



# SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES

## Consolidated Interim Financial Statements

**September 30, 2018**

**(with the Independent Auditors' Report on Review of  
Consolidated Interim Financial Statements)**



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# INDEPENDENT AUDITORS' REPORT ON REVIEW OF CONSOLIDATED INTERIM FINANCIAL STATEMENTS

**To the Shareholders and Board of Directors  
Scotiabank Perú S.A.A.**

## Introduction

We have reviewed the accompanying consolidated statement of financial position of Scotiabank Perú S.A.A (a subsidiary of The Bank of Nova Scotia – BNS, an entity established in Canada) and subsidiaries as at September 30, 2018, the consolidated statement of income, consolidated statements of income and other comprehensive income, changes in equity and cash flows for the six-month period then ended, and notes, comprising significant accounting policies and other explanatory information ("the consolidated interim financial statements"). Management is responsible for the preparation and fair presentation of these consolidated interim financial statements in accordance with accounting standards established by Superintendencia de Banca, Seguros y Administradoras Privadas de Fondos de Pensiones – SBS (Banking, Insurance and Pension Plan Agency) for financial institutions in Peru. Our responsibility is to express a conclusion on these consolidated interim financial statements based on our review.

## Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review of interim financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying September 30, 2018 consolidated interim financial statements do not present fairly, in all material respects, the financial position, financial performance and cash flows of Scotiabank Perú S.A.A. and Subsidiaries in accordance with accounting standards established by the SBS for financial institutions in Peru.

Lima, Peru

December 18, 2018

Countersigned by:

Gloria Gernell O. (Partner)  
Peruvian Certified Public Accountant  
Registration number 01-27725

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Consolidated Interim Financial Statements

**September 30, 2018**

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## SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES

Consolidated Statement of Financial Position

As of September 30, 2018 and December 31, 2017

<i>In thousands of soles</i>	<i>Note</i>	<b>09.30.2018 (Unaudited)</b>	<b>12.31.2017 (Audited)</b>	<i>In thousands of soles</i>	<i>Note</i>	<b>09.30.2018 (Unaudited)</b>	<b>12.31.2017 (Audited)</b>
<b>Assets</b>				<b>Liabilities and equity</b>			
Cash and due from banks	5			Obligations and deposits in financial system entities	13		
Cash		1,167,395	1,052,396	Demand deposits		13,624,447	11,503,337
Deposits with Banco Central de Reserva del Peru		6,361,737	5,584,554	Savings deposits		9,062,662	9,283,817
Deposits with local and foreign banks		372,878	353,448	Time deposits		16,250,394	16,061,149
Clearing		80,632	125,306	Other obligations		791,243	1,014,124
Restricted cash and other cash		1,397,306	2,260,835			<b>39,728,746</b>	<b>37,862,427</b>
		<b>9,379,948</b>	<b>9,376,539</b>	Interbank funds		60,014	150,040
Interbank funds		94,021	406,108	Borrowings and debts	14	10,010,900	9,691,622
Investments at fair value through profit or loss and available-for-sale investments	6	3,118,148	5,403,722	Held-for-trading derivative instruments	8	47,820	68,011
Loan portfolio, net	7	46,783,334	42,631,366	Provisions and other liabilities	15	4,264,045	4,828,712
Held-for-trading derivative instruments	8	62,615	41,658	<b>Total liabilities</b>		<b>54,111,525</b>	<b>52,600,812</b>
Accounts receivable, net	9	1,089,093	1,280,651				
Investments in associates		71,247	70,475	<b>Equity</b>	16		
Goodwill	10	570,664	570,664	Share capital		6,122,946	5,634,538
Property, furniture, and equipment, net	11	409,683	406,229	Additional paid-in capital		394,463	394,463
Deferred tax	26	274,617	255,827	Legal reserve		1,082,742	960,640
Other assets, net	12	763,267	346,188	Unrealized earnings		(17,615)	23,591
				Retained earnings		922,576	1,175,383
<b>Total assets</b>		<b>62,616,637</b>	<b>60,789,427</b>	<b>Total equity</b>		<b>8,505,112</b>	<b>8,188,615</b>
Risks and contingent commitments	18	45,723,260	36,359,079	<b>Total liabilities and equity</b>		<b>62,616,637</b>	<b>60,789,427</b>
				Risks and contingent commitments	18	45,723,260	36,359,079

The accompanying notes on pages 6 to 72 are part of these consolidated interim financial statements.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Consolidated Statement of Income

For the nine-month periods ended September 30, 2018 and 2017

<i>In thousands of soles</i>	<i>Note</i>	<b>2018 (Unaudited)</b>	<b>2017 (Unaudited)</b>
Interest income	19	3,675,669	3,516,880
Interest expenses	20	(831,589)	(872,565)
<b>Gross financial income</b>		<b>2,844,080</b>	<b>2,644,315</b>
Provisions for credit losses, net of recoveries	7	(903,283)	(887,390)
<b>Net financial income</b>		<b>1,940,797</b>	<b>1,756,925</b>
Income from finance services, net	21	470,823	492,036
<b>Net financial income and finance service expenses</b>		<b>2,411,620</b>	<b>2,248,961</b>
Results from financial transactions	22	237,633	233,425
<b>Operating margin</b>		<b>2,649,253</b>	<b>2,482,386</b>
Administrative expenses	23	(1,258,892)	(1,190,320)
Depreciation of property, furniture and equipment	11	(45,392)	(46,209)
Amortization of intangible assets		(11,339)	(10,941)
<b>Net operating margin</b>		<b>1,333,630</b>	<b>1,234,916</b>
Net provisions for contingent loans, doubtful and other accounts receivable, realizable, repossessed assets, and other assets		(43,001)	(29,751)
<b>Operating results</b>		<b>1,290,629</b>	<b>1,205,165</b>
Other income, net	24	35,494	6,923
<b>Net profit before income tax</b>		<b>1,326,123</b>	<b>1,212,088</b>
Deferred tax income	26	18,790	13,160
Current tax income	25.C	(376,720)	(343,141)
<b>Net profit</b>		<b>968,193</b>	<b>882,107</b>

The accompanying notes on pages 6 to 72 are part of these consolidated interim financial statements.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Consolidated Statement of Income and Other Comprehensive Income  
For the nine-month periods ended September 30, 2018 and 2017

<i>In thousands of soles</i>	<b>2018 (Unaudited)</b>	<b>2017 (Unaudited)</b>
Net profit	968,193	882,107
Other comprehensive income:		
Unrealized loss, net of available-for-sale investments	(43,464)	(3,644)
Adjustment to other comprehensive income of associates	228	(16)
Cash flow hedges	2,030	-
Income tax effect	-	(16)
<b>Other comprehensive income, net of income tax</b>	<b>(41,206)</b>	<b>(3,676)</b>
<b>Total comprehensive income for the year</b>	<b>926,987</b>	<b>878,431</b>

*The accompanying notes on pages 6 to 72 are part of these consolidated interim financial statements.*

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Consolidated Statement of Changes in Equity

For the nine-month periods ended September 30, 2018 and 2017

	Number of shares (note 16.B)	Share capital (note 16.B)	Additional paid-in capital (note 16.C)	Legal reserve (note 16.D)	Unrealized earnings (note 16.F)	Retained earnings (note 16.E)	Total equity
<i>In thousands of soles</i>							
Balance as of December 31, 2016 (Audited)	481,666,886	4,816,667	394,463	843,801	24,136	1,130,647	7,209,714
Net profit	-	-	-	-	-	882,107	882,107
Other comprehensive income:							
Unrealized loss net on available-for-sale investments	-	-	-	-	(3,660)	-	(3,660)
Adjustment to other comprehensive income of associates	-	-	-	-	(16)	-	(16)
<b>Total comprehensive income</b>	-	-	-	-	<b>(3,676)</b>	<b>882,107</b>	<b>878,431</b>
Application to legal reserve	-	-	-	116,839	-	(116,839)	-
Dividend distribution	-	-	-	-	-	(233,677)	(233,677)
Capitalization of retained earnings	81,787,056	817,871	-	-	-	(817,871)	-
Other adjustments	-	-	-	-	-	17	17
<b>Balance as of September 30, 2017 (Unaudited)</b>	<b>563,453,942</b>	<b>5,634,538</b>	<b>394,463</b>	<b>960,640</b>	<b>20,460</b>	<b>844,384</b>	<b>7,854,485</b>
Balance as of December 31, 2017 (Audited)	563,453,942	5,634,538	394,463	960,640	23,591	1,175,383	8,188,615
Net profit	-	-	-	-	-	968,193	968,193
Other comprehensive income:							
Unrealized loss net on available-for-sale investments	-	-	-	-	(43,464)	-	(43,464)
Adjustment to other comprehensive income of associates	-	-	-	-	228	-	228
Cash flow hedges	-	-	-	-	2,030	-	2,030
<b>Total comprehensive income</b>	-	-	-	-	<b>(41,206)</b>	<b>968,193</b>	<b>926,987</b>
Application to legal reserve	-	-	-	122,102	-	(122,102)	-
Dividend distribution	-	-	-	-	-	(610,510)	(610,510)
Capitalization of retained earnings	48,840,838	488,408	-	-	-	(488,408)	-
Other adjustments	-	-	-	-	-	20	20
<b>Balance as of September 30, 2018 (Unaudited)</b>	<b>612,294,780</b>	<b>6,122,946</b>	<b>394,463</b>	<b>1,082,742</b>	<b>(17,615)</b>	<b>922,576</b>	<b>8,505,112</b>

