



ACCOUNTING & DISCLOSURE POLICY

FINANCIAL CONTROL GROUP



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Any act of divulgence to third parties shall be viewed seriously and warrant
disciplinary action.**

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Financial Control Group

VERSION CONTROL SHEET	
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Next Review Date This Policy will be reviewed in 3 years or earlier by Audit & Inspection Group and Compliance Group. Circulars concerning Accounting & Disclosure Policy issued by the Regulatory Authorities from time to time shall automatically become integral part of this Policy.

This Policy is to be distributed to the following persons, Group / divisions **;

Distribution List

S. No.	Group/ Division
1	Board of Directors
2	President
3	Group Chief (Audit & Inspection Group)
4	Group Chief (Compliance Group)
5	All Other Groups (involved in accounting)

*****This is a Bank-wide policy that is to be adopted and followed across the Bank including International Jurisdictions. Therefore, ensuring dissemination and adherence to all personnel of NBP will be the responsibility of the respective Group Chiefs, Divisional Heads, Country Heads and Regional Heads.***

1. PREAMBLE

Keeping in view the importance of policy framework, the State Bank of Pakistan has from time to time issued instructions in the form of various Circulars and Guidelines. In order to facilitate banks/ DFIs and to ensure compliance of regulatory requirements, the Banking Surveillance Department of State Bank of Pakistan had issued BSD Circular No. 3 dated April 4, 2007, a consolidated instruction on policy framework. The objective was to ensure that banks/DFIs have policies in various areas that are synchronized and have uniformity according to varied nature of their respective operations. Accordingly, the banks/DFIs were advised to formulate policies in certain key areas which included Accounting and Disclosure policy as minimum and ensure their regular updation. The policies to be formulated by each bank/ DFI is to be approved by their Board of Directors and should be in line with complexity of their operations and cover as a minimum, the requirements set out at Annexure – A of the BSD Circular No. 3.

2. ACCOUNTING & FINANCIAL REPORTING FRAMEWORK

The financial statements of the bank are prepared in accordance with approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board and Islamic Financial Accounting Standards (IFASs) issued by the Institute of Chartered Accountants of Pakistan as are notified under the Companies Act, 2017, the provisions of and directives issued under the Companies Act, 2017 and the Banking Companies Ordinance, 1962 and directives issued by the State Bank of Pakistan (SBP), Securities and Exchange Commission of Pakistan (SECP) and Pakistan Stock Exchange (PSX).

Wherever the requirements of the Companies Act, 2017, the Banking Companies Ordinance, 1962 or directives issued by SBP or SECP differ with the requirements of IFRSs or IFASs, the requirements of the Companies Act, 2017, the Banking Companies Ordinance, 1962 or the requirements of the said directives shall prevail.

2.1 List of International Financial Reporting Standards Applicable in Pakistan

IFRS 1	First-time Adoption of International Financial Reporting Standards
IFRS 2	Share-based Payment
IFRS 3	Business Combinations
IFRS 4	Insurance Contracts
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations
IFRS 7	Financial Instruments: Disclosures (Not applicable on Banks)
IFRS 8	Operating Segments

- IFRS 9 IFRS 9 'Financial Instruments
- IFRS 10 Consolidated Financial Statements (The SECP vide SRO 56 (1) / 2016 dated January 28, 2016, has notified that the requirements of IFRS 10 (Consolidated Financial Statements) and section 228 of the Companies Act, 2017 will not be applicable with respect to the investment in mutual funds established under Trust structure.)
- IFRS 11 Joint Arrangement
- IFRS 12 Disclosure of Interests in Other Entities
- IFRS 13 Fair Value Measurement
- IFRS 15 Revenue from Contracts with Customers
- IFRS 16 Leases
- IFRIC 22 Foreign Currency Transactions and Advance Consideration
- IAS 1 Presentation of Financial Statements
- IAS 2 Inventories
- IAS 7 Statement of Cash Flows
- IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors
- IAS 10 Events after the Reporting Period
- IAS 12 Income Taxes
- IAS 16 Property, Plant and Equipment
- IAS 19 Employee Benefits
- IAS 21 The Effects of Changes in Foreign Exchange Rates
- IAS 23 Borrowing Costs
- IAS 24 Related Party Disclosures
- IAS 27 Consolidated and Separate Financial Statements
- IAS 28 Investments in Associates
- IAS 32 Financial Instruments: Presentation
- IAS 33 Earnings per Share
- IAS 34 Interim Financial Reporting
- IAS 36 Impairment of Assets
- IAS 37 Provisions, Contingent Liabilities and Contingent Assets
- IAS 38 Intangible Assets
- IAS 40 Investment Property – (Not applicable for Banks in Pakistan)

2.2 List of Applicable Prudential Regulation

- Prudential Regulations for Agriculture Financing
- Prudential Regulations for Corporate / Commercial Banking
- Prudential Regulations for Consumer Financing
- Prudential Regulations for Small & Medium Enterprise Financing

2.3 Applicable laws

- Banking Companies Ordinance 1962
- Companies Act, 2017
- Income Tax Ordinance, 2001
- Sales Tax Act, 1990
- Sindh Sales tax on Services Act, 2011
- Punjab Sales tax on Services Act, 2012
- Baluchistan Sales tax on Services Act, 2015
- Kyber Pakhtunkhwa Sales tax on Services Act, 2022
- The Islamabad Capital Territory (Tax on Services) Ordinance, 2001
- Listed Companies Code of Corporate Governance Regulations, 2019
- Public Sector Companies (Corporate Governance) Rules, 2013

3. MATERIAL ACCOUNTING POLICIES

3.1 Accounting Policy Defined

Those principles, bases, convention, rules and practices applied by an entity that specify how the effects of transactions and other events are to be reflected in its financial statements through

- Recognizing,
- Selecting measurement bases for, and
- Presenting Assets, liabilities, gain, losses and changes to shareholders' equity. Accounting policies define the process whereby transactions and other events are reflected in financial statements.

3.2 Objectives in selecting accounting policies

The objectives against which an entity should judge the appropriateness of accounting policies to its particular circumstances are:

- **Relevance** - the objective of financial statements is to provide information about an entity's financial performance and financial position that is useful for assessing the stewardship of management and for making economic decisions. Financial information is relevant if it has the ability to influence the economic decision of users and is provided in time to influence those decisions. Appropriate accounting policies will result in financial information being presented that is relevant.

- **Reliability** – financial information is reliable if;
 1. It can be dependent upon by users to represent faithfully what is either purports to represent or could reasonably be expected to represent and therefore, reflects the substance of the transactions and other events that have taken place
 2. It is free from deliberate or systematic basis (i.e. it is neutral)
 3. It is free from material error
 4. It is completed within the bounds of materiality; and
 5. Under conditions of certainty, it has been prudently prepared (i.e. a degree of caution has been applied in exercising judgment and making the necessary estimates).

