption | **58,405** | **–** | **–** | **58,405** |
| Experience adjustments | **(1,515,358)** | **–** | **–** | **(1,515,358)** |
| Change in the effect of asset ceiling | **–** | **–** | **(1,041,271)** | **(1,041,271)** |
| Benefits paid | **(4,167,026)** | **4,167,026** | **–** | **–** |
| At December 31 | **₱39,442,336** | **(₱56,941,403)** | **₱3,383,813** | **(₱14,115,254)** |
| Actual return on plan assets | | **₱638,771** | | |

2015

| | Present value of defined benefit obligation | Fair value of plan assets | Restrictions on asset recognized | Net pension asset |
|---|---|---|---|---|
| At January 1 | ₱41,010,203 | (₱62,753,927) | ₱5,043,015 | (₱16,700,709) |
| *Benefit cost in profit or loss* | | | | |
| Current service cost | 1,909,880 | – | – | 1,909,880 |
| Net interest income (Note 22) | 2,095,621 | (3,139,452) | 257,698 | (786,133) |
| *Remeasurements in OCI* | | | | |
| Actuarial loss on plan assets | – | 2,790,713 | – | 2,790,713 |
| Actuarial gain on defined benefit obligation | | | | |
| Financial assumption | (203,059) | – | – | (203,059) |
| Experience adjustments | (1,023,556) | – | – | (1,023,556) |
| Change in the effect of asset ceiling | – | – | (1,086,347) | (1,086,347) |
| Benefits paid | (2,633,008) | 2,633,008 | – | – |
| At December 31 | ₱41,156,081 | (₱60,469,658) | ₱4,214,366 | (₱15,099,211) |
| Actual return on plan assets | | ₱348,739 | | |

The fair value of plan assets by each class as at the end of the reporting period of the Company are as follow:

| | **2016** | 2015 |
|---|---|---|
| Mutual funds | **₱26,210,128** | ₱29,394,301 |
| Equity instrument | **16,199,829** | – |
| Government securities | **6,707,697** | 18,884,674 |
| Investment in UITF | **6,616,591** | 11,029,666 |
| Others | **1,207,158** | 1,161,017 |
| Fair value of plan assets | **₱56,941,403** | ₱60,469,658 |

The Company's investment in the plan assets carried at fair value are classified under the Level 1 category in the Fair Value Hierarchy.

For the year ended December 31, 2016 and 2015, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

The principal actuarial assumptions used in determining retirement benefit obligations follow:

| | **2016** | 2015 |
|---|---|---|
| Discount rate | **4.81%** | 5.00% |
| Salary increase rate | **4.00%** | 4.00% |
| Average remaining working lives of employees | **16.9 years** | 15.7 years |

Below shows the sensitivity analysis determined based on reasonably possible changes of each significant assumptions stated above as of December 31, 2016 and 2015, assuming all other assumptions were held constant:

| | Increase (decrease) in rates | Impact on Defined Benefit Obligation 2016 | 2015 |
|---|---|---|---|
| Discount rate | +1.0% | (₱294,009) | (₱268,288) |
| | (1.0%) | 328,901 | 296,502 |
| Salary increase rate | +1.0% | 283,316 | 253,536 |
| | (1.0%) | (259,075) | (217,593) |

Shown below is the maturity analysis of the undiscounted benefit payments as of December 31:

| | 2016 | 2015 |
|---|---|---|
| Less than 1 year | **₱18,044,438** | ₱19,746,954 |
| More than 1 year to 5 years | **5,304,199** | 7,018,921 |
| More than 5 years to 10 years | **5,449,812** | 2,229,982 |
| Total | **₱28,798,449** | ₱28,995,857 |

The Company expects no contribution to the plan in 2017.

## 25. Personnel Expenses

This account consists of:

| | 2016 | 2015 |
|---|---|---|
| Salaries and wages | **₱25,231,031** | ₱22,758,501 |
| Net pension expense (Note 24) | **1,852,430** | 1,909,880 |
| Other employee benefits | **9,243,192** | 9,305,495 |
| | **₱36,326,653** | ₱33,973,876 |

## 26. Income Tax

The benefit from income tax consists of:

| | 2016 | 2015 |
|---|---|---|
| Current – MCIT | **₱1,115,262** | ₱6,651,812 |
| Final | **1,728,995** | 1,399,742 |
| Deferred | **(3,503,064)** | (8,642,885) |
| | **(₱658,807)** | (₱591,331) |

The Company adjusted the 2015 provision for deferred income tax to reflect the movement in deferred tax liability pertaining to the depreciation recognized on the revaluation increment. The provision for income tax deferred decreased by ₱183,110 resulting to an increase in net income by the same amount. The adjustment has no effect on the reported amounts in the 2015 statement of financial position and statement of cash flows.