The accompanying notes on pages 6 to 72 are part of these consolidated interim financial statements.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

## Consolidated Statement of Cash Flows

For the nine-month periods ended September 30, 2018 and 2017

<i>In thousands of soles</i>	<i>Note</i>	<b>2018 (Unaudited)</b>	<b>2017 (Unaudited)</b>
Cash flows from operating activities			
Net profit		968,193	882,107
<b>Adjustments to reconcile net profit to cash used in operating activities</b>			
Provision for doubtful loans, net of recoveries	<i>7.d</i>	903,283	887,390
Provision for realizable, repossessed and other assets, net		15,342	7,583
Provision for accounts receivable, net		11,186	11,108
Depreciation and amortization		56,332	57,150
Provision for fringe benefits		36,401	37,538
Provision for current and deferred income tax	<i>26 &amp; 25 C</i>	357,930	329,981
Provision for contingent loans and country risk, net of recoveries		10,213	2,968
Other provisions		1,592	2,427
Loss (gain) on sale of investment, property, furniture, and equipment		4,150	(257)
Gains on sale of realizable and repossessed assets		(5,742)	(3,300)
<b>Net changes in assets and liabilities</b>			
Loans		(5,077,419)	(3,790,177)
Investments at fair value through profit or loss:		435,193	165,215
Available-for-sale investments		1,805,566	(1,617,908)
Accounts receivable		163,847	(515,704)
Other assets		(413,908)	42,113
Non-subordinated financial liabilities		2,068,021	4,079,709
Accounts payable		(404,242)	728,431
Provisions and other liabilities		463,683	147,603
<b>Net results for the year after net changes in assets, liabilities and adjustments</b>		<b>1,399,621</b>	<b>1,453,977</b>
Income taxes paid		(181,909)	(165,602)
<b>Net cash and cash equivalents from operating activities</b>		<b>1,217,712</b>	<b>1,288,375</b>
Dividends received		5,079	5,606
Acquisition of property, furniture, and equipment	<i>11</i>	(56,317)	(67,290)
Acquisition of other financial assets		(4,412)	(6,249)
Sale of property, furniture, and equipment		90	1,037
<b>Net cash and cash equivalents used in investing activities</b>		<b>(55,560)</b>	<b>(66,896)</b>
Dividend paid		(610,510)	(233,677)
<b>Net cash and cash equivalents used in financing activities</b>		<b>(610,510)</b>	<b>(233,677)</b>
Net decrease in cash and cash equivalents, before the effect of exchange rate fluctuations		551,642	987,802
<b>Exchange rate fluctuations effect on cash and cash equivalents</b>		<b>4,485</b>	<b>2,281</b>
Net decrease in cash and cash equivalents		556,127	990,083
<b>Cash and cash equivalents at beginning of year</b>		<b>7,527,096</b>	<b>8,856,571</b>
<b>Cash and cash equivalents at end of year</b>		<b>8,083,223</b>	<b>9,846,655</b>

The accompanying notes on pages 6 to 72 are part of these consolidated interim financial statements.

## **SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

### **1. Reporting Entity**

#### **A. Background**

Scotiabank Perú S.A.A. (hereinafter the Bank) is a subsidiary of The Bank of Nova Scotia - BNS (a financial entity from Canada), which holds directly and indirectly 98.05% of the Bank's capital stock as of September 30, 2018 and December 31, 2017, respectively. The Bank of Nova Scotia owned 2.32% of the Bank's shares directly, and through NW Holdings Ltd. and Scotia Perú Holdings S.A. owns indirectly 55.32% and 40.41% of shares as of September 30, 2018 and December 31, 2017, respectively.

#### **B. Economic activity**

The Bank is a public corporation established on February 2, 1943 and is authorized to operate as a banking entity by Superintendencia de Banca, Seguros y Administradoras Privadas de Fondos de Pensiones (Banking, Insurance and Pension Plan Agency, hereinafter the SBS). The Bank's operations mainly comprise financial intermediation, characteristic of banking entities, which are governed by the SBS through the Ley General del Sistema Financiero y del Sistema de Seguros y Orgánica de la SBS, Law 26702 (hereinafter the Banking Law). This law establishes the requirements, rights, obligations, guarantees, restrictions, and other operating conditions to which every legal entity operating in the financial and insurance system is subject.

The Bank's registered office address is Av. Dionisio Derteano N° 102, San Isidro, Lima, Peru. As of September 30, 2018 Scotiabank Peru S.A.A. and Subsidiaries performed their activities through a national network of 363 branches (as of December 31, 2017, it had 360 national branches).

As of September 30, 2018 and December 31, 2017, the accompanying financial statements include the financial statements of the Bank and other companies of the consolidated group (hereinafter the Scotiabank Group), such as: CrediScotia Financiera S.A., (hereinafter the CrediScotia) engaged in intermediation operations for the micro-business and consumer sectors; Servicios, Cobranzas e Inversiones S.A.C., engaged in collections and domicile verification, among other activities; Scotia Sociedad Agente de Bolsa S.A. (hereinafter SAB), engaged in intermediation activities in the Peruvian securities market; Scotia Fondos Sociedad Administradora de Fondos S.A. (hereinafter SAF), engaged in mutual funds management; Scotia Sociedad Tituladora S.A., (hereinafter Tituladora), engaged in the management of trusts as well as special purpose entities called Fideicomiso CrediScotia-Dinero Electrónico, and, finally, the Fideicomiso sobre Bienes Inmueble – Depsa.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

Below are the main balances of the Bank and other companies mentioned in the previous paragraphs as of September 30, 2018 and December 31, 2017 indicating the Bank's shareholding percentages, as well as relevant information in this regards:

<i>In thousands of soles</i>	<b>Activity</b>	<b>Shareholding percentage</b>	<b>Assets</b>	<b>Liabilities</b>	<b>Equity</b>
<b>09.30.2018</b>					
Scotiabank Perú S.A.A.	Banking	-	59,592,134	51,040,196	8,551,938
CrediScotia Financiera S.A.	Financing	100.00	4,714,869	3,808,311	906,558
Servicios, Cobranzas e Inversiones S.A.C.	Collection services	100.00	132,400	62,828	69,572
Scotia Fondos Sociedad Administradora de Fondos S.A.	Administration of mutual funds	100.00	70,049	8,575	61,474
Scotia Sociedad Agente de Bolsa S.A.	Stock market broker	100.00	44,837	2,394	42,443
Scotia Sociedad Titulizadora S.A.	Securitization	100.00	4,307	196	4,111
Fideicomiso sobre Bienes Inmueble - Depsa	Special purpose entity	-	1,577	1,275	302
Fideicomiso CrediScotia-Dinero Electrónico	Special purpose entity	-	528	580	(52)
<b>12.31.2017</b>					
Scotiabank Perú S.A.A.	Banking	-	57,750,449	49,515,888	8,234,561
CrediScotia Financiera S.A.	Financing	100.00	4,528,148	3,695,368	832,780
Servicios, Cobranzas e Inversiones S.A.C.	Collection services	100.00	122,095	56,365	65,730
Scotia Fondos Sociedad Administradora de Fondos S.A.	Administration of mutual funds	100.00	54,524	3,261	51,263
Scotia Sociedad Agente de Bolsa S.A.	Stock market broker	100.00	43,846	899	42,947
Scotia Sociedad Titulizadora S.A.	Securitization	100.00	3,579	100	3,479
Fideicomiso sobre Bienes Inmueble - Depsa	Special purpose entity	-	1,746	1,270	476
Fideicomiso CrediScotia-Dinero Electrónico	Special purpose entity	-	520	560	(40)

**C. Approval of financial statements**

The consolidated interim financial statements as of September 30, 2018 were approved by the Bank's management on November 15, 2018. The consolidated financial statements as of December 31, 2017 were approved by the Annual General Meeting of Shareholders held on March 21, 2018.

**D. Subsidiary's acquisition**

On May 9, 2018, the Bank reached an agreement with Cencosud Peru to acquire a 51% controlling interest in Banco Cencosud S.A., which offers credit cards and consumer loans in Peru, for approximately US\$ 100 MM. The two companies will also enter into a 15-year partnership to manage the credit card business and provide additional products and services to customers. The amount of the consideration to be paid for the Bank might be adjusted depending on the value of equity of Banco Cencosud S.A. to the date on which the transaction becomes effective, subject to respective regulatory approvals.

## **SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

### **2. Basis for the Preparation of Consolidated Interim Financial Statements**

#### **A. Statement of compliance**

The accompanying consolidated interim financial statements have been prepared from the accounting records of the Scotiabank Group and are presented in accordance with current legal regulation and accounting principles authorized by the SBS and, in the absence of such applicable SBS standards, the International Financial Reporting Standards (IFRS), made official in Peru by the Peruvian Accounting Board (CNC) are applied. Such standards comprise the Standards and Interpretations issued or adopted by the International Accounting Standards Board (IASB), which include the International Financial Reporting Standards (IFRS), International Accounting Standards (IAS), and the Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC), or the former Standing Interpretations Committee (SIC), adopted by the IASB and made official by the CNC for their application in Peru.

#### **B. Basis of measurement**

The consolidated interim financial statements have been prepared in conformity with the historical cost principle, except for the following:

- Derivative instruments are measured at fair value.
- Financial instruments at fair value through profit or loss are measured at fair value.
- Available-for-sale financial assets are measured at fair value.