Appropriate accounting policies will result in financial information being presented that is reliable. They will present transactions and other events in a way that reflects their substance. A transaction or other event is faithfully presented in financial statements if the way in which it is recognized, measured and presented in those statements corresponds closely to the effect of that transaction or event.

- **Comparability** – information in an entity’s financial statements gains greatly in usefulness if it can be compared with similar information about the entity for some other period or point in time and with similar information about other entities. Such comparability can usually be achieved through a combination of consistency and disclosure. Appropriate accounting policies will result in financial information being presented in a way that enables users to discern and evaluate similarities in, and differences between, the nature and effects of transactions and other events taking place over time. In selecting accounting policies, an entity will assess whether accepted industry practices are appropriate to its particular circumstances.
- **Understandability** – information provided by financial statements needs to be capable of being understood by users having a reasonable knowledge of business and economic activities and accounting and a willingness to study with reasonable diligence the information provided. Appropriate accounting policies will result in financial information being presented in a way that enables its significance to be perceived by such users.

4. SCOPE OF ACCOUNTING & DISCLOSURE POLICY

The accounting and disclosure policy is applicable to all the Branches, Regional Offices, including Overseas Branches, Head Office in the preparation of financial statements.

However, in the case of overseas branches and domestic and local subsidiaries, each overseas branch is responsible for preparing accounting disclosure according to the accounting standards and laws of the respective countries in which branches and subsidiaries are operating.

5. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with accounting and reporting standards as applicable in Pakistan requires management to make judgments, estimates and assumptions that affect the reported amounts of assets and liabilities and income and expenses as well as in the disclosure of contingent liabilities. It also requires management to exercise judgment in application of its accounting policies. The estimates and associated assumptions used are based on historical experience and various other factors, that are believed to be reasonable under the circumstances. These estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised, if the revision affects only that period, or in the period of revision and in future periods if the revision affects both current and future periods.

a) **Credit Loss Allowance /Provision against non-performing loans and advances**

The Bank regularly reviews its loan portfolio to assess amount of non-performing loans and determine the credit loss allowance/provisions required there against at each reporting date. In assessing this requirement, various factors including the days past dues, delinquency in the account, financial position and future business / financial plan of the borrower, value of collateral held and requirements of SBP Prudential Regulations are considered. Credit loss allowances are maintained at the higher of ECL under IFRS 9 or the Prudential Regulation R-8. The Bank also considers the impact of Forced Sale Value (FSV) of collaterals when determining the amount of provisions.

General provisions for loan losses for overseas branches where IFRS-9 has not been implemented, are made as per the requirements of the respective central banks. Overseas branches may continue to follow local accounting requirement where IFRS-9 is not applicable but at Group level financial reporting will however continue to be consolidated in line with SBP directives on IFRS-9.

b) **Fair value of derivatives**

The fair values of derivatives which are not quoted in active markets are determined by using valuation techniques. The valuation techniques take into account the relevant interest and exchange rates over the term of the contract.

c) **Impairment of FVOCI investments**

Provision and ECL for unquoted debt securities is calculated as per SBP's Prudential Regulations and IFRS-9 respectively

A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Bank. If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Impairment/ECL of stage 3 FVOCI quoted TFCs, PTC, Ijarah Sukuks & Government Bonds is recognized in accordance with the requirements of Prudential Regulations and other directives issued by SBP as per subjective and objective criteria of Prudential Regulations after taking into account of FSV benefit under Prudential Regulations and IFRS-9.

d) Amortized Cost investments

The Bank follows the guidance provided in the SBP circulars and IFRS 9 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as Amortized Cost. In making this judgment, the Bank evaluates its intention and ability to hold such investments till maturity.

e) Income taxes

In making the estimates for current and deferred taxes, the management looks at the income tax law and the decisions of appellate authorities on certain issues in the past. There are certain matters where the Bank's view differs with the view taken by the income tax department and such amounts are shown as contingent liabilities.

f) Property and Equipment, Non-Banking asset and intangible assets, revaluation, depreciation and amortization

In making estimates of the depreciation / amortization method, the management uses the method which reflects the pattern in which economic benefits are expected to be consumed by the Bank. The method applied is reviewed at each financial year end and if there is a change in the expected pattern of consumption of the future economic benefits embodied in the assets, the method is changed to reflect the change in pattern.

The Bank also revalues its properties on a periodic basis. Such revaluations are carried out by independent valuer and involve estimates / assumptions and various market factors and conditions.

g) Defined benefit plans including pension expense

The liabilities for employees' benefits plans are determined using actuarial valuations. The actuarial valuations involve assumptions about discount rates, expected rates of return on assets, future salary increases, future inflation rates and future pension increases. Due to the long-term nature of these plans, such estimates are subject to significant uncertainty.

h) Provision against contingencies

Provision against contingencies is determined based on the management judgement regarding the probability of future outflows of resources embodying economic benefits to settle an obligation arising from past events.

i) Lease liability against right of use assets

The Bank applies judgement to determine the lease term for some lease contracts in which it is a lessee that includes renewal options. The assessment of whether the Bank is reasonably certain to exercise such options impacts the lease term, which significantly affects the amount of lease liabilities and right-of-use assets recognized.

Moreover, management exercises judgement in establishing the discount rate for new leases, utilizing the incremental borrowing rate as a benchmark.

j) Classification of financial assets and liabilities

The classification of financial assets is determined through solely payment and principal (SPPI) criteria and business model of the Bank. The Bank determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective.

The financial liabilities are being carried at amortized cost except for derivatives which are being measured at FVTPL.

k) Contingent assets and contingent liabilities

Contingent assets are not recognized and are also not disclosed unless an inflow of economic benefits is probable. Contingent liabilities are not recognized but are disclosed unless the probability of an outflow of resources embodying economic benefits are remote. The Bank uses estimates in determining the probability of inflow or outflow of economic benefits.

l) Impairment of non-financial assets

The carrying amount of the assets are reviewed at each Statement of Financial Position date to determine whether there is any indication of impairment. If such indication exists, the recoverable amount of the relevant asset is estimated. An impairment loss is recognized whenever the carrying amount of an asset exceeds its recoverable amount.

6. BASIS OF MEASUREMENT

The financial statements are prepared under the historical cost convention except that:

- i. Certain property and equipment and non-banking assets acquired in satisfaction of claims are stated at revalued amounts;

- ii. Investments classified at fair value through profit and loss and fair value through other comprehensive income are carried at fair value;
- iii. Foreign exchange contracts are measured at fair value; and
- iv. Staff retirement benefits are carried at present value;

7. MATERIAL ACCOUNTING POLICY INFORMATION

The material accounting policies that are applied in the preparation of financial statements are discussed below. IFRS-9 related policies pertaining to all financial assets, i.e. investments, loan and advances and any other financial assets have been discussed separately under clause 8 of the policy.

