

# Audit proposal letter to Republic Surety and Insurance Company, Inc.

January 5, 2018

Ms. Sally C. Ong Pac  
Treasurer

Pioneer House, 108 Paseo de Roxas  
Legaspi Village, Makati City 12290  
Philippines

Dear Ms. Ong-Pac:

1. This Engagement Letter, together with the attached General Terms and Conditions (collectively, this "Agreement"), confirms the terms and conditions upon which SyCip Gorres Velayo & Co. ("we" or "SGV") has been engaged to audit and report on the financial statements of Republic Surety and Insurance Company, Inc. (the "Company") for the year ended December 31, 2017. The services described in this Agreement may hereafter be referred to as either the "Audit Services" or the "Services."
2. Should conditions not now anticipated preclude us from completing our audit and issuing our auditor's report (the "Report") as contemplated by this Agreement, we will advise you and those charged with governance promptly and take such action as we deem appropriate.

## Audit Responsibilities and Limitations

3. We will conduct the audit in accordance with Philippine Standards on Auditing ("PSAs") as promulgated by the Auditing and Assurance Standards Council. Those standards require that we are independent and that we fulfill our other ethical responsibilities that are relevant to our audit.
4. The objectives of our audit 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 express an opinion on whether the financial statements present fairly, in all material respects, the financial position, financial performance and cash flows of Republic Surety and Insurance Company, Inc. in accordance with Philippine Financial Reporting Standards ("PFRS").

In addition:

- (a) in relation to our audit of the financial statements of the Company taken as a whole, we shall report on the supplementary information required under Revenue Regulations 15-2010 as prepared by management;
- (b) in relation to our audit of the financial statements taken as a whole, we shall report on the following supplementary schedules prepared by management as required under Securities Regulation Code (SRC) Rule 68, As Amended (2011) and SEC Financial Reporting Bulletin No. 001, dated February 16, 2012:
  - i. Supplementary schedules required by SRC Rule 68, Part II, Annex 68-E;
  - ii. Reconciliation of retained earnings available for dividend declaration;
  - iii. Tabular schedule of standards and interpretations as of reporting date;

5. 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.

6. 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.
7. There are inherent limitations in the audit process, including, for example, the use of judgment and selective testing of data and the possibility that collusion, forgery, intentional omissions, misrepresentations, or the override of internal control may preclude the detection of material error, fraud, or non-compliance with laws or regulations. Accordingly, there is some risk that a material misstatement of the financial statements may remain undetected. Also, an audit is not designed to detect fraud or error that is immaterial to the financial statements.
8. As part of our audit, we will also:
  - ▶ Consider, solely for the purpose of planning our audit and determining the nature, timing, and extent of our audit procedures, the Company's internal control over financial reporting. This consideration will not be sufficient to enable

us to express an opinion on the effectiveness of internal control or to identify all significant deficiencies.

- ▶ 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.
  - ▶ Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions in a manner that achieves fair presentation.
  - ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.
9. In accordance with the PSAs, we will communicate certain matters related to the conduct and results of the audit to those charged with governance. Such matters include:
- ▶ Our responsibility under the PSAs for forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance and that such an audit does not relieve manage-

ment and those charged with governance of their responsibilities.

- ▶ An overview of the planned scope and timing of the audit including the significant risks that we have identified and the type of work to be performed on the financial statements of the Company's components and the nature of the group engagement team's planned involvement in the work to be performed by component auditors on the financial information of significant components.
- ▶ Significant findings from the audit, which include: (1) our views about the significant qualitative aspects of the Company's accounting practices, including accounting policies, accounting estimates, and financial statement disclosures; (2) significant difficulties, if any, encountered during the audit; (3) uncorrected misstatements, other than those we believe are trivial; (4) disagreements with management, if any, whether or not satisfactorily resolved; and (5) other matters, if any, arising during the audit that are, in our professional judgment, significant and relevant to those charged with governance regarding the oversight of the financial reporting process, including significant matters in connection with the Company's related parties.
- ▶ Circumstances that affect the form and content of our Report including those highlighted in the next section.
- ▶ Written representations requested from management and significant matters, if any, arising from the audit that were discussed, or the subject of

correspondence, with management.

As part of our responsibility as an accredited external auditor of the Insurance Commission (IC), we shall report to the IC any of the following cases which may have been discovered based on PSAs, if the Company fails to disclose the same to the IC under its current reports:

- a. Any material findings involving fraud or error, as defined under Sections 3.3 and 3.4 of Circular 29-2009;
- b. Under-reserving of Incurred but Not Reported (IBNR) losses/policy reserves, the aggregate of which leads to capital deficiency impairment;
- c. Any findings to the effect that the consolidated assets of the Company, on a going concern basis, are no longer adequate to cover the total liabilities;
- d. Material internal control weaknesses which may lead to financial reporting problems;
- e. Termination or resignation as external auditor and stating the reason therefor;
- f. Discovery of a material breach of laws or IC rules and regulations;
- g. Findings on matters of corporate governance that may require urgent action by the IC.