#### **C. Functional and presentation currency**

These consolidated interim financial statements are presented in soles (S/) in accordance with SBS standards, which is the Scotiabank Group's functional and presentation currency. The information presented in soles (S/) been rounded to the nearest thousand (S/ 000), except as otherwise indicated.

#### **D. Significant accounting estimates and criteria**

The preparation of the consolidated interim financial statements in conformity with accounting principles requires management to use certain accounting estimates and criteria. Estimates and criteria are evaluated continuously according to experience and include reasonable future assumptions for each circumstance. Since these are estimates, final results might differ; however, according to Management's opinion, the estimates and assumptions applied do not have significant risk as to produce a material adjustment to the balances of assets and liabilities in the short term.

The significant estimates related to the consolidated interim financial statements correspond to provision for doubtful loans, valuation of investments, estimation of useful life and the recoverable amount of property, furniture, and equipment, intangible assets, impairment of goodwill, provision for realizable assets, received as payment and repossessed assets, estimate of the deferred sales tax recovery, provision for income tax, and the fair value of derivative instruments. Accounting criteria is described in note 3.

## **SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

### **3. Accounting Principles and Practices**

The main accounting principles and practices applied to prepare the consolidated interim financial statements of the Scotiabank Group, which have been consistently applied in previous period, unless otherwise indicated, are the following:

#### **A. Basis of consolidation**

The consolidated interim financial statements include the financial statements of entities comprising the Scotiabank Group, described in note 1, after eliminating significant balances and transactions among the consolidated companies, and the profits and losses resulting from those transactions. All subsidiaries have been consolidated from their date of incorporation or acquisition.

Subsidiaries are all companies over which the Bank has control and is able to manage its financial and operating policies.

The accounting records of companies of the Scotiabank Group comply with the information requirements established by the SBS.

Financial statements of the Subsidiaries and Special Purpose entities have been included for consolidation purposes and represent 7.70% and 7.61%, respectively, of the total Bank's assets before eliminations as of September 30, 2018 and December 31, 2017. As of those dates, there is no non-controlling interests resulting from the consolidation process.

#### **B. Financial instruments**

A financial instrument is any contract that gives rise to both a financial asset in one entity and a financial liability or equity instrument in another.

Financial instruments are recognized on the date when they are originated and are classified as assets, liabilities or equity instruments according to the substance of the contract. Interest, gains and losses generated by a financial instrument, whether classified as an asset or liability, are recorded as income or expense. The payment to holders of financial instruments classified as equity is recorded directly in equity.

The Scotiabank Group classifies its financial instruments in one of the following categories defined by IAS 39: (i) financial assets and liabilities at fair value through profit or loss, (ii) loans and accounts receivable, (iii) available-for-sale investments, (iv) held-to-maturity investments, and (v) other financial liabilities. The Scotiabank Group determines the rating of financial instruments at initial recognition and on basis of instrument by instrument.

The classification of financial instruments at initial recognition depends on the purpose for which the financial instruments were acquired and their characteristics. All financial instruments are initially recognized at their fair value plus incremental costs directly attributable to the acquisition or issuance of the instrument, except in the case of financial assets or liabilities held at fair value through profit or loss.

Purchases or sales of financial assets requiring the provision of the assets within a time frame established according to regulations or market conventions (regular market terms) are recognized at the contracting date.

## **SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

### ***Derecognition of financial assets and liabilities***

#### ***i. Financial assets***

A financial asset (or when applicable, a part of a financial asset or a part of a group of similar financial assets) is derecognized when: (i) the contractual rights to the cash flows from the asset expire; or (ii) the Scotiabank Group transfers its rights to receive cash flows of assets or has assumed a contractual obligation to pay total cash flows immediately received from a third party subject to a pass through agreement; and (iii) the Scotiabank Group has substantially transferred all the risks and rewards of the asset or, if the Scotiabank Group has neither transferred nor retained all of the risks and rewards of the asset, but it has transferred their control.

#### ***ii. Financial liabilities***

A financial liability is derecognized when the payment obligation is discharged, canceled or expires. When an existent financial liability is replaced by other of the same borrower in terms significantly different, or terms are significantly modified, such replacement or modification is treated as a derecognition of the original liability and as a recognition of a new liability, recognizing the difference between both of them in the results for the period.

### ***Impairment of financial assets***

The Bank evaluates at the end of each year whether there is objective evidence that results in a conclusion that an asset or group of financial assets is impaired.

A financial asset or group of financial assets is impaired, if and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset ("loss event"), and if such loss event had an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be estimated reliably. The evidence of impairment can be an indication that a borrower or group of borrowers are experiencing significant financial difficulties, defaults or delays in payments of interest or principal, the probability that the company will enter bankruptcy, restructuring or other legal and financial reorganization in which it is shown that there is a significant decrease in expected future cash flows such as changes in circumstances or economic conditions related to non-compliance with payments.

### ***Financial instruments offsetting***

Financial assets and liabilities are offset and the net amount is presented in the consolidated statement of financial position, when, and only when: a current legal right to offset the amounts exists, and there is an intention either to settle them on a net basis or to realize the asset, and settle the liability simultaneously.

The financial assets and liabilities presented in the consolidated statement of financial position correspond to cash and due from banks, interbank funds, investments at fair value through profit or loss and available-for-sale investments, held-for-trading derivatives, loan portfolio, accounts receivable, other assets and liabilities in the consolidated statement of financial position, except as otherwise indicated in the note corresponding to assets or liabilities. Accounting policies on recognition and valuation of these items are disclosed in corresponding accounting policies described in this note.

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### **C. Financial derivative instruments**

The SBS provides authorizations per type of derivative instrument contract and underlying asset, and may comprise more than one type of contract and underlying asset. Authorization schemes, valuation guidelines and accounting treatment for derivative instruments that financial entities shall apply are established in SBS Resolution 1737-2006 *Regulation for Trading and Accounting of Derivative Products in Financial System Companies* and its amendments which include accounting criteria for held-for-trading, hedging and embedded derivative operations which conform to IAS 39 *Financial Instruments: Recognition and measurement*.

#### **Recognition and measurement**

Held-for-trading derivative instruments are initially recognized in the consolidated statement of financial position at fair value; subsequently, any change in the fair value of such derivative generates an asset or liability in the consolidated statement of financial position, as applicable, and will affect the results of the period.

In addition to their recording in the consolidated statement of financial position, derivative instruments described above are recorded in contingent accounts at their notional amounts translated at the spot exchange rate.

#### **Hedging**

A derivative financial instrument that seeks to achieve a financial hedge for a given risk is designated as for hedge purposes if, at its negotiation, it is foreseen that changes in fair value or cash flows are expected to be highly effective in offsetting the fair value or cash flow changes of the hedged item attributable to the hedged risk from inception, which must be documented when the financial derivative is negotiated and during the period that the hedge relation exists. A hedge is considered as highly effective if changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80 to 125 percent.

If the SBS considers the documentation to be insufficient or finds weaknesses in the methodologies applied, it may require the immediate termination of the hedge relationship and the recording of the derivative financial instrument as trading, consequently, with effect from that date, the variations in fair value will be recognized in the result of the period.

For cash flow hedges, the effective portion of gain or loss over the hedge instrument, net of its tax effect, is recognized directly in equity, in the caption "Unrealized earnings (losses)" as a cash flow hedge reserve. The ineffective portion of gain or loss of the hedging instrument is recognized in the consolidated statement of income. The amounts recorded in equity are transferred to the consolidated statement of income in the periods in which the hedged item is recorded in the consolidated statement of income or when a planned transaction occurs.

As of September 30, 2018 the Bank hold a derivative instruments classified as an accounting cash flow hedge with an underlying asset of US\$ 70MM related to the transaction mentioned in note, 1.D. As of December 31, 2017 Scotiabank Group not hold derivative instruments classified as hedge accounting.

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### **D. Investments**

The Scotiabank Group apply the recording and valuation criteria of investments established in SBS Resolution 7033-2012 *Regulations for Classification and Valuation of Investments of Financial System Companies*, which is in line with the classification and valuation criteria stated in IAS 39 *Financial Instruments: Recognition and Measurement*, except for investments in associates; which are not within the scope of IAS 39, as detailed below:

#### **i. Investments at fair value through profit or loss**

Debt securities and equity shares are classified as investments at fair value through profit or loss if they have been acquired principally for the purpose of selling in the near future, or they form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. These financial assets are initially recognized on trade date, when the Scotiabank Group enters into contractual arrangements with counterparties to purchase securities, and they are normally derecognized when sold.

Measurement is initially made at fair value without including transaction costs, which is recognized in the consolidated statement of income. Subsequently, fair values are re-measured, and fluctuations generated through profit or loss are recognized in the consolidated statement of income.

Interest income is recognized using the effective interest rate method. Dividends are recognized in the consolidated statement of income when the right to receive the payment has been established.

Investment instruments held by companies can be reclassified. Investment instruments at fair value through profit or loss cannot be reclassified except: (1) for equity shares with no market quote lacking of reliable fair value estimations or (2) investment instruments given in guarantee and transferred through a repurchase agreement representing a guaranteed loan shall be reclassified as available for sale. Once these transactions are concluded, instruments shall be reclassified at their initial category, transferring the unrealized earnings from equity to the consolidated statement of income. During the six month period ended in September 30, 2018 and during the year 2017, its investment instruments have not been reclassified between categories.