Deferred Tax

The details of the Company's net deferred tax liabilities are as follows:

| | 2016 | 2015 |
|---|---|---|
| **Presented in profit or loss** | | |
| Deferred tax liabilities on: | | |
| Fair value gain on investment properties | **₱23,088,972** | ₱27,069,000 |
| Deferred acquisition costs | **23,522,995** | 27,086,848 |
| Accrued rental income | **397,982** | 33,454 |
| Forex gain – net | **341,426** | – |
| Total deferred tax liabilities | **47,351,375** | 54,189,302 |
| Deferred tax assets on: | | |
| Provision for IBNR | **9,122,953** | 790,428 |
| Excess of reserve per books over tax basis | **7,783,868** | 20,378,413 |
| Deferred reinsurance commission | **1,473,177** | 1,380,607 |
| Deferred reinsurance premiums | **1,205,047** | 1,311,387 |
| Allowance for impairment losses | **984,121** | 863,766 |
| Pension asset | **1,387,197** | 1,026,703 |
| Total deferred tax assets | **21,956,363** | 25,751,304 |
| | **25,395,012** | 28,437,998 |
| **Presented in OCI** | | |
| Deferred tax liabilities: | | |
| Revaluation reserve | **50,066,832** | 48,370,229 |
| Pension asset | **5,621,774** | 5,556,467 |
| | **55,688,606** | 53,926,696 |
| Net deferred tax liabilities | **₱81,083,618** | ₱82,364,694 |

The Company's unrecognized deferred tax asset amounted to ₱1.12 million and nil as of December 31, 2016 and 2015.

In 2015, the Company applied its remaining balance of excess MCIT which was incurred in 2013 amounting to ₱281,195.

The reconciliation of pretax income computed at the statutory tax rate to provision for income tax follows:

| | 2016 | 2015 |
|---|---|---|
| Statutory income tax rate | **30.00%** | 30.00% |
| Reduction in income tax resulting from: | | |
| Interest income subjected to final tax | **(19.24)** | (1.97) |
| Changes in unrecognized deferred tax assets | **(12.11)** | – |
| Nondeductible expenses | **6.82** | 2.04 |
| Nontaxable income | **(0.44)** | (32.13) |
| Dividend income exempt from tax | **(0.05)** | (0.01) |
| Effective income tax rate | **4.98%** | (2.07%) |

## 27. Management of Capital, Insurance and Financial Risks

Governance Framework

The Company has established a risk management function with clear terms of reference and with the responsibility for developing policies on market, credit, liquidity, insurance and operational risks. It also supports the effective implementation of policies at the individual business unit levels. The policies define the Company's identification of risk and its interpretation, limit structure to ensure the appropriate quality and diversification of assets, alignment of underwriting and reinsurance strategy to the corporate goals and specify reporting requirements.

Capital Management Framework

The Company maintains a certain level of capital to ensure sufficient solvency margins and to adequately protect the policyholders. The level of capital maintained is usually higher than the minimum capital requirements set by the regulators and the amount computed under the Risk-based Capital (RBC) Requirement model.

To ensure compliance with these externally-imposed capital requirements, it is the Company's policy to monitor the regulatory requirements of the IC on a quarterly basis as part of the Company's internal financial reporting process.

As of December 31, 2016 and 2015, the Company fully complied with the externally-imposed capital requirements during the reported financial periods. These are the fixed capitalization requirement and RBC requirement.

Fixed Capitalization Requirements and Minimum Statutory Networth

On August 5, 2013, the President of the Philippines approved Republic Act No. 10607 to be known as the "New Insurance Code" which provides the new capitalization requirements for all existing insurance companies based on net worth on a staggered basis starting June 30, 2013 up to December 31, 2022. The following presents the amount of required networth and the schedule of compliance per New Insurance Code:

| Networth | Compliance Date |
|---|---|
| ₱250,000,000 | June 30, 2013 |
| 550,000,000 | December 31 ,2016 |
| 900,000,000 | December 31, 2019 |
| 1,300,000,000 | December 31, 2022 |

On January 13, 2015, the IC issued the Circular Letter (CL) No. 2015-02-A which provides for the clarification of minimum capital requirements under Sections 194, 197, 200 and 289 of the New Insurance Code. The said circular supersedes the Department Order Nos. 27-06 and 15-2012 and CL Nos. 22-2008 and 26-2008.