7.1 Cash and cash equivalents

Cash and cash equivalents include cash and balances with treasury banks, balances with other banks and call money lendings, less call borrowings and overdrawn nostro accounts having original maturity of three months or less.

7.2 Investments

Investments include Federal Government securities, shares, mutual funds, non-Government debt securities, foreign securities, associates and subsidiaries.

Associates are all entities over which the Bank has significant influence but not control. Investment in associates is carried at cost less accumulated impairment losses, if any.

Subsidiary is an entity over which the Bank has control. Investment in subsidiaries is carried at cost less accumulated impairment losses, if any.

7.3 Repurchase and resale agreements

Securities sold with a simultaneous commitment to repurchase at a specified future date (repos) continue to be recognized in the statement of financial position and are measured in accordance with accounting policies for investment securities. The counterparty liability for amounts received under these agreements is included in borrowings. The difference between sale and repurchase price is treated as mark-up/return/interest expense and accrued over the life of the Repo agreement using effective yield method.

Securities purchased with a corresponding commitment to resell at a specified future date (reverse repos) are not recognized in the statement of financial position, as the Bank does not obtain control over the securities. Amounts paid under these agreements are included in lending's to financial institutions. The difference between purchase and resale price is treated as mark-up/return/interest income and accrued over the life of the reverse repos agreement using effective yield method.

7.4 Advances

Loans and advances including net investment in finance lease are stated net of credit loss allowance / provisions against non-performing loan and advances. Credit loss allowance / provisions against loans and advances have been made in accordance with the requirements of Prudential Regulations and IFRS 9 application instructions issued by SBP. General provisions against loans and advances have been maintained as allowed by SBP until December 31, 2026. Advances are written off / charged off when there are no realistic prospects of recovery or to clean up the balance sheet as allowed by the SBP.

Subsidised loans disbursed under Temporary Economic Refinance Facility (TERF) have been recorded at fair value resulting in recognition of fair value adjustment on initial recognition. Unwinding of income on fair value adjustment is recognised in the statement of profit and loss account.

7.4.1 Islamic financing and related assets

Murabaha financing is a cost-plus profit transaction. Under Murabaha financing, funds disbursed for the purchase of goods are recorded as advance against Murabaha finance and the financing is recorded at the deferred sale price. Profit earned on financing is recognised as unearned income and amortised into the profit and loss account over the term of the Murabaha financing. Goods purchased but remaining unsold at the statement of financial position date are recorded as inventories.

Assets given on Ijarah are stated at cost less accumulated depreciation and accumulated impairment losses, if any. Ijarah assets are depreciated on a reducing balance basis over the term of the Ijarah after taking into account the estimated residual value. Impairment of Ijarah assets is recognised in line with the Prudential Regulations or upon the occurrence of an impairment event which indicates that the carrying value of the Ijarah asset may exceed its recoverable amount.

In Running Musharakah, the Bank and the customer enter into a Musharakah agreement where the Bank agrees to finance the operating activities of the customer's business and share in the statement of profit and loss account in proportion to an agreed ratio at an agreed frequency.

Under Diminishing Musharakah financing, the Bank creates joint ownership with the customer over the tangible assets to fulfil capital expenditure / project requirements. The Bank receives periodic payments from the customer partly for renting its portion of the assets to the customer and partly for the gradual transfer of its share of ownership to the customer. The rental payment is recognised as profit while the asset transfer / sale payments are applied towards reducing the outstanding principal.

In Istisna transactions, the Bank finances the cost of goods manufactured by the customer. Once the goods are manufactured, these are sold by the customer as an agent of the Bank to recover the cost plus the agreed profit.

Under *Tijarah*, the Bank purchases the finished goods from the customer against payment, takes possession and appoint customer as an agent to sell these goods to ultimate buyer on deferred payment basis. Goods purchased by the Bank and sold by the customer on a deferred payment basis are recognised as financing, while goods purchased by the Bank but remaining unsold by the customer are recorded as inventories. Profit is recognized on accrual basis over the period of transaction.

Wakalah is an agency contract in which Bank provides funds to the customer who invests it in a Shariah compliant manner. This is recorded as financing and profit is recognised on an accrual basis.

In *Musawamah* financing, the Bank purchases the goods and after taking the possession, sells them to the customer either in spot or credit transaction, without disclosing the cost.

7.5 Fixed Assets & Depreciation

7.5.1 Property and Equipment

7.5.1.1 Owned assets

Property and Equipment except land and buildings are stated at cost less accumulated depreciation and accumulated impairment losses, if any. Land is stated at revalued amount. Buildings are stated at revalued amount less accumulated depreciation and accumulated impairment losses, if any. The cost and the accumulated depreciation of property and equipment of foreign branches include exchange differences arising on currency translation at the year-end rates..

Depreciation is charged to statement of profit and loss account applying the straight line method except buildings, which are depreciated on diminishing balance method.

Depreciation on addition is charged from the month in which the assets are available for use and no depreciation is charged in the month the assets are disposed off.

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 bank and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of profit and loss account during the period in which they are incurred.

Assets are derecognised when disposed off or when no future economic benefits are expected from its use or disposal. Gains and losses on disposal of property and equipment are included in statement of profit and loss account.

The assets' residual values and useful lives are reviewed annually, and adjusted if appropriate, at statement of financial position date.

Land and buildings' valuations are carried out by professionally qualified valuers with sufficient regularity to ensure that their carrying amounts do not differ materially from their fair value.

- Any revaluation increase arising on the revaluation of such assets is recognised in the statement of comprehensive income and accumulated in equity, except to the extent that it reverses a revaluation decrease for the same asset previously recognised in the statement of profit and loss account, in which case the increase is credited to statement of profit and loss account to the extent of the decrease previously expensed. A decrease in the carrying amount arising on the revaluation of such assets is recognised in statement of profit and loss account to the extent that it exceeds the balance, if any, held in “Surplus on Revaluation of Fixed Assets” relating to a previous revaluation of that asset.
- Depreciation on assets which are revalued is determined with reference to the value assigned to such assets on revaluation and depreciation charge for the year is taken to the statement of profit and loss account.
- An amount equal to incremental depreciation for the year net of associated deferred tax is transferred from “Surplus on Revaluation of Fixed Assets” to unappropriated profit through statement of changes in equity to record realization of surplus to the extent of the incremental depreciation charge for the year. On the subsequent sale or retirement of a revalued asset, the attributable revaluation surplus remaining in the revaluation reserve is transferred directly to unappropriated profit.