#### **ii. Available-for-sale investments**

Available-for-sale investments are all other investment instruments that are not classified as investments at fair value through profit or loss, held-to-maturity investments and investments in associates. Likewise, investment instruments will be included in this category when the SBS explicitly requires it.

Available-for-Sale Investments are initially recognized on the trade date and measured at fair value plus direct and incremental transaction costs. They are subsequently re-measured at fair value, and changes therein are recognized in equity in the 'unrealized earnings' account until the securities are either sold or impaired. When available-for-sale securities are sold, cumulative gains or losses previously recognized in equity are recognized in the consolidated statement of income.

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For debt securities at fair value, the amortized cost shall be remeasured applying the effective interest method, and based on the resulting amortized cost, gains and losses from the variation in the fair value shall be recognized.

If an available-for-sale security is impaired, the accumulated loss (measured as the difference between the asset's acquisition cost, net of any principal repayments and amortization, and its current fair value, less any impairment loss on that asset previously recognized in the consolidated statement of income and other comprehensive income) is removed from equity and recognized in the consolidated statement of income.

In the case of unquoted equity shares, the impairment loss shall be the difference between the carrying amount and the present value of estimated future cash flows, discounted using current market rates for similar assets.

SBS Resolution 7033-2012 details a standard methodology for the identification of impairment of instruments classified as available-for-sale investments, which considers two filters; the first one contains two conditions: i) significant decrease in the fair value up to under 50% of the cost or, ii) a decrease exceeding the 20% consecutively during the last twelve months; in the event of meeting any of these two conditions of the first filter, it will be necessary to evaluate if these conditions are justified at least concerning two of the qualitative aspects of the issuer indicated in the second filter of such resolution.

Gains or losses from foreign exchange differences related to instruments representing capital shall be recognized in equity in the 'unrealized earnings' account while those related to debt instruments shall be recognized as profit or loss of the period.

Interest income is recognized on available-for-sale securities using the effective interest rate method, calculated over the asset's expected life. Premiums and/or discounts originated on the investment purchase date are included in the calculation of its effective interest rates. Dividends are recognized in the consolidated statement of income when the right to receive the payment has been established.

### **iii. *Investments in associates***

The account includes equity shares acquired to participate with and/or have significant influence over companies and institutions. This category shall include the goodwill determined in the purchase of such investments. Investments in Associates are initially measured at fair value plus transactions costs directly attributable to their acquisition, and are subsequently measured applying the equity participation method, meaning; the carrying amount of the investment will be increased or decreased by proportional recognition of equity obtained as of measurement date.

When variations in the equity of associate are due to concepts other than the profit or loss of the year; these variations shall be accounted directly in the equity. Dividends are accounted reducing the investment carrying amount.

According to the SBS Resolution 7033-2012, when the investments in associates have suffered an impairment of their value, it will be necessary to follow guidelines of IAS 36 "Impairment of Assets". Impairment losses on investments

## **SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

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will be recognized in the consolidated statement of income.

During the nine month period ended in September 30, 2018 and during the year 2017, the Scotiabank Group has not recognized impairment losses on investment instruments.

### **E. Loans, classification and provision for doubtful loans**

Direct loans are recorded when fund disbursements are made in favor of clients. Indirect loans (contingent) are recorded when documents that support such credit facilities are issued and may become direct loans in the event of making a payment to third parties. Likewise, changes in loan payment conditions due to debtors' payment difficulties are considered as refinancing or restructuring.

Finance lease operations are accounted for using the financial method, recording the amount of the receivable installments as loans. Corresponding finance income is recorded on an accrual basis in conformity with the lease agreement terms. Initial direct costs are recognized immediately as expenses.

The Portfolio Risk Management's Debtor Classification Unit is responsible for conducting, the evaluation and rating of the loan portfolio on a permanent basis. Each debtor receives a credit risk rating according to the guidelines established by the SBS Resolution 11356-2008 and its amendments.

#### ***Loan portfolio classification***

The Bank and CrediScotia classify their loan portfolio in two groups: Wholesale Banking (corporate, large companies and medium companies) and Retail Banking (small business, micro business, revolving consumer, non-revolving consumer and mortgage loans). These classifications consider nature of the client (corporate, government or individual), the purpose of loan, and business size measured by revenues, indebtedness, among other qualitative and quantitative indicators.

#### ***Credit risk rating categories***

The categories of credit risk rating established by the SBS are as follows: Standard, Potential Problem, Substandard, Doubtful, and Loss, which are assigned according to credit history of the debtor as established in SBS Resolution 11356-2008 and amendments.

For the Wholesale Banking portfolio, the Bank and CrediScotia mainly consider the payment capacity of debtor, cash flow, level of compliance with obligations, rating designated by other companies in the financial system, financial position, and quality management. For Retail Banking portfolio, the rating is based mainly on the level of compliance with credit payments, which is reflected by number of delinquent days and their classification in other financial system entities if rating alignment is applicable. Retail Banking portfolio is classified through an automatic rating process. The Bank and CrediScotia have included in the automatic rating process, wholesale debtors loan portfolio with credits up to US\$ 100 thousand.

#### ***Provisions for doubtful loans***

According to current SBS regulations, the Bank and CrediScotia determine generic and specific provisions for loans. The generic provision is recorded in a preventive manner for standard risk direct loans, credit risk equivalent exposure of indirect loans, and additionally the procyclical component when the SBS orders its application. Specific provision is recorded for direct loans and credit risk equivalent exposure of indirect loans for which a specific risk, higher than standard, has been identified.

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The equivalent credit risk exposure of indirect loans is determined by multiplying indirect loans by the different types of Credit Conversion Factor (CCF), as follows:

Description	CCF (%)
(i) Confirmations of irrevocable letters of credit for up to one year, when the issuing bank is a first level entity from a foreign financial system.	20
(ii) Standby letters of credit that support obligations to do or not to do.	50
(iii) Issuances of guarantees, and those not included in the previous item, as well as banker's acceptance.	100
(iv) Approved loans not disbursed and unused credit lines.	-
(v) Others not considered above.	100

Provision requirements are determined by considering the risk rating of the debtor, if it is backed by collaterals or not, and depending on the type of collateral.

The Bank and CrediScotia apply the following percentages to determine provisions for the loan portfolio:

Risk category	%			
	No collateral	Preferred collateral	Preferred easily realizable collateral	Preferred readily realizable collateral
Standard				
Corporate loans	0.70	0.70	0.70	0.70
Large-business loans	0.70	0.70	0.70	0.70
Medium-business loans	1.00	1.00	1.00	1.00
Small-business loans	1.00	1.00	1.00	1.00
Micro-business loans	1.00	1.00	1.00	1.00
Consumer loans (*)	1.00	1.00	1.00	1.00
Mortgage loans	0.70	0.70	0.70	0.70
Potential problem	5.00	2.50	1.25	1.00
Substandard	25.00	12.50	6.25	1.00
Doubtful	60.00	30.00	15.00	1.00
Loss	100.00	60.00	30.00	1.00

(\*) Include revolving consumer loans and non-revolving consumer loans.

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### **Procyclical component**

The rates of procyclical component to calculate the provisions for direct loans and credit risk equivalent exposure of indirect loans for debtors classified in standard risk rating are as follows:

<b>Type of credit</b>	<b>Procyclical component %</b>
Corporate loans	0.40
Large-business loans	0.45
Medium-business loans	0.30
Small-business loans	0.50
Micro-business loans	0.50
Revolving consumer loans	1.50
Non-revolving consumer loans	1.00
Mortgage loans	0.40

For corporate, large-business and mortgage loans that have preferred readily realizable collateral, the procyclical component rate is 0.3%. For all other types of credit with preferred readily realizable collateral, the procyclical component rate is 0% for the portion covered by such collateral.

For consumer loans that have contracts with discount agreements from eligible payrolls, the procyclical component shall be 0.25%.

The SBS requires that financial system companies establish a debt overindebtedness risk management system that allow reducing the risk before and after the granting of a credit, conducting a permanent monitoring of the portfolio in order to identify debtors with overindebtedness including periodic evaluation of the control mechanisms used and corrective action or required improvements, as appropriate. Companies that do not comply with these SBS provisions shall, for provision purposes, calculate the credit risk equivalent exposure by applying a 20% factor to the unused amount of revolving credit lines for Micro-business, small-business and consumer loans. Regarding this exposure equivalent to credit risk, the rates of provisions determined in the *Regulation for Debtor Classification* shall apply.

Regarding this concern, the amount of revolving credit line used for the computation referred in previous paragraph shall correspond to the last approved amount communicated to client.

Additionally, those companies that do not comply with the SBS provisions must establish an additional generic provision of 1% on direct debt. This provision will be applicable to direct consumer debt (revolving and non-revolving) and/or Micro-business loans and/or small-business loans of the customers rated by the company as Standard, as applicable.

The SBS can activate or deactivate the application of the procyclical component whether the average annual percentage of the Gross Domestic Product (GDP) is above or below 5%, respectively.

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Likewise other conditions for activation or deactivation are set out in Appendix I of SBS Resolution 11356-2008. The application of the procyclical component was activated between December 2008 and August 2009, and between September 2010 and October 2014. From November 2014, it is deactivated.

SBS has established that during the deactivation of the procyclical component, financial institutions cannot, under any circumstances, generate profits caused by the reversals of such provisions, which should only be used to record specific mandatory provisions.

Provisions for direct loans are presented deducting balances from the corresponding asset (note 7), and provisions for indirect loans are presented as liabilities (note 15).