The minimum networth requirement must remain unimpaired for the continuance of the license.

As of December 31, 2016 and 2015, the Company's estimated statutory net worth amounted to ₱661.59 million and ₱651.97 million, respectively.

Risk-based capital requirements

Insurance Memorandum Circular (IMC) No. 7-2006 provides for the RBC framework for the non-life insurance industry to establish the required amounts of capital to be maintained by the companies in relation to their investment and insurance risks. Every non-life insurance company is annually required to maintain a minimum RBC ratio of 100% and not fail the trend test. Failure to meet the minimum RBC ratio shall subject the insurance company to the corresponding regulatory intervention which has been defined at various levels.

The RBC ratio shall be calculated as net worth divided by the RBC requirement. Net worth shall include the company's paid-up capital, contributed and contingency surplus and unassigned surplus. Revaluation and fluctuation reserve accounts shall form part of net worth only to the extent authorized by the IC. The RBC requirement is the ratio of the number of insurers which are able to meet the corresponding RBC Hurdle Rate requirement for a given year to the total number of insurers in the industry.

The following table shows how the RBC ratio was determined by the Company:

| | **2016** | 2015 |
|---|---|---|
| Net worth | **₱661,591,339** | ₱651,967,062 |
| RBC requirement | **353,266,926** | 296,573,053 |
| RBC Ratio | **187.28%** | 219.83% |

Under Section D of IMC No. 7-2006, Mandatory Control Event shall occur if the RBC ratio of the company is less than 35%. Should this event occur, the Commissioner is required to place the company under regulatory control under Sec. 247 (Title 13, Suspension or Revocation of Authority) of the Code. The Mandatory Control Event shall be deemed sufficient grounds for the Commissioner to take action under Sec. 247 of the Insurance Code.

The final amount of the RBC can only be determined after the accounts of the Company have been examined by the IC, particularly with respect as to determination of admitted and non-admitted assets. Further, the IC is already in the process of finalizing the new RBC computation under the Insurance Code.

New regulatory framework

Pursuant to the powers vested in the Insurance Commissioner by Sections 189, 200, 437 and 438 of Republic Act (RA) No. 10607, otherwise known as the Insurance Code, as amended, the following regulatory requirements and actions for the new regulatory framework are hereby adopted and promulgated:

Circular Letter No. 2016-65, *Financial Reporting Framework under Section 189 of the Amended Insurance Code (Republic Act No. 10607)*, prescribes the new financial reporting framework (FRF) that will be used for the statutory quarterly and annual reporting. This also includes rules and regulations concerning Titles III and IV of Chapter III of the Amended Insurance Code and all other accounts not discussed in the Amended Insurance Code but are used in accounting of insurance and reinsurance companies.

Circular Letter 2016-67, *Valuation Standards for Non-life Insurance Policy Reserves*, prescribes the new valuation methodology for the non-life insurance companies. Non-life insurance companies will be changing the basis of valuation of their non-life insurance reserves. In addition to the unearned premium reserves, the concept of unexpired risk reserves is also included in the calculation of the premium liability. The incurred but not reported (IBNR) reserves will now be computed using actuarial projection techniques such as but not limited to the chain ladder method, expected loss ratio method and Bornheutter-Ferguson method. A margin for adverse deviation is estimated based on standard projection techniques or combination of such techniques, such as but not limited to the Mack Method, Bootstrapping Method, Stochastic Chain Ladder Method to bring the actuarial estimate of the Policy Liabilities at the 75th percentile level of sufficiency. Discount rates to be used shall be current risk-free rates. The rates shall exactly match the duration of the policy and the currency of the cash flows and shall be prescribed by the Insurance Commission.

Circular Letter No. 2016-68, *Amended Risk-Based Capital (RBC2) Framework*, prescribes that all insurance companies must satisfy the minimum statutory RBC ratio of 100% and not fail the Trend Test as stated under Section 3 of this Circular. The RBC ratio of an insurance company shall be equal to the Total Available Capital (TAC) divided by the RBC requirement.