In case there are no matters to report (e.g., fraud, dishonesty, breach of laws, etc.), we shall submit directly to IC within 15 calendar days after the closing of the audit engagement a notarized certification that there is none to report.

The management of the Company shall be informed of the adverse findings. Our report to the IC shall include pertinent explanation and/or corrective action.

The disclosure of the above information by us to the IC shall not be a ground for civil, criminal or disciplinary proceedings against us.

The management of the Company shall be given the opportunity to be present in the discussions between the IC and SGV regarding the audit findings, except in circumstances where SGV believes that the Company's management is involved in fraudulent conduct.

In accordance with Circular No. 2015-40, the Company's management shall provide us copies of the IC Reports of Examination, and SGV shall treat the contents of the IC Reports of Examination appropriately and confidentially.

It is, however, understood that our accountability as external auditor is based on matters within the normal coverage of an audit conducted in accordance with PSAs.

As part of our responsibility as an accredited external auditor of the Philippine Securities and Exchange Commission (the "Commission"), we shall report to the Commission any of the following cases which may have been discovered based on PSAs, if the Company fails to disclose the same to the Commission under its current reports:

- a. Any material findings involving fraud or error which reduces or increases the consolidated total assets, total liabilities or income of the Company by five percent (5%);

- b. Losses or potential losses the aggregate of which amounts to at least ten percent (10%) of the consolidated total assets of the Company;
- c. Any findings to the effect that the consolidated assets of the Company, on a going concern basis, are no longer adequate to cover the total claims of the creditors;
- d. Material internal control weaknesses which may lead to financial reporting problems.

The disclosure of the above information by us to the Commission shall not be a ground for civil, criminal or disciplinary proceedings against us.

10. In addition, we will communicate all relationships and other matters between SGV, other member firms of the global Ernst & Young network ("EY Firms") and the Company that, in our professional judgment, may reasonably be thought to bear on independence (including total fees charged during the period covered by the financial statements for audit and non-audit services provided by SGV and EY Firms to the Company and components controlled by the Company) and the related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level. Further, we will confirm that the engagement team and other SGV Persons as appropriate, SGV and, when applicable, EY Firms have complied with relevant ethical requirements regarding independence.

11. When we become aware of identified or suspected non-compliance with laws and regulations, including fraud,

we will bring such matters to the attention of the appropriate level of management. If we become aware of fraud involving management or fraud involving employees who have significant roles in internal control, we will report this matter directly to those charged with governance. We will communicate with those charged with governance matters involving non-compliance with laws and regulations, including fraud, that come to our attention unless they are clearly inconsequential. However, we will not communicate non-compliance matters, including fraud to the extent we are prohibited to do so by law or regulation.

12. We will communicate in writing significant deficiencies in internal control identified during the audit of the Company's financial statements.
13. We also may communicate our observations as to the potential for economies in, or improved controls over, the Company's operations.

#### **Circumstances that Affect the Form and Content of our Report**

14. From the matters we communicate with those charged with governance, we are required to determine those matters that were of most significance in our audit (i.e., Key Audit Matters). We describe those matters in our Report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our Report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

15. We have responsibilities for other information included in document(s) comprising an annual report as described in the Other Information section below. We are required to include an Other Information section in our Report that identifies the documents subject to our responsibilities and a description of our responsibilities to read and consider the other information in connection with our audit. We are also required, for documents that are available prior to our Report date, to include a statement that we have nothing to report or a statement describing any uncorrected material misstatements of the other information.

16. The final form and content of our Report will reflect the results of our final audit findings and conclusions. We will communicate to management and those charged with governance all circumstances affecting the final form and content of our Report.

#### Management's Responsibilities and Representations

21. Our audit will be conducted on the basis that management and where appropriate, those charged with governance, acknowledge and understand that they have responsibility:

- a. For the preparation and fair presentation of the financial statements in accordance with PFRS.

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.

- b. For such internal control as management determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.
- c. To provide us with: 1) access, on a timely basis, to all information of which management is aware that is relevant to the preparation of the financial statements and related disclosures, such as records, documentation and other matters; 2) additional information that we may request from management for the purpose of the audit; and 3) unrestricted access to persons within the Company from whom we determine it necessary to obtain audit evidence; Management's failure to provide us with the information referred to above or access to persons within the Company may cause us to delay our Report, modify our procedures, or even terminate our engagement.

22. Management is also responsible for adjusting the financial statements to correct misstatements identified by us and for affirming to us in its representation letter that they believe the effects of unrecorded misstatements are immaterial, individually and in aggregate, to the financial statements as a whole.