### **F. Securities trading transactions carried out by third parties**

Scotia Sociedad Agente de Bolsa S.A. conducts security trading transactions carried out on behalf of its clients (principals).

Transfer of funds made by clients for purchase/sale transactions in the stock market and over-the-counter market result in the consolidated statement of financial position items only if they comply with assets definition (accounts receivable) and liabilities definition (accounts payable); otherwise, such balances are presented more appropriately in memoranda accounts.

An account receivable or payable is only recognized when they have not yet been settled at their maturity or if SAB, due to any operating cause, does not have the funds transferred by principals, however, since it is a solvent entity, funds are covered by SAB in an amount equivalent to the acquisition of securities acquired through a loan that is regularized almost immediately.

Since SAB only manages funds from principals, in its capacity as trustor, cannot use these resources and there is a commitment to return them to the trustees; these resources do not belong to the entity and are accounted in memoranda accounts.

Unsettled transactions by Bolsa de Valores de Lima S.A. are recorded in memoranda accounts, until corresponding collection or payment.

### **G. Property, furniture and equipment**

The property, furniture, and equipment are recorded at the historical acquisition cost, less accumulated depreciation and impairment losses. Disbursements incurred after acquisition of property, furniture, and equipment are recognized as assets when probable future economic benefits associated with the asset are generated by the Scotiabank Group, and costs can be reliably measured.

Maintenance and repair expenses are charged to income in the period they are incurred. Work-in-progress and in-transit goods are recorded at acquisition cost. These goods are not depreciated until relevant assets are finished and/or received, and are in operative condition.

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Depreciation is determined based on the straight-line method in using the following estimated useful lives:

	<b>Years</b>
Property and premises	Between 30 and 10
Furniture, fixture, and IT equipment	Between 10 and 2
Vehicles	5

Cost and accumulated depreciation of assets disposed of or sold are eliminated from their respective accounts, and any resulting gain or loss is included to profit or loss in the year they are incurred.

### **H. Realizable assets, received as payment, repossessed assets**

Realizable assets include assets purchased specifically for granting financial leases which are accounted initially at their acquisition cost. Further, realizable assets not granted as financial leases, including recovered assets, are accounted at the lower of its cost or market value.

Realizable assets, received as payment, and repossessed assets (note 12) are regulated by SBS Resolution 1535-2005. This caption mainly includes property, plant, and equipment received as payment for doubtful loans, and are initially recorded at the lower of value determined by the court, arbitrator, recovery value, estimated market value or the value of unpaid debt amount.

According to current legislation, the treatment to record provisions for this type of assets is as follows:

- Realizable assets, received as payment and repossessed assets are initially recorded at cost and at the same time, a provision equivalent to 20% of the cost. If the net realizable value shown in the valuation report demonstrates that the asset is impaired by a percentage higher than 20%, then the required initial provision shall be recorded at an amount equivalent to the amount effectively impaired.
- For the provision of furniture and equipment is recorded monthly, from the first month of the awarding or recovery of assets, a monthly provision equivalent to 1/18 of the cost in books, less the aforementioned initial provision. Regarding assets that have not been sold or leased within a one-year term and that do not have the extension established in the Banking Act, the provision shall be completed up to 100% of the value upon repossession or recovery less the impairment provision, at the maturity of the corresponding year.
- A provision shall be recorded for real estate that has not been sold or leased within one year from its recovery or repossession. This provision shall be a uniform monthly provision over a term of three and a half years until there is a 100% provision of the net carrying amount in books obtained in the eighteenth or twelfth month, depending on if there is or is not an extension approved by the SBS, respectively.

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An impairment loss is recognized in the consolidated statement of income when the net realizable value is lower than net carrying amount; accordingly, the carrying amount will be reduced and the loss shall be recognized in the consolidated statement of income. In cases where the net realizable value is higher than the net carrying amount, the higher value shall not be recognized in the books.

Valuation reports of real estate may not be aged over a year.

### **I. Impairment of non-financial assets**

When there are events or circumstantial economic changes indicating that the value of a long-lived asset might not be recoverable. At each consolidated statement of financial position date, management reviews the carrying amount of these assets to determine if there is impairment. When the carrying amount of the asset exceeds its recoverable amount, it is recognized an impairment loss in the consolidated statement of income, by an amount equivalent to the excess in the carrying amount net of its tax effects. Recoverable amounts are estimated for each asset or, if it is not possible, for each cash-generating unit.

The recoverable amount of a long-lived asset or a cash-generating unit is the higher of the asset's fair value less costs to sell and its value in use.

Fair value less selling cost of a long-lived asset or cash-generating unit, is the amount resulting from an arm's length sale transaction, between knowledgeable parties, less corresponding selling costs. Value in use is the present value of the future cash flows expected to arise from an asset or a cash-generating unit.

For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows (cash-generating units) from continuing use that are largely independent of the cash inflows of other assets.

An impairment loss on goodwill is determined by assessing the recoverable amount for each cash-generating unit or group of cash-generating unit to which the goodwill relates.

### **J. Intangible assets**

Intangible assets are mainly related to the acquisition and development cost of computing software shown in other assets and are amortized using the straight-line method over an average period of 3 years. Likewise, they include depreciable costs coming from commercial activities of CrediScotia and are amortized during the effectiveness of the contract.

Costs related to the development or maintenance of computing software are recognized in profit or loss when they are incurred. However, costs that are directly related to a single and identifiable computing software controlled by Management and that will give future economic benefits higher than their cost in a period exceeding one year, are considered as an intangible asset. Direct costs related to the development of software include personnel costs of the development team and a fractional part of general expenses.

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### **K. Goodwill**

Goodwill is related to the higher value paid between the acquisition cost over the identifiable fair values of a subsidiary, an associate and as a result of the acquisition of the equity block from Citibank Perú S.A. (note 10).

Business acquisitions are accounted using the purchase accounting method. This means, recognizing identifiable assets of the acquired company at fair value. Any excess between the acquisition cost and the fair value of the identifiable net assets is recognized as goodwill.

When the acquisition agreement foresees adjustments to the price based on the compliance with some future assumptions, and at the moment of the initial accounting, its occurrence has not arisen or the value cannot be reliably estimated, this adjustment is not included in the acquisition cost. If, subsequently, such adjustment becomes likely and can be reliably estimated, the additional amount will be treated as an adjustment to the acquisition cost.

Goodwill owns an indefinite useful life and it is proved through impairment every year or more frequently, when there are events or circumstantial changes indicating that goodwill balance might not be recoverable.

### **L. Securities, bonds, and obligations issued**

This includes the liability for the issuance of redeemable subordinated bonds and corporate bonds; those are measured at their amortized cost using the effective interest method. Discounts granted or income generated during the bonds issuance is amortized during the maturity term of these instruments.

Interest is recognized in profit or loss when accrued.

### **M. Provisions and contingencies**

#### ***i. Provisions***

Provisions are recognized when the Scotiabank Group has a present obligation (legal or constructive), as a result of past events, and when it is probable that an outflow of resources will be required to settle the obligation, and it is possible to reliably estimate its amount. Provisions are reviewed and adjusted in each period to reflect the best estimates as of the date of the consolidated statement of financial position.

The provision for length of service legal compensation (CTS) is calculated according to current legislation, on the total employees' indemnities and should be paid, in May and November each year, through deposits in authorized financial entities as chosen by them. Calculation is made for the amount that should have to be paid as at the date of the consolidated statement of financial position and it is included in the Provision for fringe benefits account. It is presented in the consolidated statement of financial position under other liabilities.

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### **ii. Contingencies**

Contingent liabilities are not recognized in the consolidated interim financial statements. They are disclosed in the notes to the consolidated interim financial statements, unless the possibility of an outflow of economic resources is remote. Contingent assets are not recognized in the consolidated interim financial statements, and they are only disclosed when an inflow of economic benefits is probable.

### **N. Share capital**

Common shares are classified as equity. Preferred shares, if any, are recorded as other debt instruments; the difference between the redeemable amounts of preferred shares and their par value being recorded in the capital account. Dividends on preferred shares are accounted as liabilities and charged to income of the period. As of September 30, 2018 and December 31, 2017, the Scotiabank Group does not hold preferred shares outstanding.

### **O. Income and expense recognition**

Interest income and expense are recognized in income in the corresponding period on an accrual basis, depending on the term of the generating transactions and the interest rate agreed with the clients. Commissions for banking services are recognized as income when earned.

SBS Resolution 7036-2012 establishes that this income from commission of indirect loans shall be recognized on an accrual basis during the term of such indirect loans. Likewise, commissions and expenses for formalization of loans, as well as opening, study and evaluation of direct and indirect loans, are recognized as income based on the accrual within the term of the corresponding contracts.

When management considers that there are reasonable doubts about the collectability of the principal of a loan, the Bank and CrediScotia suspend the recognition of interest in income. Interest in suspense is accounted in memoranda accounts and recognized as earned when collected. When management considers that the financial position of the debtor has improved and that the doubt about the collectability of the principal has dissipated, the recording on accrual basis is restated.

Interest income includes the return on fixed-income investments and trading securities, as well as the recognition of discounts and premiums on financial instruments. Dividends are accounted for as income when declared.

Brokerage service fees for buying and selling securities on the stock market are recorded in the Finance Services Income account when these transactions have been performed through generation and acceptance of operation policies by clients.