*Implementation requirements and transition accounting*
Circular Letter No. 2016-69, *Implementation Requirements for Financial Reporting, Valuation Standards for Insurance Policy Reserves and Amended Risk-based Capital Framework*. The new regulatory requirements under circular letters 2016-65, 2016-67, 2016-68 and 2016-69 shall take effect beginning January 1, 2017.

Circular Letter No. 2017-15, *Regulatory Requirements and Actions for the New Regulatory Framework*. The cumulative prior year impact of the changes arising from the adoption of the New Financial Reporting Framework, including the revaluation of the reserves for Claims and Premiums Liabilities computed based on the new valuation standards for non-life insurance policy reserves as provided under CL No. 2016-67, shall be recognized in Retained Earnings – Transition Adjustments account. All changes in valuation shall be measured net of any tax effect.

Consolidated Compliance Framework
IMC 10-2006 integrated the compliance standards for the fixed capitalization and RBC framework. The fixed capitalization requirement for a given period may be suspended for insurers that comply with the required RBC hurdle rate, provided that the industry complies with the required Industry RBC Ratio Compliance Rate. The IMC provides the annual schedule of progressive rates for the Industry RBC Ratio Compliance Rates and the RBC Hurdle Rates from 2007 to 2011. For the review year 2013 which shall be based on the 2012 synopsis, the Industry RBC Ratio Compliance Rate is 90% and the RBC Hurdle Rate is 250%. For the review year 2012 which shall be based on the 2011 synopsis, the Industry RBC Ratio Compliance Rate is 90% and the RBC Hurdle Rate is 250%. Failure to achieve one of the rates will result in the imposition of the fixed capitalization requirement for the period under review. As of December 31, 2016 and 2015, the Company has complied with the RBC requirement.

Insurance Risk
The risk under an insurance contract is the risk that an insured event will occur including the uncertainty of the amount and timing of any resulting claim. The principal risk the Company faces under such contracts is that the actual claims and benefit payments exceed the carrying amount of insurance liabilities. This could occur due to any of the following:

Occurrence risk - the possibility that the number of insured events will differ from those expected.

Severity risk - the possibility that the cost of the events will differ from those expected.

Development risk - the possibility that changes may occur in the amount of an insurer’s obligation at the end of the contract period.

**2016**

| | Gross Claims Liabilities | Reinsurers' Share of Claims Liabilities | Net Claims Liabilities |
|---|---|---|---|
| Fire | **₱93,159,854** | **₱49,747,565** | **₱43,412,289** |
| Motorcar | **54,514,521** | **198,272** | **54,316,249** |
| Casualty and others | **91,727,204** | **74,243,475** | **17,483,730** |
| | **₱239,401,579** | **₱124,189,312** | **₱115,212,268** |

2015

| | Gross Claims Liabilities | Reinsurers' Share of Claims Liabilities | Net Claims Liabilities |
|---|---|---|---|
| Fire | ₱25,584,617 | ₱4,763,534 | ₱20,821,083 |
| Motorcar | 48,427,153 | 71,340 | 48,355,813 |
| Casualty and others | 134,313,620 | 108,719,957 | 25,593,663 |
| | ₱208,325,390 | ₱113,554,831 | ₱94,770,559 |

For general insurance contracts, the most significant risks arise from climate changes, natural disasters and terrorist activities. These risks vary significantly in relation to the location of the risk insured by the Company and types of risks insured.

The variability of risks is improved by diversification of risk of loss to a large portfolio of insurance contracts and as a more diversified portfolio is less likely to be affected across the board by change in any subset of the portfolio.

The variability of risks is also improved by careful selection and implementation of underwriting strategies, strict claims review policies to assess all new and ongoing claims, as well as the investigation of possible fraudulent claims. The Company also enforces a policy of actively managing and promptly pursuing claims, in order to reduce its exposure to unpredictable future developments that can negatively impact the Company.

The Company has also limited its exposure by imposing maximum claim amounts on certain contracts as well as the use of reinsurance arrangements. The purpose of these underwriting and reinsurance strategies is to limit exposure to catastrophes to a predetermined maximum amount based on the Company's premiums retained.

The majority of reinsurance business ceded is placed on a quota share basis with retention limits varying by product line and territory. Amounts recoverable from reinsurers are estimated in a manner consistent with the assumptions used for ascertaining the underlying policy benefits and are presented in the statement of financial position as reinsurance assets.