7.5.2 Capital work in progress

Capital work in progress is stated at cost less accumulated impairment losses, if any. These are transferred to specific assets as and when assets are available for use.

7.5.3 Impairment

The carrying values of fixed assets are reviewed for impairment when events or changes in circumstances indicate that the carrying values may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amounts, the fixed assets are written down to their recoverable amounts.

The resulting impairment loss is taken to the profit and loss account except for impairment loss on revalued assets, which is adjusted against the related revaluation surplus to the extent that the impairment loss does not exceed the surplus on revaluation of assets. Where impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised recoverable amount but limited to the extent of the amount which would have been determined had there been no impairment. Reversal of impairment loss is recognized as income in the statement of profit and loss account.

7.6 Lease liability and right-of-use assets

The lease liabilities are initially measured at the present value of lease payments that includes:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payment that are based on an index or a rate at the commencement date;
- amounts expected to be payable by the lessee under residual value guarantees, if any;
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option; and
- payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

The lease payments are to be discounted using incremental borrowing rate, being the rate that the Bank would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions.

On initial recognition, right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability;
- any lease payments made at or before the commencement date less any lease incentives received;
- any initial direct costs incurred; and
- an estimate of restoration costs.

The Bank leases various offices / branches for the purpose of its operational activities. Rental contracts are typically made for fixed periods of 3 to 10 years. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants, but leased assets may not be used as security for borrowing purposes.

7.7 Intangible assets

Intangible assets are stated at cost less accumulated amortization and accumulated impairment losses, if any. The cost and the accumulated amortization of intangible assets of foreign branches include exchange differences arising on currency translation at the year-end rates. Amortization is charged to the statement of profit and loss account applying the straight-line method. Amortization on addition is charged from the month in which the assets are available for use and no amortization is charged in the month the intangible assets are disposed off. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

7.8 Non-banking assets acquired in satisfaction of claims

In accordance with the requirements of the 'Regulations for Debt Property Swap' (the regulations) issued by SBP vide its BPRD Circular No. 1 of 2016, dated January 1, 2016, the non-banking assets acquired in satisfaction of claims are carried at revalued amounts less accumulated depreciation. These assets are revalued by professionally qualified valuers with sufficient regularity to ensure that their net carrying value does not differ materially from their fair value. A surplus arising on revaluation is credited to the 'surplus on revaluation of fixed assets' account and any deficit arising on revaluation is taken to the profit and loss account directly. Legal fees, transfer costs and direct costs of acquiring title to property is charged to profit and loss account and not capitalized. Depreciation on non-banking assets acquired in satisfaction of claims is charged to profit and loss account on the same basis as depreciation charge on the bank's owned fixed assets.

7.9 Deposits and their cost

Deposits are recorded at the fair value of proceeds received.

Deposits costs are recognized as an expense in the period in which these are incurred using effective yield method.

7.10 Taxation

7.10.1 Current

Provision of current taxation is based on taxable income for the year determined in accordance with the prevailing laws of taxation on income earned for local as well as foreign operations, as applicable to the respective jurisdictions. The charge for the current tax also includes adjustments wherever considered necessary relating to prior year, arising from assessments framed during the year.

7.10.2 Deferred

Deferred tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax assets are recognized for all deductible temporary differences and unused tax losses, to the extent that it is probable that taxable profits will be available against which the deductible temporary differences and unused tax losses can be utilized. Deferred tax is not recognised on differences relating to investment in subsidiaries and branches to the extent the deductible temporary difference probably will not reverse in the foreseeable future.

The carrying amount of deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit or

deductible temporary differences will be available to allow all or part of the deferred income tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax relating to gain / loss recognised on surplus on revaluation of assets is charged / credited to such account.

7.11 Employee benefits

7.11.1 Defined Benefits Plans

The Bank operates an approved funded pension scheme, an un-funded post retirement medical benefits scheme and an un-funded benevolent scheme for its eligible employees. The Bank also operates an un-funded gratuity scheme for its eligible contractual employees. An actuarial valuation of all defined benefit schemes is conducted every year. The valuation uses the Projected Unit Credit Method. Remeasurements of the net defined benefit liability / assets which comprise actuarial gains and losses, return on plan assets (excluding interest) and the effect of asset ceiling (if any, excluding interest) are recognised immediately in other comprehensive income. Past-service costs are recognised immediately in the statement of profit and loss account when the plan amendment occurs.

7.11.2 Other employee benefits

7.11.2.1 Employees' Compensated Absences

The Bank operates a non-funded compensated absences benefits plan for its eligible employees and makes provision in financial statements for its liability towards compensated absences. This liability is estimated on the basis of actuarial advice under the Projected Unit Credit Method.

7.12 Revenue Recognition and Mark Up / Non Mark Up Income

Revenue is recognised to the extent that the economic benefits associated with a transaction will flow to the Bank and the revenue can be reliably measured.

7.12.1 Advances and Investment

Income on loans and advances and debt security investments are recognized on a time proportion basis that takes into account effective yield on the asset. In case of advances and investments , profit suspended in compliance with the Prudential Regulations issued by the SBP is recognized on receipt basis.

Interest/mark-up on rescheduled/restructured advances and investments is recognized in accordance with the Prudential Regulations of SBP.

Where debt securities (excluding FVTPL) are purchased at a premium or discount, those premiums / discounts are amortised through the statement of profit and loss account over the remaining maturity.

7.12.2 Non mark up / interest income

The Bank earns fee and commission income from certain non-funded banking services. The related fee and commission income is recognised at an amount that reflects the consideration to which the Bank expects to be entitled in exchange for providing the services. The recognition of fee and commission income depends on the purpose for which the fees are received. Fee and commission income is recognised when or as an entity satisfies the performance obligation, either over time or at a specific point of time. Unearned fees and commissions are included under Other liabilities.

Commission on letters of credit and guarantees is recognized on time proportion basis.

Dividend income on equity investments is recognized when right to receive is established.

Gains and losses on disposal of investments , property and equipment, intangible assets and Ijarah assets are dealt with through the profit and loss account in the year in which they arise.

Gain or loss on sale / modification of financial assets is included in the unconsolidated statement of profit and loss account in the period in which they arise.

7.12.3 Lease Financing

Income from lease financing is accounted for using the financing method. Under this method, the unearned lease income (defined as the sum of total lease rentals and estimated residual value less the cost of the leased assets) is deferred and taken to income over the term of the lease so as to produce a constant periodic rate of return on the outstanding net investment in the lease. Gains or losses on termination of lease contracts are recognised through the statement of profit and loss account when these are realised. Unrealised lease income and other fees on classified leases are recognised on a receipt basis.