23. Management is responsible, with the oversight of those charged with governance, to determine that the Company's business activities

are conducted in accordance with laws and regulations. It is also the responsibility of management and those charged with governance to identify and address any non-compliance with applicable laws or regulations. Management is responsible for communicating to us on a timely basis, to the extent that management or those charged with governance are aware, all instances of identified or suspected non-compliance with laws and regulations (a) involving financial improprieties, (b) having a direct effect on the determination of material amounts and disclosures in the Company's financial statements and/or (c) that do not have a direct effect on amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operations of the Company's business, its ability to continue its business, or to avoid material penalties. Management must communicate the foregoing instances regardless of the source or the form in which the instances of identified or suspected non-compliance may have been discovered or communicated to them (including, without limitation, instances identified by "whistle-blowers," employees, former employees, analysts, regulators or others), and provide us full access to information and any internal investigations related to them. Such instances include manipulation of financial results by management or employees, misappropriation of assets by management or employees, intentional circumvention of internal controls, inappropriate influence on related party transactions by related parties, intentionally misleading SGV, or other identified or suspected non-compliance with law and regulation, including fraud that

could result in a misstatement of the financial statements or otherwise affect the financial reporting of the Company. If the Company limits the information otherwise available to us under this paragraph (based on the Company's claims of attorney/client privilege, work product doctrine, or otherwise), the Company will immediately inform us of the fact that certain information is being withheld from us. Any such withholding of information could be considered a restriction on the scope of the audit and may prevent us from opining on the Company's financial statements; alter the form of Report we may issue on such financial statements; or otherwise affect our ability to continue as the Company's independent auditors. We will disclose any such withholding of information to those charged with governance.

24. We will make specific inquiries of management about the representations contained in the financial statements. At the conclusion of the engagement, we will also obtain written representations from management about these matters, and that management has:

- ▶ Fulfilled its responsibility for the preparation and fair presentation of the financial statements in accordance with PFRS and that all transactions have been recorded and are reflected in the financial statements.
- ▶ Provided us with all relevant information and access as contemplated in this Agreement. The responses to those inquiries, the written representations, and the results of our procedures comprise evidence on which we will rely in forming an opinion on the financial statements.

25. Management and where appropriate, those charged with governance, agree that the internal auditors providing us direct assistance in the audit will be allowed to follow our instructions and the entity will not intervene in the work the internal auditors perform for us.

**Fees and Billings**

26. We estimate that our fees for the 2017 Audit Services is P450,000, exclusive of 10% out-of-pocket expenses (OPE) and 12% value-added tax (VAT). However, our actual fees may exceed this estimate based on changes to the business (e.g., nature of the business or change in business entities) or out-of-scope work. Payment is due upon receipt.

The Insurance Commission (IC) issued Circular Letter (CL) 2016-69 dated December 28, 2016 wherein the implementation requirements for Financial Reporting Framework (CL 2016-65), Valuation Standards for Insurance Policy Reserves (CL 2016-66 and CL 2016-67), and amended Risk-Based Capital (RBC2) Framework (IC 2016-68) took effect on January 1, 2017. The new valuation standards are to be accounted for as a change in accounting policy which would require the restatement of January 1, 2016 and December 31, 2016 balances. We estimate that our fees specific to this circular is P150,000, exclusive of 10% OPE and 12% VAT.

Audit fees	P450,000
IC circular fees	150,000
Total	P600,000

27. Our estimated pricing and schedule of performance are based upon, among other things, our preliminary review of the Company's records and the representations Company personnel have made to us and are dependent upon the Company's personnel providing a reasonable level of assistance. Should our assumptions with respect to these matters be incorrect or should the condition of records, degree of cooperation, results of our audit procedures, or other matters beyond our reasonable control require additional commitments by us beyond those upon which our estimates are based, we may adjust our fees and planned completion dates. Fees for any special audit-related projects, such as proposed business combinations or research and/or consultation on special business or financial issues, will be billed separately from the fees referred to above and will be the subject of other written agreements.

To the extent that SGV is engaged to perform Audit. Services for a subsequent fiscal year, the terms and conditions set forth in this Agreement shall apply to the performance of such Audit. Services, except as specifically modified, amended, or supplemented by the parties to this Agreement. Changes in the scope of the Audit Services and estimated fees for such services in subsequent fiscal years will be communicated in supplemental letters.

We appreciate the opportunity to be of assistance to the Company. If this Agreement accurately reflects the terms on which the Company has agreed to engage us, please sign below on behalf of the Company and return it to us at SGV & Co., 6760 Ayala Avenue, Makati City.

Yours very truly,



**Bernalette L. Ramos**  
Partner  
For and on behalf of  
SyCip Gorres Velayo & Co.

Agreed and accepted by:  
**Republic Surety and Insurance  
Company, Inc.**

By:



Ms. Sally C. Ong Pac

Date

cc: Ms. Ma. Cristina C. De Guzman

Attached: General terms and conditions