Although the Company has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to the reinsurance ceded, to the extent that any reinsurers is unable to meet its obligations assumed under such reinsurance agreements.

The Company's placement of reinsurance is diversified such that it is neither dependent on a single reinsurer nor are the operations of the Company substantially dependent upon any single reinsurance contract. There is no single counterparty exposure that exceeds 5% of the total reinsurance assets at the reporting date.

Fair Values of Financial Instruments
Due to the short-term nature of cash and cash equivalents, insurance receivables, loans and other receivables, insurance contract liabilities, insurance payables, and accounts payable and other liabilities, their carrying values reasonably approximate fair values at year-end.

The fair values of AFS financial assets that are actively traded in organized financial markets are determined by reference to quoted market bid prices, at the close of business on the reporting date or the last trading day as applicable. Unquoted AFS financial instruments are carried at cost, less any allowance for impairment loss. The fair values of HTM financial assets were determined using quoted market prices.

Due to long term nature of the HTM investments, its carrying value differs from its fair value. The fair value of HTM investments is based on the quoted market prices at the end the reporting date. The carrying value and the fair value of HTM investments as of December 31, 2016 and 2015, respectively, are summarized below.

| | **2016** | | 2015 | |
|---|---|---|---|---|
| | **Carrying Value** | **Fair Value** | Carrying Value | Fair Value |
| **HTM investments** | **₱154,751,813** | **₱195,322,474** | ₱119,337,823 | ₱119,863,464 |

The Company's fair value of financial assets as of December 31, 2016 and 2015 amounted to ₱893,176,358 and ₱709,908,666, respectively. In addition, its fair value of financial liabilities as of December 31, 2015 and 2014 amounted to ₱740,644,279 and ₱615,452,289, respectively.

Fair Value Hierarchy
The table below presents the Company's financial instruments carried at fair value by valuation method as of December 31, 2016 and 2015. The different levels have been defined as follows:

| | **December 31, 2016** | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| **Financial assets** | | | | |
| **AFS financial assets** | **₱33,596,937** | **₱20,300** | – | **₱33,617,237** |

| | December 31, 2014 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Financial assets | | | | |
| AFS financial assets | ₱26,527,935 | ₱420,300 | – | ₱26,948,236 |

Financial Risk and Management
The Company is exposed to financial risk through its financial assets, financial liabilities, reinsurance assets and insurance liabilities. In particular, the key financial risk is that the proceeds from its financial assets are not sufficient to fund the obligations arising from its insurance contracts. The most important components of this financial risk are credit risk, liquidity risk and market risk.

These risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements.

*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 Company manages the level of credit risk setting up exposure limits for each counterparty or group of counterparties, and industry segments; right of offset where counterparties are both debtors and creditors; guidelines on obtaining collaterals and guarantees; reporting of credit risk exposures; monitoring compliance with credit risk policy and review of credit risk policy for pertinence and changing environment.

The Company further restricts its credit risk exposure by entering into master netting arrangements with counterparties with which it transacts significant volumes of transactions. Although, such arrangements do not generally result in offset of statement of financial position assets and liabilities, as transactions are usually settled on gross basis. However, the credit risk associated with such balances is reduced in the event of a default, when such balances are settled on a net basis. The situation may however change substantially within a short period following the reporting date because the exposure is affected by transactions subject to the arrangement.

Reinsurance is placed with high-rated counterparties and concentration of risk is avoided by following policy guidelines in respect of counterparties' limits that are set each year and are subject to regular reviews. At each year-end, management performs assessment of credit worthiness of reinsurers to update reinsurance purchase strategies and ascertaining suitable allowance for impairment of reinsurance assets.

In respect of investment securities, the Company secures satisfactory credit quality by setting maximum limits of portfolio securities with a single issuer or group of issuers, excluding those secured on specific assets and setting the minimum ratings for the issuer.

The Company sets the maximum amounts and limits that may be advanced to/placed with individual corporate counterparties which are set by reference to their long term ratings.

Credit risk exposure in respect of all other counterparties is managed by setting standard business terms that are required to be met by all counterparties. Commissions due to intermediaries are netted off against amounts receivable from them to reduce the risk of doubtful debts. The credit risk in respect of customer balances, incurred on nonpayment of premiums or contributions will only persist during the grace period specified in the policy document.