7.13 Net investment in finance lease

Leases where the bank transfers substantially all the risk and rewards incidental to ownership of the assets to the lessee are classified as finance leases. Net investment in finance lease is recognised at an amount equal to the aggregate of present value of minimum lease payment including any guaranteed residual value and excluding unearned finance income, write-offs and provision for doubtful lease finances, if any.

7.14 Foreign Currency Translation and Foreign Operation

7.14.1 Foreign Currencies Translation

The bank's financial statements are presented in Pak Rupees (Rs.) which is the Bank's functional and presentation currency.

Foreign currency transactions are converted into Rupees applying the exchange rate at the date of the respective transactions. Monetary assets and liabilities in foreign currencies including assets/liabilities of foreign branches are translated into Rupees at the rates of exchange prevailing at the statement of financial position date. Forward exchange contracts are valued at rates applicable to their respective maturities. All gains or losses on dealing in foreign currencies are taken to the statement of profit and loss account.

Commitments for outstanding forward foreign exchange contracts are disclosed in these financial statements at committed amount. Contingent liabilities / commitments for letters of credit and letters of guarantee denominated in foreign currencies are expressed in rupee terms at the rate of exchange prevailing at the statement of financial position date.

7.14.2 Foreign Operation

Statement of Profit and loss account balances of foreign branches are translated at average exchange rate prevailing during the year. Gains and losses on translation are included in the profit and loss account except net gain arising on translation of net investment in foreign branches, which is credited to an exchange equalization reserve reflected under reserves.

Statement of financial position balances of foreign branches are translated at exchange rate prevailing at statement of financial position date. Gains and losses on translation are included in the statement of profit and loss account except gains / losses arising on translation of net assets of foreign branches, which is credited to the statement of comprehensive income.

7.15 Credit Allowance for Off Balance Sheet Obligations

ECL for guarantees, claims and other off balance sheet obligations are made when the bank has legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate of amount can be made. ECL against off balance sheet items created based on ORR or Days past dues of borrows and based on CCF factor on undrawn commitments. Charge to profit and loss account is stated net of expected recoveries.

7.16 Off Setting

Financial assets and financial liabilities are only set off and the net amount is reported in the financial statements when there is a legally enforceable right to set off and the Bank intends either to settle on a net basis, or to realize the assets and to settle the liabilities simultaneously.

7.17 Fiduciary Assets

Assets held in a fiduciary capacity are not treated as assets of the Bank in the statement of financial position.

7.18 Dividend and Other Appropriations

Dividend and other appropriations to reserve, except appropriations which are required by law are recognized in the Bank's financial statements in the year in which these are approved.

7.19 Earnings per share

The bank presents basic and diluted earnings per share (EPS) for its shareholders. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the year. Diluted EPS is determined by adjusting the statement of profit or loss account attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, if any.

7.20 Bai Muajjal

Bai Muajjal transactions represent sales of Sukuks on a deferred payment basis and are shown in lendings to financial institutions except for transactions undertaken directly with the Government of Pakistan which are disclosed as investments.

The difference between the deferred payment amount receivable and the carrying value at the time of sale is accrued and recorded as income over the life of the transaction.

7.21 Acceptances

Acceptances comprise undertakings by the Bank to pay bill of exchange drawn on customers. Acceptances are recognised as financial liability in the statement of financial position with a contractual right of reimbursement from the customer as a financial asset. Therefore, commitments in respect of acceptances have been accounted for as on balance sheet financial assets and financial liabilities.

7.22 Segment Reporting

A segment is a distinguishable component of the Bank that is subject to risks and rewards that are different from those of other segments. A business segment is one that is engaged either in providing certain products or services, where as a geographical segment is one engaged in providing certain product or services within a particular economic environment. Segment information is presented as per the Bank's functional and management reporting structure.

Business Segments

The Bank's primary segment reporting is based on the following business segments:

- i. **Retail Banking Group** includes retail lending and deposits, banking services, cards and branchless banking.
- ii. **Inclusive Development Group** consists of loans to individuals, agriculture, SME, commodity and commercial customers.
- iii. **Corporate and Investment Banking Group** offers a wide range of financial services to medium and large sized public and private sector entities. These services include, providing and arranging tenured financing, corporate advisory, underwriting, cash management, trade products, corporate finance products and customer services.
- iv. **Treasury** includes fixed income, equity, foreign exchange, credit, funding, own position securities, landings and borrowings and derivatives for hedging and market making.
- v. **International Financial Institution and Remittance Group** includes the results of all international branches, correspondent banking business and global remittances. This represents Bank's operations in 11 countries including Pakistan and 16 branches including one branch in Export Processing Zone in Pakistan.
- vi. **Aitemaad and Islamic Banking Group** provides shariah compliant services to customers including loans, deposits and other transactions.
- vii. **Head Office / Others** includes the head office related activities and other functions which cannot be classified in any of the above segments.

Geographical Segments

The Bank is managed along the following geographic lines for monitoring and reporting purposes:

- i. Pakistan (including branch in Export Processing Zone)
- ii. Asia Pacific (including South Asia)
- iii. Europe
- iv. United States of America
- v. Middle East

8. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRSS)

8.1 IFRS 9 - 'Financial Instruments'

As per the SBP BPRD Circular Letter No. 07 of 2023 dated April 13, 2023, IFRS 9 is applicable on banks with effect from January 01, 2024. IFRS 9 brings fundamental changes to the accounting for financial assets and to certain aspects of accounting for financial liabilities. To determine appropriate classification and measurement category, IFRS 9 requires all financial assets, except equity instruments, to be assessed based on combination of the entity's business model for managing the assets and the instruments' contractual cash flows characteristics. The adoption of IFRS 9 has also fundamentally changed the impairment method of financial assets with a forward-looking Expected Credit Losses (ECL) approach.

The SBP through BPRD Circular Letter No. 16 dated July 29, 2024 and BPRD Circular Letter No. 01 dated January 22, 2025 (Letters) has made certain amendments and clarified the timelines of some of the SBP's IFRS 9 Application Instructions to address the matters raised by the banks to ensure compliance by the timelines. The Letters have provided clarifications / relaxations on measurement of unquoted equity securities, modification accounting, maintenance of general provisions over and above ECL, accounting methodology for Islamic Banking Institutions and treatment of charity. In addition, the SBP in a separate instruction SBPHOK-BPRD-RPD-NBP-821909 dated January 22, 2025 has allowed extension for application of Effective Interest Rate up to December 31, 2025.