Revenues from sales of securities and its cost are recognized when the seller has transferred all the risks and rewards of ownership to the buyer and it is probable that economic benefits associated to the transaction will flow to SAB; they are recorded in the entity 'other income, net' on the consolidated statement of income. Dividends are accounted for as income when declared.

Income from remunerations of funds managed by SAF, are estimated daily as an equity percentage of each of the funds.

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Income generated by fees from redemption of shares is recognized as income when such redemption is carried out.

Fees for trust management services are recognized in profit or loss of the period to the extent the service is rendered and accrued.

Other income and expenses of the Scotiabank Group are recognized as earned or incurred in the period when they are accrued.

### **P. Income tax**

Current income tax is determined based on the taxable income and recorded according to tax legislation applicable to the Bank and each company that are part of the Scotiabank Group independently (note 25).

Deferred income tax is accounted for using the liability method based on temporary differences derived from tax accounting of assets and liabilities, and their balances in the financial statements of each company of the Scotiabank Group on legislation and tax rates to be applied when the deferred tax asset is realized or the deferred tax liability is settled (note 26).

Deferred income tax assets and liabilities are recognized without considering the estimated time when the temporary differences will disappear. Deferred tax asset is only recognized if it is probable there would be future tax benefits, so that the deferred asset can be used.

### **Q. Employees' profit sharing**

The Scotiabank Group recognizes a liability and an expense for employees' profit sharing in the consolidated statement of income based on 5% of taxable base determined according to the current tax legislation.

### **R. Repurchase agreements**

The Bank applies SBS Resolution 5790-2014 which establishes that securities sold under repurchase agreements on a specific future date, are not derecognized from the consolidated statement of financial position since the Bank retains substantially all of the risks and rewards inherent to the property. In the same sense, securities purchased under repurchase agreements on a specific future date are not derecognized from the consolidated statement of financial position. The consideration paid, including the accrued interest, is recorded in the statement of financial position under other accounts receivable.

For securities sold under repurchase agreements, the Bank recognizes received cash and liability for the obligation to return such cash at maturity. Also, it will make the reclassification of securities subject to the operation in conformity with SBS provisions. Accounting records of returns will depend on the agreements between the parties. Difference between the final amount and initial amount will be recognized as expenses against liabilities, within the term of the operation applying the effective interest rate method.

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For securities purchased under repurchase agreements, the Bank recognizes delivered cash and an account receivable for the right to receive such cash at maturity. Also, it will record the securities that are object to the operation in accounts off balance. Accounting records of returns will depend on the agreements between the parties. Difference between the final amount and initial amount will be recognized as income against account receivables, within the term of the operation applying the effective interest rate method.

As of September 30, 2018 and December 31, 2017, the Bank conducts sold repurchase agreements of securities and currency (notes 5 and 15) and purchased under repurchase agreements of securities (note 9).

### S. Consolidated statement of cash flows

For presentation purposes of this consolidated interim financial statement, the balances of Cash and due from banks and Interbank funds, of the assets, as of September 30, 2018 and 2017, were considered as cash and cash equivalents except for the restricted cash and due from banks for compliance with foreign currency repurchase commitments with BCRP and reserve funds for compliance with contractual commitments with foreign financial entities (note 5.c).

### T. Trust funds

Assets and income from trust operations, where there is an obligation to return the assets to clients, and the Bank and Scotia Sociedad Titulizadora S.A. act as trustee, are not included in the consolidated interim financial statements since they belong to neither the Bank nor Scotia Sociedad Titulizadora S.A., and are accounted for in memoranda accounts for corresponding control, and commissions on those activities are included in Income from Finance Services (note 21).

### U. Foreign currency transactions and balances

Foreign currency transactions are those transactions carried out in a currency that is different from the Sol. Foreign currency transactions are translated into Sol using exchange rates established by the SBS reported at the dates of the transactions (note 4). Foreign exchange gains or losses resulting from the payment of such transactions and from the translation of monetary assets and liabilities stated in foreign currency at exchange rates ruling at period-end closing are recognized in the consolidated statement of income.

### V. New accounting pronouncements

#### i. ***New accounting pronouncements not early adopted***

The following new standards, amendments and interpretations have been issued or adapted by the International Accounting Standards Board - IASB, but are effective for annual periods beginning on or after January 1, 2018, and the Bank has not adopted them in preparing these consolidated interim financial statements. Those that might be relevant to Scotiabank Group are detailed below. Scotiabank Group do not plan to adopt these standards early.

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<b>New IFRS, amendments and interpretations</b>	<b>Effective date</b>
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IFRS 16: Leases.

For annual periods beginning on or after January 1, 2019. Earlier adoption is permitted for entities that apply IFRS 15 at or before the date of initial application of IFRS 16.

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## SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

<b>New IFRS, amendments and interpretations</b>	<b>Effective date</b>
IFRIC 23: Uncertainty over income tax treatments.	For annual periods beginning on or after January 1, 2019. Earlier adoption is permitted.
Sale or Contribution of assets between an investor and its associate or joint venture (Amendments to IFRS 10: Consolidated interim financial statements and IAS 28: Investments in Associates and Joint Ventures).	Effective date was indefinitely deferred.
Plan Amendment, Curtailment or Settlement – Amendments to IAS 19.	For annual periods beginning on or after January 1, 2019.
Annual improvement cycle of IFRS 2015 - 2017 (amendments to IFRS 3, IAS 12 and IAS 23).	For annual periods beginning on or after January 1, 2019.
Conceptual Framework for Financial Reporting.	For annual periods beginning on or after January 1, 2020.

### **ii. Resolutions and Standards issued by CNC and the Peruvian Securities Market Regulator concerning the approval and adoption of IFRS in Peru**

As of the date of the consolidated interim financial statements, the CNC issued:

- Resolution 002-2018-EF/30 on August 29, 2018 making official the 2018 version of the International Financial Reporting Standards, the amendment to IAS 19 Employee Benefits and Financial Information Conceptual Framework.
- Resolution 001-2018-EF/30 on April 27, 2018 making official the amendments to IFRS 9 *Financial Instruments*, IAS 28 *Investments in Associates and Joint Ventures* and the Annual Improvements to IFRS 2015-2017 Cycle.

As indicated in note 2.A, the standards and interpretations detailed above in i) and ii) will only be applicable to the Bank and CrediScotia in absence of applicable SBS regulations for situations not covered in the Accounting Manual. Management has not determined the effect on the preparation of its consolidated interim financial statements in case such standards were adopted by the SBS.

### **iii. SBS pronouncements**

- By means of SBS Resolution 2755-2018 dated July 16, 2018, the SBS issue SBS Infractions and Sanctions Regulation.
- By means of SBS Resolution 2610-2018 dated July 4, 2018, is modified the regulation for Classification and Valuation of Investments of Financial System Companies, which goes into effect in October 2018.

## SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

- By means of Official Letter 10250-2017-SBS, dated March 16, 2017, the SBS empowers financial entities to modify the contractual conditions of the different loan modalities of retail debtors that are located in state-of-emergency zones, provided that they meet the conditions established in said document.
- By means of SBS resolution 930-2017 dated March 1, 2017, the SBS extends the exceptional treatment for repossessed and recovered assets without the authorization of the SBS.

### 4. Foreign Currency Balances

Consolidated statement of financial position include balances of foreign currency transactions, mainly in U.S. dollars (US\$), which are recorded in soles (S/) at the exchange rate established by the SBS. As of September 30, 2018 and December 31, 2017, the exchange rate was US\$ 1 = S/ 3.30 and S/ 3.241, respectively.

Foreign currency transactions in the country and international trade transactions referred to the concepts authorized by Banco Central de Reserva del Perú (Central Bank), are channeled through an interbank foreign exchange market. As of September 30, 2018, buy and sell exchange rates used were US\$ 1 = S/ 3.298 and US\$ 1 = S/ 3.302, respectively (US\$ 1 = S/ 3.238 buy and US\$ 1 = S/ 3.245 sell, as of December 31, 2017).

Foreign currency balances stated in thousands of U.S. dollars and other currencies as of September 30, 2018 and December 31, 2017, are summarized as follows:

<i>In thousands of U.S. dollars</i>	09.30.2018			12.31.2017		
	US dollars	Other currencies	Total	US dollars	Other currencies	Total
<b>Assets</b>						
Cash and due from banks	2,406,895	8,571	2,415,466	2,479,019	9,197	2,488,216
Investments at fair value through profit or loss and available-for-sale investments	3,872	-	3,872	86,522	-	86,522
Loan portfolio, net	4,304,632	-	4,304,632	4,536,490	-	4,536,490
Held-for-trading derivative instruments	2,663	-	2,663	697	-	697
Accounts receivable, net	15,423	2	15,425	16,473	-	16,473
Other assets, net	38,417	5,533	43,950	9,622	1,560	11,182
	<b>6,771,902</b>	<b>14,106</b>	<b>6,786,008</b>	<b>7,128,823</b>	<b>10,757</b>	<b>7,139,580</b>
<b>Liabilities</b>						
Obligations and deposits and other obligations	4,400,489	24,643	4,425,132	4,295,566	26,642	4,322,208
Borrowings and debts	2,509,080	-	2,509,080	2,350,397	-	2,350,397
Held-for-trading derivative instruments	517	-	517	212	-	212
Other liabilities	140,395	14,002	154,397	36,302	3,340	39,642
	<b>7,050,481</b>	<b>38,645</b>	<b>7,089,126</b>	<b>6,682,477</b>	<b>29,982</b>	<b>6,712,459</b>
<b>Net (liability) asset position in the consolidated statement of financial position</b>	<b>(278,579)</b>	<b>(24,539)</b>	<b>(303,118)</b>	<b>446,346</b>	<b>(19,225)</b>	<b>427,121</b>
<b>Derivative instruments operations</b>	<b>197,924</b>	<b>23,233</b>	<b>221,157</b>	<b>(336,766)</b>	<b>18,035</b>	<b>(318,731)</b>

As of September 30, 2018 and 2017, the Scotiabank Group recorded gains on foreign exchange, net of various operations amounting to S/ 171,951 thousand and S/ 183,595 thousand, respectively in Results from financial transactions (note 22).