The Company did not have any significant concentration of credit risk with a single counterparty or group of counterparties and industry segments as of December 31, 2016 and 2015.

The table below shows the maximum exposure to credit risk for the components of its statement of financial position.

| | **2016** | 2015 |
|---|---|---|
| Cash and cash equivalents (excluding cash on hand) | **₱260,788,539** | ₱322,493,674 |
| Short-term investments | **60,586,358** | – |
| Insurance receivables (excluding taxes receivable) | **275,961,176** | 244,904,379 |
| HTM investments | **154,751,813** | 119,337,823 |
| Loans and receivables | | |
| Bond loss recoverable | **9,248,542** | 9,248,542 |
| Other receivables | **4,557,602** | 5,643,823 |
| Notes receivable | **2,955,507** | 3,046,861 |
| Accrued rent receivable | **1,326,605** | 111,514 |
| Receivable from tenants | – | 18,394 |
| Accrued interest income | **1,231,442** | 539,573 |
| Total | **₱771,407,584** | ₱705,344,583 |

As of December 31, 2016 and 2015, the carrying values of the Company's financial instruments represent maximum exposure to credit risk at reporting date. The gross maximum exposure to credit risk of the Company approximates its net maximum exposure. There were no amounts that are set-off in accordance with the criteria in PAS 32. There were no amounts subject to an enforceable master netting arrangement or similar agreement as of December 31, 2016 and 2014.

Since the Company transacts only with recognized, creditworthy third parties, there is no requirement for collateral. Insurance receivables and loans and receivables are highly collectible. Cash and cash equivalents are placed with reputable financial institution.

The standard credit-term given by the Company is 90 days. However, accounts more than 90 days may be past due but not necessarily impaired. A 180-day credit term may be given for those accounts with reciprocal business and those accounts involving large amounts of sum insured or the jumbo accounts which as practiced are subject to quarterly remittance scheme.

*Liquidity risk*
Liquidity or funding risk is the risk that an entity will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from either the inability to sell financial assets quickly at their fair values; or counterparty failing on repayment of a contractual obligation; or insurance liability falling due for payment earlier than expected; or inability to generate cash inflows as anticipated.

The major liquidity risk confronting the Company is the daily calls on its available cash resources in respect of claims arising from insurance contracts.

The Company manages liquidity specifying minimum proportion of funds to meet emergency calls; setting up of contingency funding plans; specifying the sources of funding and the events that would trigger the plan; determining concentration of funding sources; reporting of liquidity risk exposures; monitoring compliance with liquidity risk policy and review of liquidity risk policy for pertinence and changing environment.

It is unusual for a Company primarily transacting insurance business to predict the requirements of funding with absolute certainty as theory of probability is applied on insurance contracts to ascertain the likely provision and the time period when such liabilities will require settlement. The amounts and maturities in respect of insurance liabilities are thus based on management's best estimate based on statistical techniques and past experience.

*Market risk*
Market risk is the risk of change in fair value of financial instruments from fluctuation in foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (price risk), whether such change in price is caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

The Company structures levels of market risk it accepts through a market risk policy that determines what constitutes market risk for the Company; basis used to fair value financial assets and liabilities; asset allocation and portfolio limit structure; diversification benchmarks by type of instrument and geographical area; sets out the net exposure limits by each counterparty or group of counterparties, geographical and industry segments; control over hedging activities; reporting of market risk exposures and breaches to the monitoring authority; monitoring compliance with market risk policy and review of market risk policy for pertinence and changing environment.

*Interest rate risk*
Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's exposure to interest rate risk relates primarily to its financial instruments with floating and/or fixed rates. Fixed rate financial instruments are subject to fair value interest rate risk while floating rate financial instruments are subject to cash flow interest rate risk.

For fair value interest rate risk, the Company's investment policy requires it to buy and hold AFS financial assets, unless the need to sell arises, and to reduce the duration gap between financial assets and financial liabilities to minimize interest rate risk.

The Company manages its interest rate risk by investing in fixed rate instruments. It also manages the maturities of interest-bearing financial assets and financial liabilities.