8.2 Classification

Financial assets

Under IFRS 9, existing categories of financial assets: Held for trading (HFT), available for sale (AFS), Held-to-maturity (HTM) and loans and receivables have been replaced by:

- Financial assets at fair value through profit or loss account (FVTPL)
- Financial assets at fair value through other comprehensive income (FVOCI)
- Financial assets at amortised cost

Financial liabilities

Under IFRS 9, the accounting for financial liabilities remains largely the same as before adoption of IFRS 9 and thus financial liabilities are being carried at amortised cost except for derivatives which are being measured at FVTPL.

8.2.1 Business model

The Bank determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective.

The Bank's business model is not assessed on an instrument-by-instrument basis, but at a higher level of aggregated portfolios and is based on observable factors such as:

- The objectives for the portfolio, in particular, whether management's strategy focuses on earning contractual revenue, maintaining a particular yield profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- How the performance of the business model and the financial assets held within that business model are evaluated and reported to the Bank's key management personnel;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed; and
- The expected frequency, value and timing of sales are also important aspects of the Bank's assessment. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account.

Eventually, the financial assets fall under either of the following three business models:

- i. Hold to Collect (HTC) business model: Holding assets in order to collect contractual cash
- ii. Hold to Collect and Sell (HTC&S) business model: Collecting contractual cash flows and selling financial assets
- iii. Other business models: Resulting in classification of financial assets as FVTPL

8.2.2 Assessments whether contractual cash flows are solely payments of principal and interest / profit (SPPI)

As a second step of its classification process, the Bank assesses the contractual terms of financial assets to identify whether they meet the SPPI test. 'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium / discount). The most significant elements of interest / profit within a financing arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Bank applies judgment and considers relevant factors

such as, but not limited to, the currency in which the financial asset is denominated, and the period for which the interest / profit rate is set. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with basic lending arrangement, the related financial asset is classified and measured at FVTPL.

8.2.3 Application to the Bank's financial assets

Debt based financial assets

Debt based financial assets held by the Bank include: Advances, lending to financial institutions, investment in Federal Government securities, corporate bonds and other private sukuks, cash and balances with treasury banks, balances with other banks, and other financial assets.

- a. These are measured at amortised cost if these assets meet both of the following conditions and are not designated as fair value through profit and loss (FVTPL):
- the assets are held within a business model whose objective is to hold assets to collect contractual cash flows; and
 - the contractual terms of the financial assets give rise on specified dates to cash flows that are solely payments of principal and interest / profit on the principal amount outstanding.

The Bank's business model for these financial assets can still be held to collect (HTC) even when sales of these financial assets occur. However, if more than an infrequent number of sales of significant value are made, the Bank assesses whether and how the sales are consistent with the HTC objective.

- b. Debt based financial assets are measured at fair value through other comprehensive income (FVOCI) only if these meet both of the following conditions and are not designated as FVTPL:
- the asset are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
 - the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest / profit on the principal amount outstanding.
- c. Debt based financial assets if these are held for trading purposes are classified as measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI or at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Equity instruments

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

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

Gains and losses on equity instruments at FVTPL are included in the 'Gain on sales of securities' line in the statement of profit and loss account.

8.2.4 Initial recognition and subsequent measurement

Financial assets and financial liabilities are recognised when the entity becomes party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade date, the date on which the Bank purchases or sells the asset. Other financial assets and liabilities like advances, lending to financial institutions, deposits etc. are recognised when funds are transferred to the customers' account or financial institutions. However, for cases, where funds are transferred on deferred payment basis, recognition is done when underlying asset is purchased.

a) Amortised cost (AC)

Financial assets and financial liabilities under amortised cost category are initially recognised at fair value adjusted for directly attributable transaction costs. These are subsequently measured at amortised cost. An expected credit loss allowance (ECL) is recognised for financial assets in the unconsolidated statement of profit and loss account. Interest income / profit / expense on these assets / liabilities are recognised in the unconsolidated statement of profit and loss account. On derecognition of these financial assets and liabilities, capital gain / loss will be recognised in the unconsolidated statement of profit and loss account.

b) Fair value through other comprehensive income (FVOCI)

Financial assets under FVOCI category are initially recognised at fair value adjusted for directly attributable transaction cost. These assets are subsequently measured at fair value with changes recorded in OCI. An expected credit loss allowance (ECL) is recognised for debt based financial assets in the unconsolidated statement of profit

and loss account. Interest / profit / dividend income on these assets are recognised in the unconsolidated statement of profit and loss account. On derecognition of debt based financial assets, capital gain / loss will be recognised in the unconsolidated statement of profit and loss account. For equity based financial assets classified as FVOCI, capital gain / loss is transferred from surplus / deficit to unappropriated profit.

c) Fair value through profit or loss (FVTPL)

Financial assets under FVTPL category are initially recognised at fair value. Transaction cost will be directly recorded in the unconsolidated statement of profit and loss account. These assets are subsequently measured at fair value with changes recorded in the unconsolidated statement of profit and loss account. Interest / dividend income on these assets are recognised in the unconsolidated statement of profit and loss account. On derecognition of these financial assets, capital gain / loss will be recognised in the unconsolidated statement of profit and loss account. An expected credit loss allowance (ECL) is not recognised for these financial assets.

8.2.5 Derecognition

Financial assets

The Bank derecognizes a financial asset when:

- the contractual rights to the cash flows from the financial asset expire;
- it transfers the rights to receive the contractual cash flows in a transaction in which either;
- substantially all of the risks and rewards of ownership of the financial asset are transferred; or
- the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

The Bank enters into transactions whereby it transfers assets recognised in its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets. In these cases, the transferred assets are not derecognised.

Financial liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled, or expired. The Bank also derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different, in which case a new financial liability based on the modified terms is recognised at fair value.

On derecognition of a financial liability, the difference between the carrying amount extinguished and the consideration paid (including any non-cash assets transferred or liabilities assumed) is recognised in the unconsolidated financial statement of profit and loss account.

8.2.6 Modification

The Bank sometimes renegotiates or otherwise modifies the contractual cash flows of financing to its customers. The Bank assesses whether the modified terms result in the financial asset being significantly modified and therefore derecognized. When the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset in accordance with IFRS 9, the Bank recalculates the gross carrying amount of the financial asset and shall recognize a modification gain or loss in unconsolidated statement of profit and loss account. The gross carrying amount of the financial asset is recalculated as the present value of the renegotiated or modified contractual cash flows that are discounted at the financial asset's original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets). Any costs or fees incurred adjust the carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.

Modification accounting is to be applied retrospectively, however, the same may be effective on loans modified on or after January 01, 2020.

8.3 Expected Credit Loss (ECL)

The Bank assesses on a forward-looking basis the expected credit losses ('ECL') associated with all advances and other debt financial assets not held at FVTPL, together with letter of credit, guarantees and unutilised financing commitments hereinafter referred to as "Financial Instruments". The Bank recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

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

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12mECL). The 12mECL is the portion of LTECLs that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Both LTECLs and 12mECLs are calculated at facility level.