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

As of September 30, 2018, the Scotiabank Group has contingent operations in foreign currency amounting to US\$ 10,706,082 thousand equivalent to S/ 35,330,072 thousand (US\$ 8,105,607 thousand, equivalent to S/ 26,270,272 thousand as of December 31, 2017).

**5. Cash and Due from Banks**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Cash (a)	1,167,395	1,052,397
Banco Central de Reserva del Perú - BCRP (a)	6,361,737	5,584,554
Banks and other financial system companies of country(b)	53,044	51,238
Banks and other financial system companies of abroad (b)	319,834	302,210
Clearing	80,632	125,306
Restricted cash and due from banks (c)	1,396,636	2,260,534
Other cash and due from banks	670	300
	<b>9,379,948</b>	<b>9,376,539</b>

- (a) As of September 30, 2018, funds held in cash and deposits with BCRP include US\$ 1,304,753 thousand and S/ 903,595 thousand (US\$ 1,650,264 thousand and S/ 870,515 thousand as of December 31, 2017) destined to cover the legal cash reserves that the Bank and CrediScotia must maintain for deposits and obligations from third parties according to the limits established by current legislation. These funds are held at BCRP and in the own financial entities' vaults.

Cash reserves held at BCRP do not accrue interest, except for the foreign and local currency amount that exceeded the minimum legal cash reserve. As of September 30, 2018, the excess of minimum legal cash reserve in foreign currency accrues interest at annual rate of 0.54%. There was no excess of minimum legal cash reserve in local currency as of that date (as of December 31, 2017, excess of minimum legal cash reserve accrued interest at an annual effective rate of 0.37%, there was no minimum legal cash reserve in local currency). Interest accrued from the excess in foreign currency as of September 30, 2018 amounts to US\$ 4,705 thousand (S/ 215 thousand and US\$ 3,052 thousand as of September 30, 2017).

As of September 30, 2018, balance in BCRP include overnight operations of US\$ 578,300 thousand and S/ 506,000 thousand; such operations accrued interest at an annual nominal rate of 2.22% and 1.50%, respectively (overnight operations of US\$ 30,000 thousand and S/ 288,000 thousand as of December 31, 2017 at annual nominal rates of 1.41% and 2.00%, respectively).

- (b) Deposits in local and foreign banks mainly correspond, to balances in soles and in U.S. dollars, and lower amounts in other currencies, with free withdrawal option and accrue interest at market rates. As of September 30, 2018, deposits in foreign banks, included deposits held at The Bank of Nova Scotia of US\$ 4,297 thousand and Canadian dollars CAD 2,894 thousand (US\$ 10,900 thousand and Canadian dollars CAD 262 thousand as of December 31, 2017).

As of September 30, 2018 and December 31, 2017, the Scotiabank Group concentrate 77% and 83% of its deposits at foreign banks, in three financial entities, respectively.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

- (c) As of September 30, 2018, restricted cash and due from banks are comprised of:
- i) reserve funds for compliance with foreign currency repurchase commitments with BCRP for US\$ 419,492 thousand, (note 15.a) (US\$ 688,367 thousand as of December 31, 2017);
  - ii) reserve funds for compliance with contractual commitments with foreign financial entities for US\$ 1,946 thousand (US\$ 7,576 thousand as of December 31, 2017);
  - iii) guarantee funds for treasury transactions for US\$ 38 thousand and S/ 2 thousand (US\$ 43 thousand and S/ 2 thousand as of December 31, 2017);
  - iv) guarantee funds for lawsuits against the Bank for US\$ 263 thousand and S/ 952 thousand (US\$ 14 thousand and S/ 952 thousand as of December 31, 2017);
  - and v) other operational restrictions for US\$ 857 thousand and S/ 1,116 thousand (US\$ 851 thousand and S/ 1,087 thousand as of December 31, 2017).

As of September 30, 2018 and 2017, interest income from cash and due from banks amounted to S/ 32,674 thousand and S/ 23,015 thousand, respectively, and it is included as interest income in the consolidated statement of income (note 19).

## 6. Investments at Fair Value Through Profit or Loss and Available-For-Sale Investments

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
<b>Investments at fair value through profit or loss</b>		
Peruvian Treasury Bonds (a)	111,427	161,735
Mutual funds (b)	11,171	11,116
US Treasury Bonds (c)	9,861	-
Ordinary Bonds (d)	2,171	-
BCRP indexed certificates of deposit (e)	-	277,451
BCRP certificates of deposit (f)	-	119,521
	<b>134,630</b>	<b>569,823</b>
<b>Available-for-sale investments</b>		
BCRP certificates of deposit (f)	2,092,046	3,981,432
Peruvian Treasury Bonds (a)	883,296	846,521
Unlisted shares	7,436	5,390
Listed shares	722	538
Other shares, net	18	18
	<b>2,983,518</b>	<b>4,833,899</b>
<b>Total investments at fair value through profit or loss and available-for-sale investments</b>	<b>3,118,148</b>	<b>5,403,722</b>

- (a) Peruvian Treasury Bonds correspond to sovereign bonds issued in local currency by the Peruvian Ministry of Economy and Finance and represent internal public debt instruments of the Republic of Peru. As of September 30, 2018, these bonds accrue interest at annual rates ranging from 2.55% to 6.26% (from 1.05% to 6.26% annually as of December 31, 2017), with maturities between August 2020 and August 2037 (between February 2018 and February 2055 as of December 31, 2017).
- (b) As of September 30, 2018, SAF holds mutual fund investment shares in local and foreign currency for S/ 9,469 thousand and US\$ 516 thousand, respectively (S/ 9,343 thousand and US\$ 547 thousand as of December 31, 2017).
- (c) As a September, 2018 US Treasury Bonds are issued in foreign currency by the Government of the United States, these bonds accrue interest at an annual rate 3.0% with maturity in May 2028.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

- (d) They are ordinary bonds issued by the Fondo Mi Vivienda in local currency. As of September 30, 2018 these bonds accrue interest at an annual rate 5.18% with maturity in February 2024.
- (e) BCRP indexed certificates of deposit, recorded at fair value through profit or loss, are securities freely negotiable in foreign currency; they are acquired through BCRP public bids and traded in the Peruvian secondary market. These certificates are subject to a readjustment based on an average exchange rate variation between the date of issuance and the date of maturity.
- (f) BCRP certificates of deposit, are securities freely negotiable in local currency; they are acquired through BCRP public bids and traded in the Peruvian secondary market. As of September 30, 2018, these certificates accrue interest based on the BCRP reference rate which ranged from 2.43% to 3.38% annually (from 3.08% to 4.96% annually as of December 31, 2017), and have maturities between October 2018 and September 2019 (between January and December 2018 as of December 31, 2017). Likewise, as of September 30, 2018, the Bank holds certificates of negotiable deposits issued by BCRP which cannot be withdrawn since they warrant repurchase agreement for an amount of S/ 869,355 thousand (note 15) (S/ 1,182,657 thousand as of December 31, 2017).

As of September 30, 2018 and 2017, the accrued interest on investments administered by the Scotiabank Group amounted to S/ 100,824 thousand and S/ 101,937 thousand, respectively, and it is included as interest income item of the consolidated statement of income (note 19).

As of September 30, 2018 and December 31, 2017, investment at fair value through profit or loss and available-for-sale, have the following maturities:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Up to 3 months	1,118,709	2,115,458
From 3 to 12 months	984,508	2,313,532
Over 12 months	1,014,931	974,732
	<b>3,118,148</b>	<b>5,403,722</b>

**7. Loan Portfolio, Net**

- a) This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>		<b>12.31.2017</b>	
<b>Direct loans</b>				
Current loans	46,434,119	95%	42,480,703	95%
Refinanced loans	781,191	1%	602,918	1%
Restructured loans	521	-	-	-
Past due loans	867,792	2%	810,944	2%
Lawsuits loans	922,942	2%	743,456	2%
	<b>49,006,565</b>	<b>100%</b>	<b>44,638,021</b>	<b>100%</b>
<b>Plus (less)</b>				
Accrued interest on current loans	338,359		297,687	
Non-accrued interest	(28,340)		(33,342)	
Provision for loan losses	(2,533,250)		(2,271,000)	
	<b>46,783,334</b>		<b>42,631,366</b>	
<b>Contingent loans (note 18)</b>	<b>8,361,610</b>		<b>9,280,506</b>	

## SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

As of September 30, 2018 and December 31, 2017, 51% of the direct and indirect loan portfolio was concentrated in 628 and 622 clients, respectively.

The loan portfolio (direct and indirect) is mainly backed up with collaterals received from clients, mainly consisting of mortgages, industrial and merchant pledges, third-party letters of guarantees and securities. The value of these mortgages and pledges has been determined based on net realizable value in the market, less selling expenses according to SBS regulations.