The following table shows the information relating to the financial assets that are exposed to fair value interest rate risk presented by maturity profile:

**December 31, 2016**

| | **Range of Interest** | **Up to a year** | **2-3 years** | **Over 3 years** | **Total** |
|---|---|---|---|---|---|
| Loans and receivable | **6.00%-14.00%** | **₱5,390,974** | **₱2,955,506** | **₱9,248,542** | **₱17,595,022** |
| Cash and cash equivalents | **0.25%-1.50%** | **452,915,879** | **–** | **–** | **322,565,374** |
| HTM debt securities | **1.625% 9.125%** | **143,063** | **40,086,297** | **114,522,453** | **154,751,813** |
| | | **₱458,449,916** | **₱43,041,803** | **₱123,770,995** | **₱625,262,714** |

December 31, 2015

| | Range of Interest | Up to a year | 2-3 years | Over 3 years | Total |
|---|---|---|---|---|---|
| Loans and receivable | 6.00%-14.00% | ₱16,458,954 | ₱– | ₱– | ₱16,458,954 |
| Cash and cash equivalents | 0.25%-1.50% | 322,565,374 | – | – | 322,565,374 |
| HTM debt securities | 1.625% 9.125% | 47,184,650 | 40,177,690 | 31,975,483 | 119,337,823 |
| | | ₱386,208,978 | ₱40,177,690 | ₱31,975,483 | ₱458,362,151 |

The Company is not exposed to significant interest rate risk since its debt instruments have fixed interest rate (cash flow interest rate risk) and is classified as HTM investments which is carried at amortized cost (fair value interest rate risk).

*Price risk*
The Company's price risk exposure at year-end relates to financial assets and liabilities whose values will fluctuate as a result of changes in market prices, principally AFS equity securities.

Such investment securities are subject to price risk due to changes in market values of instruments arising either from factors specific to individual instruments or their issuers or factors affecting all instruments traded in the market.

The Company's market risk policy requires it to manage such risks by setting and monitoring objectives and constraints on investments, diversification plan, limits on investment in each sector and market, and careful and planned use of derivative instruments.

The analysis below is performed for reasonably possible movements in Philippine Stock Exchange index (PSEi) with all other variables held constant, showing the impact on OCI (that reflects adjustments on changes in fair value of AFS financial assets).

**December 31, 2016**

| Market Indices | Change in Variable | Impact on OCI |
|---|---|---|
| **PSEi** | **+2.44%** | **₱407,504** |
| **PSEi** | **-2.44%** | **(₱407,504)** |

December 31, 2015

| Market Indices | Change in Variable | Impact on OCI |
|---|---|---|
| PSEi | +1.31% | ₱419,330 |
| PSEi | -1.31% | (₱419,330) |

The reasonably possible movements in PSEi are based on the Company's stock composite index for the past three years.

## 28. Related Party Transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. These include: (a) parties owning, directly or indirectly through one or more intermediaries, control, or are controlled by, or under common control, or are controlled by, or under common control with, the Company; (b) associates; and (c) individuals owning, directly or indirectly, an interest in the voting power of the Company that gives them significant influence over the Company and close members of the family of any such individuals.

On December 29, 2015, the investment in an associate was sold to the individual directors of Mercantile Careplans, Inc. (MCI) for ₱20.00 million.

As of December 31, 2016 and 2015, there are no advances extended by the Company to its directors and key officers.

Significant transactions with MCI follow:

December 31, 2015

| | Amount | Outstanding | Nature | Terms | Conditions |
|---|---|---|---|---|---|
| Accrued rent receivable | ₱236,148 | ₱21,648 | Amount uncollected for office rental | On demand, noninterest bearing | Unsecured; Not impaired |
| Advances | ₱507,049 | ₱346,101 | Amount paid for the Meralco bills of the tenant | On demand, noninterest bearing | Unsecured; Not impaired |

Advances to MCI are settled through cash.

Compensation of Key Management Personnel
Key management personnel of the Company include the President, Senior Vice-President, Department Managers, Supervisors and Officers-in-Charge.

The salaries and other short term employee benefits of key management personnel amounted to ₱8,523,989 and ₱10,462,565 in 2016 and 2015, respectively.