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. The Bank considers an exposure to have significantly increased in credit risk when there is considerable deterioration in the internal rating grade for subject customer. The Bank also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer / facility to the watch list, or the account becoming forborne. Regardless of the change in credit grades, generally, the Bank considers that there has been a significant increase in credit risk when contractual payments are more than 60 days past due. When estimating ECLs on a collective basis for a group of similar assets, the Bank applies the similar principles for assessing whether there has been a significant increase in credit risk since initial recognition.

Based on the above process, the Bank groups its loans into Stage 1, Stage 2 and Stage 3, as described below:

- Stage 1: When financial instruments are first recognized, the Bank recognizes an allowance based on 12mECLs. Stage 1 financial instruments also include facilities where the credit risk has improved and these have been reclassified from Stage 2. The 12mECL is calculated as the portion of LTECLs that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. The Bank calculates the 12mECL allowance based on the expectation of a default occurring in the 12 months following the reporting date. These expected 12-month default probabilities are applied to a forecast Exposure At Default (EAD) and multiplied by the expected LGD and discounted by an approximation to the original Effective Interest Rate (EIR). This calculation is made for all the scenarios.
- Stage 2: When a financial instrument has shown a significant increase in credit risk since origination, the Bank records an allowance for the LTECLs. Stage 2 also includes facilities, where the credit risk has improved and the instrument has been reclassified from Stage 3. The mechanics are similar to those explained above, including the use of multiple scenarios, but PDs are applied over the lifetime of the instrument. The expected cash flows are discounted by an approximation to the original EIR.
- Stage 3: For financial instruments considered credit-impaired, the Bank recognizes the LTECLs for these instruments. The Bank uses a PD of 100% and LGD as computed for each portfolio or as prescribed by the SBP.

Undrawn financing commitments	When estimating LTECLs for undrawn financings commitments, the Bank estimates the expected portion of the financings commitment that will be drawn down over its expected life. The ECL is then based on the present value of the expected cash flows if the financings are drawn down, based on a probability-weighting of the three scenarios. For revolving facilities that include both a financing and an undrawn commitment, ECLs are calculated on un-drawn portion of the facility and presented within other liabilities.
Guarantee and letters of credit contracts	The Bank estimates ECLs based on the BASEL driven and internally developed credit conversion factor (CCF) for guarantee and letter of credit contracts respectively. The calculation is made using a probability weighting of the three scenarios. The ECLs related to guarantee and letter of credit contracts are recognized within other liabilities.

The calculation of ECLs

The Bank calculates ECLs based on three probability-weighted scenarios to measure the expected cash flows, discounted at an approximation to the EIR.

The mechanics of the ECL calculations are outlined below and the key elements are, as follows:

- PD** The Probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognized and is still in the portfolio. PD is estimated based on transitioning among credit states. Credit states are defined by rating classes and are based on the Bank's internal risk ratings (i.e. from 1 to 12). Through the yearly review of the non-consumer portfolio, the Bank has drawn a yearly transition matrix of ratings to compute a count-based PD over the one year horizon for the last 11 years. PDs for Non rated portfolios are calculated based on Days Past Due (DPD) bucket level for each segment separately. Where practical, they also build on information from External Rating Agencies. PDs are then adjusted for IFRS 9 ECL calculations to incorporate forward looking information.
- EAD** The Exposure at Default (EAD) is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and profit, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest / profit from missed payments. The maximum period for which the credit losses are determined is the contractual life of a financial instrument unless the Bank has a legal right to call it earlier. The Bank's product offering includes a variety of corporate and retail facilities, in which the Bank has the right to cancel and / or reduce the facilities with one day notice. However, in case of revolving facilities, the Bank does not limit its exposure to credit losses to the contractual notice period, but instead calculates ECL over a period that

reflects the Bank expectations of the customer behavior, its likelihood of default and the Bank future risk mitigation procedures, which could include reducing or cancelling the facilities.

LGD The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realization of any collateral. It is usually expressed as a percentage of the EAD.

The discount rate used to discount the ECLs is based on the effective interest rate that is expected to be charged over the expected period of exposure to the facilities. In the absence of computation of the effective interest rate (at reporting date), the Bank uses an approximation e.g. contractual rate (at reporting date).

Effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liabilities to the gross carrying amount of a financial asset or to the amortized cost of a financial liability.

To mitigate its credit risks on financial assets, the Bank seeks to use collateral, where possible. The Bank considers only those collaterals as eligible collaterals in the EAD calculation which have the following characteristics:

- History of legal certainty and enforceability
- History of enforceability and recovery

When estimating the ECLs, the Bank considers three scenarios (a base case, a best case, a worst case). Each of these is associated with different PDs.

The Bank only considers cash, liquid securities, and Government of Pakistan guarantees as eligible collaterals, while calculating EADs.

The credit exposures (in local currency) that have been guaranteed by the Government and Government Securities are exempted from the application of ECL calculation.

As per BPRD Circular No. 03 of 2022 dated July 05, 2022 and BPRD Circular Letter No. 16 of 2024 dated July 29, 2024, ECL of Stage 1 and Stage 2 is calculated as per IFRS 9, while ECL of Stage 3 has been calculated based on higher of either the Prudential Regulations or IFRS 9 at borrower / facility level for corporate / commercial / SME loan portfolios and at segment / product basis for retail portfolio.

Forward looking information

In its ECL models, the Bank relies on range of the following forward looking information as economic inputs, such as:

- GDP Growth
- Consumer Price Index
- Unemployment rate

Definition of default

The concept of "impairment" or "default" is critical to the implementation of IFRS 9 as it drives determination of risk parameters, i.e. PD, LGD and EAD.

As per BPRD Circular No. 03 of 2022 dated July 05, 2022 and BPRD Circular Letter No. 16 of 2024 dated July 29, 2024, ECL of Stage 1 and Stage 2 is calculated as per IFRS 9, while ECL of Stage 3 has been calculated based on higher of Prudential Regulations or IFRS 9 at borrower / facility level for corporate / commercial / SME loan portfolios and at segment / product basis for retail portfolio.

This implies that if one facility of a counterparty becomes 90+ DPD in repaying its contractual dues or as defined in PRs; all other facilities would deem to be classified as stage 3.

Write-offs

Advances are written off where there are no realistic prospects of recovery. The amounts so written off are a book entry and does not necessarily prejudice the Bank's right of recovery against the customers.

8.4 Non-current assets (or disposal groups) held-for-sale

Non-current assets (or disposal groups) are classified as assets held-for-sale if their carrying amount will be recovered principally through a sale transaction rather than continuing use and a sale is considered highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell.

An impairment loss is recognized for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell. A gain is recognized for any subsequent increases in fair value less costs to sell of an asset (or disposal group), but not in excess of any cumulative impairment loss previously recognized. A gain or loss not previously recognized by the date of the sale of the non-current asset (or disposal group) is recognized at the date of derecognition.

Non-current assets (including those that are part of a disposal group) are not depreciated or amortized while they are classified as held for sale. Non-current assets classified as held for sale and the assets of a disposal group classified as held for sale are presented separately from the other assets in the statement of financial position. The liabilities of a disposal group classified as held for sale are presented separately from other liabilities in the statement of financial position.

9. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (GROUP – CONSOLIDATED BASIS)

9.1 The Group and its operations

The "Group" Consist of:

Holding Company

- National Bank of Pakistan (the bank)

Subsidiary Companies

- CJSC Subsidiary Bank of NBP in Kazakhstan
- First National Bank Modaraba, Pakistan
- NBP Exchange Company Limited, Pakistan
- National Bank Modaraba Management Company Limited, Pakistan
- Taurus Securities Limited, Pakistan
- NBP Fund Management Limited Pakistan
- Cast-N-Link Products Limited

The subsidiary company of the Group, National Bank Modaraba Management Company Limited, Pakistan exercises control over First National Bank Modaraba, Pakistan as its management company and also has a direct economic interest in it.

The Group is principally engaged in commercial banking, modaraba management, brokerage, leasing , foreign currency remittances, asset management, exchange transactions and investment advisory asset.

9.2 Basis of Consolidation

- The consolidated financial statements include the financial statements of the bank (holding company) and its subsidiary companies together - "the Group".
- Subsidiary companies are fully consolidated from the date on which more than 50% of voting rights are transferred to the Group or power to control the company is established and excluded from consolidation from the date of disposal or when the control is lost.
- The assets, liabilities, income and expenses of subsidiary companies are consolidated on a line by line basis.
- Income and expenses of subsidiaries acquired during the year are included in the consolidated statement of the comprehensive income from the effective date of acquisition.
- Non-Controlling interest / (minority interest) in equity of the subsidiary companies are measured at fair value for all the subsidiaries acquired from period beginning on or after January 1, 2010 whereas minority interest of previously acquired subsidiaries are measured at the proportionate net assets of subsidiary companies attributable to interest which is not owned by holding company.

Material intra-group balances and transactions are eliminated.

9.3 Material Accounting Policy Information

The material accounting policies for preparation of consolidated financial statements are same as financial statements except for the following which is defined below:

9.4 Business combination

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit and loss account as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognised at their fair value.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition date amount of the identifiable assets acquired and the liabilities assumed. If, after reassessment, net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognised immediately in profit or loss as a bargain purchase gain.

Non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the Group's net assets in the event of liquidation, are measured at fair value at the date of the acquisition.

When a business combination is achieved in stages, the Group's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date (i.e. the date when the Bank obtains control) and the resulting gain or loss, if any, is recognized in profit or loss account.

9.5 Goodwill

Goodwill arising on an acquisition of a business is carried at cost as established at the date of acquisition of the subsidiary company.

For the purposes of impairment testing, goodwill is allocated to each of the Group's cash-generating units (or entities of cash-generating units) that is expected to benefit from the synergies of the combination.

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If

the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit on a pro-rata basis based on the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in profit and loss account. An impairment loss recognised for goodwill is not reversed in subsequent periods.

On disposal of the relevant cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

10.DISCLOSURE POLICY

The financial statements of the Bank are prepared in accordance with approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board and Islamic Financial Accounting Standards (IFASs) issued by the Institute of Chartered Accountants of Pakistan as are notified under the Companies Act, 2017, the provisions of and directives issued under the Companies Act, 2017 and the Banking Companies Ordinance, 1962 and directives issued by the State Bank of Pakistan (SBP) and Securities, Exchange Commission of Pakistan (SECP) and Pakistan Stock Exchange. Wherever the requirements of the Companies Act, 2017, the Banking Companies Ordinance, 1962 or directives issued by SBP or SECP differ with the requirements of IFRSs or IFASs, the requirements of the Companies Act, 2017, the Banking Companies Ordinance, 1962 or the requirements of the said directives shall prevail.

10.1 Quarterly & Half Yearly Financial Statements - Format of Accounts and Mode of Disclosure

State Bank of Pakistan through its BPRD Circular Letter No. 02 dated February 09, 2023 has amended the format of quarterly and half yearly financial statements of banks. Accordingly quarterly and half yearly financial statements are prepared on the revised format effective from accounting year starting from January 1, 2024.

10.2 Revised forms of Annual Financial Statements

The financial statements of the bank are prepared using the format of financial statements prescribed by State Bank of Pakistan. The State Bank has vide BPRD Circular No. 2 of 2023 dated February 09, 2023, issued the revised format for presentation of financial statements, which is applicable for annual financial statements prepared by banks for periods commencing from December 31, 2024.

11. ROLES AND RESPONSIBILITIES

The responsibility for preparation and presentation of financial statements in accordance with the accounting and reporting standards as applicable in Pakistan for financial reporting along with requirements of the Banking Companies Ordinance, 1962, the Companies Act, 2017, the directives issued by the SBP and the SECP, is primarily that of the Financial Control Group. The Financial Control Group's responsibilities include maintenance of adequate accounting records and such internal controls as the management and the Board determines is necessary to enable the preparation of the financial statements that are free from material misstatement. The Board is responsible for overseeing the strategic direction of the Bank and overseeing the financial reporting process.

The preparation of financial statements requires management to exercise judgement in making accounting estimates that are reasonable in the circumstances, as well as to select and apply appropriate accounting policies. In connection with preparation of financial statements, the accounting policies need to be understood and followed consistently by each Group to ensure accuracy and transparency in financial reporting so that it help stakeholders understand the bank's financial position and performance. For example, the Treasury Back office by applying appropriate accounting policies, can provide reliable numbers pertaining to investments, placements, borrowings, lending, receivable, payables etc and income earned and expenses thereon. Similarly, Business Groups in coordination with Operations Group, should apply proper accounting policies pertaining to loans and advances, deposits, borrowings, mark-up receivable, payables and income earned and expense thereon. Likewise, Logistics Group should apply proper accounting policies to ensure fixed assets and non-banking assets have been revalued at correct amount along with FCG to further ensure the depreciation method and rates are properly applied.

The responsibilities of the independent auditors, in a usual examination of financial statements, are explained in International Standard on Auditing 200 "Overall Objectives of the Independent Auditor and the conduct of an audit in accordance with International Standards on Auditing." While the auditors are responsible for forming and expressing their opinion on the financial statements, this does not relieve the management of its responsibilities.