There are no agreements between the Company and any of its directors and key officers providing for benefits upon termination of employment, except for such benefits to which they may be entitled under the Company's retirement plan

## 29. Reconciliation of Net Income Under PFRS to Statutory Net Income

The reconciliation of net income under PFRS to statutory net income follows:

| | **2016** | 2015 |
|---|---|---|
| PFRS net income | **(₱12,580,913)** | ₱28,998,239 |
| Add (deduct): | | |
| Difference in change in unearned premiums - net | **(16,844,957)** | 51,774,867 |
| Deferred acquisition costs - net | **12,201,016** | (26,340,233) |
| Tax effect of PFRS adjustments | **1,393,182** | (7,630,390) |
| Statutory net income | **(₱15,831,672)** | ₱46,802,483 |

## 30. Commitments

Operating Lease Commitments - as Lessee
The Company entered into various lease agreements for its branch offices renewable every year. Future minimum rentals payable and rent expense under non-cancellable operating leases which are due within one (1) year amounted to ₱1.85 million and ₱1.71 million in 2016 and 2015, respectively.

Operating Lease Commitments - as Lessor
The Company has entered into commercial property leases on its investment property. These non-cancellable leases are renewable every year. All leases include a clause to enable upward revision of the rental charge on an annual basis based on prevailing market conditions. Future minimum rentals receivable under non-cancellable operating leases which are all due within one year amounted to ₱12.09 million and ₱4.52 million in 2016 and 2015, respectively. Rental income amounted to ₱14.19 million and ₱11.80 million in 2016 and 2015, respectively.

## 31. Contingencies

The Company is a defendant in several lawsuits arising from the normal course of carrying out its insurance business. Provisions have been recognized in the financial statements to cover liabilities that may arise as a result of adverse decisions that may be rendered by the courts. The information usually required by PAS 37, *Provisions, Contingent Assets and Contingent Liabilities,* is not disclosed on the grounds that it can be expected to prejudice the Company's position with regard to the outcome of these claims. In 2015, a provision of ₱1.22 million was recognized for estimated losses on claims by a third party.

## 32. Supplementary Tax Information under Revenue Regulations 15-2010

The Company reported and/or paid the following types of taxes for the year:

Value added tax (VAT)

Details of the Company's net sales/receipts, output VAT and input VAT accounts are as follows:

a. Net Sales/Receipts and Output VAT declared in the Company's VAT returns filed for 2016

| | Net Sales/ Receipts | Output VAT |
|---|---|---|
| Taxable sales: | | |
| Sale of services-premium | ₱538,881,956 | ₱64,665,870 |
| Leasing income | 14,187,360 | 1,702,483 |
| | ₱553,069,316 | ₱66,368,353 |

The Company's sales of services are based on actual collections received, hence, may not be the same as amounts accrued in the statement of comprehensive income in 2015.

b. Input VAT for 2016

| | |
|---|---|
| Balance at January 1 | ₱680,998 |
| Current year's domestic purchases/payments for: | |
| Goods other than for resale | 820,877 |
| Services lodged under cost of goods sold | 23,048,459 |
| | 24,550,334 |
| Input VAT applied to Output VAT | 21,081,011 |
| Balance at December 31 | ₱3,469,323 |

The Company does not undertake importation activities.

Taxes and Licenses
This includes all other taxes, local and national, including real estate taxes, license and permit fees lodged under the 'Taxes and Licenses' under the 'Operating Expenses' section the Company's statement of income.

Details for 2016 consist of the following:

| | |
|---|---|
| *Local* | |
| License and permit fees | ₱923,549 |
| Real estate taxes | 1,726,775 |
| Donor's taxes | 918,704 |
| Penalties | 787,732 |
| Others | 550,097 |
| | 4,906,857 |
| *National* | |
| BIR Registration and other fees | 5,500 |
| | ₱4,912,357 |

The following taxes relate to nonlife insurance policies that have been shifted or passed on to the policyholders and are not recognized in the statement of comprehensive income in 2016:

| | |
|---|---|
| Documentary stamp taxes on: | |
| DS110-Policies of insurance upon property | ₱70,633,350 |
| DS114-CTPL | 1,580,771 |
| DS109-Accident and health | 7,670,625 |
| DS111-Fidelity bonds | 8,003,773 |
| Fire service taxes | 2,111,851 |
| Local government taxes | – |
| Premium taxes | 1,401,494 |
| | ₱91,401,864 |

Withholding Taxes
Details of withholding taxes for 2016 are as follows:

| | |
|---|---|
| Withholding taxes on compensation and benefits | ₱2,607,220 |
| Expanded withholding taxes | 17,183,578 |
| | ₱19,790,798 |

Tax Assessment and Cases
The Company has no deficiency tax assessments, whether protested or not. The Company has not been involved in any tax cases under preliminary investigation, litigation and/or prosecution in courts or bodies outside the BIR.