Annual interest rates are regulated by the market and may be set at the discretion of the Bank and CrediScotia. As of September 30, 2018 and December 31, 2017 the annual average effective rates of main products fluctuated as follows:

	09.30.2018		12.31.2017	
	Local currency	Foreign currency	Local currency	Foreign currency
%				
Overdrafts (*)	55.00 – 85.00	30.00 – 55.00	55.00 – 85.00	30.00 – 55.00
Discounts and commercial loans	3.72 – 48.83	2.14 – 28.31	4.79 – 49.03	1.62 – 27.76
Consumer loans	14.76 – 45.03	9.04 – 27.11	14.87 – 45.69	9.68 – 27.11

(\*) For loans exceeding S/ 100 thousand and US\$ 100 thousand, respectively.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

- b) As of September 30, 2018 and December 31, 2017, according to current SBS regulations, the loan portfolio of the Bank and CrediScotia risk-based ratings are as follows:

<i>In thousands of soles</i>	<b>09.30.2018</b>				<b>12.31.2017</b>			
	<b>N° of debtors</b>	<b>Direct</b>	<b>Indirect</b>	<b>Total</b>	<b>N° of debtors</b>	<b>Direct</b>	<b>Indirect</b>	<b>Total</b>
<b>Risk category</b>								
Standard	1,016,113	44,960,962	8,121,528	53,082,490	1,012,590	40,828,371	9,122,355	49,950,726
With potential problems	44,820	1,041,883	198,230	1,240,113	45,991	1,195,085	132,835	1,327,920
Substandard	34,064	643,301	6,023	649,324	34,602	511,657	6,933	518,590
Doubtful	59,705	799,016	5,350	804,366	57,802	761,453	5,823	767,276
Loss	53,147	1,561,403	30,479	1,591,882	54,592	1,341,455	12,560	1,354,015
	<b>1,207,849</b>	<b>49,006,565</b>	<b>8,361,610</b>	<b>57,368,175</b>	<b>1,205,577</b>	<b>44,638,021</b>	<b>9,280,506</b>	<b>53,918,527</b>

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

- c) The movement of the provision for direct doubtful loans is as follows:

<i>In thousands of soles</i>	<b>Specific</b>	<b>Generic</b>	<b>Total</b>
Balance as of January 1, 2017	1,435,174	563,045	1,998,219
Additions debited to profit or loss	1,528,059	211,762	1,739,821
Recovery of provisions	(627,817)	(175,697)	(803,514)
Transfers of provisions and other	3,716	(3,108)	608
Write-offs and forgiveness	(745,864)	-	(745,864)
Foreign exchange differences	(11,914)	(3,888)	(15,802)
<b>Balance as of September 30, 2017</b>	<b>1,581,354</b>	<b>592,114</b>	<b>2,173,468</b>
Balance as of January 1, 2018	1,679,624	591,376	2,271,000
Additions debited to profit or loss	1,594,520	258,979	1,853,499
Recovery of provisions	(689,457)	(212,561)	(902,018)
Transfers of provisions and other	15,181	(13,479)	1,702
Write-offs and forgiveness	(701,185)	-	(701,185)
Foreign exchange differences	7,358	2,894	10,252
<b>Balance as of September 30, 2018</b>	<b>1,906,041</b>	<b>627,209</b>	<b>2,533,250</b>

- d) Provision for doubtful loans, net, as shown in the consolidated statement of income is as follows:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Provisions for doubtful loans of the period	1,853,499	1,739,821
Recovery of provisions	(902,018)	(803,514)
Recovery from write-offs portfolio	(48,198)	(48,917)
<b>Provisions for loans, net of recoveries</b>	<b>903,283</b>	<b>887,390</b>

The Bank and CrediScotia record regulatory provisions for loan portfolios according to the policy described in note 3.E. Also, these entities record discretionary provisions for doubtful loans included in the generic provision for loans. As of September 30, 2018 and December 31, 2017, discretionary provisions amount to S/ 102,532 thousand and S/ 97,955 thousand, respectively.

As of September 30, 2018, the provision for foreign exchange credit risk amounts to S/ 1,145 thousand (S/ 682 thousand as of December 31, 2017).

As indicated in note 3.E, from November 2014, the procyclical component for provision for doubtful loans calculation was deactivated. As of September 30, 2018 and December 31, 2017, the Bank and CrediScotia did not apply procyclical provisions for the registration of specific provisions. As of September 30, 2018 and December 31, 2017 a procyclical provisions balance amounting to S/ 41,513 thousand and S/ 54,264 thousand, respectively.

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

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- e) As of September 30, 2018 and December 31, 2017, direct loan portfolio had the following maturities:

<i>In thousands of soles</i>	09.30.2018			12.31.2017		
	Local currency	Foreign currency	Total	Local currency	Foreign currency	Total
Up to 1 month	2,589,597	2,189,366	4,778,963	1,675,291	3,019,501	4,694,792
From 1 to 3 months	3,891,260	3,075,213	6,966,473	2,507,608	3,320,693	5,828,301
From 3 to 6 months	4,687,142	1,923,026	6,610,168	3,551,360	1,607,604	5,158,964
From 6 to 12 months	4,224,736	1,268,279	5,493,015	4,378,191	1,193,552	5,571,743
Over 12 months	17,838,579	5,866,992	23,705,571	16,432,082	5,695,426	22,127,508
Overdue and lawsuit loans	1,298,376	492,358	1,790,734	1,111,982	442,418	1,554,400
Less, accrued interest	(263,342)	(75,017)	(338,359)	(236,442)	(61,245)	(297,687)
	<b>34,266,348</b>	<b>14,740,217</b>	<b>49,006,565</b>	<b>29,420,072</b>	<b>15,217,949</b>	<b>44,638,021</b>

**8. Held-For-Trading Derivative Instruments**

The Bank holds agreements of foreign currency forwards, cross currency swaps (CCS) and interest rate swaps (IRS). As of September 30, 2018 and December 31, 2017, the fair value of these trading financial instruments has generated accounts receivable and payable as described below:

<i>In thousands of soles</i>	09.30.2018		12.31.2017	
	Accounts receivable	Accounts payable	Accounts receivable	Accounts payable
Forwards	36,131	28,331	26,044	33,720
Interest Rate Swap - IRS	8,787	1,707	2,258	687
Cross Currency Swaps - CCS	17,697	17,782	13,356	33,604
	<b>62,615</b>	<b>47,820</b>	<b>41,658</b>	<b>68,011</b>

As of September 30, 2018 and 2017 these derivatives generated a net gains of S/ 35,834 thousand and a net losses of S/ 19,451 thousand, respectively (note 22).

**9. Accounts Receivable, Net**

This caption comprises the following:

<i>In thousands of soles</i>	09.30.2018	12.31.2017
<b>Financial instruments</b>		
Sale of investments (a)	238,733	469,830
Collection services	41,761	41,931
Payments on behalf of thirds parties, net	19,303	21,074
Commissions receivable	18,303	20,119
Advances to personnel	4,134	8,749
Sales of goods and services, trust, net	868	1,476
Accounts receivable from brokerage customers	241	423
Other accounts receivable, net	69,490	20,181
	<b>392,833</b>	<b>583,783</b>
<b>Non-financial instruments</b>		
Tax claims (b)	696,260	696,868
	<b>1,089,093</b>	<b>1,280,651</b>

## **SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

Notes to the Consolidated Interim Financial Statements

As of September 30, 2018 (unaudited), December 31, 2017 (audited) and September 30, 2017 (unaudited)

- (a) As of September 30, 2018 and December 31, 2017, corresponds to accounts receivable generated in the negotiation for the sale of Sovereign Bonds on the last day of the month, which are settled during the first days of the following month and are mainly related to: i) the sale of sovereign bonds for S/ 100,871 thousand and S/ 224,535 thousand; and ii) short selling of sovereign bonds in the short-term for S/ 137,862 thousand and S/ 245,295 thousand, respectively.
- (b) Tax claims comprise tax proceedings with the Tax Authority (SUNAT) that as of September 30, 2018 and December 31, 2017 include principally: i) S/ 230,094 thousand for payments made by the Bank under protest referred to the Temporary Tax on Net Assets (ITAN) of fiscal years 2005 and 2006 which are being challenged in the courts by the Bank as they are considered undue payments and shall be offset with the income tax and other tax credits and, ii) S/ 20,666 thousand for income tax paid in excess by CrediScotia for the years 2010, 2011, 2012 and 2013 (S/ 21,274 thousand as of December 31, 2017). In the opinion of Management and legal advisors of the Bank and CrediScotia, these amounts will be returned upon the favorable resolution of the case.

Also, this account receivable net of the pertinent provision for doubtful account includes tax claims amounting to S/ 433,815 thousand, as of September 30, 2018 and December 31, 2017, which are related to payments made under protest due to a resolution issued by the Tax Authority, which is being challenged in the Constitutional Court by the Bank. In the opinion of the Bank's Management and its legal advisors, these amounts will be returned to the Bank upon the favorable resolution of the case.

### **10. Goodwill**

It corresponds to the goodwill determined on the purchases of capital investments made by the Bank. As of September 30, 2018 and December 31, 2017, goodwill amounts to S/ 570,664 thousand which mainly includes: i) goodwill arising on the acquisition of 100% of the capital stock of Banco de Trabajo S.A., currently CrediScotia which amounts to S/ 278,818 thousand, ii) goodwill arising on the business acquisition of the commercial banking related to retail and consumer banking of Citibank del Perú which amounts to S/ 287,074 thousand, and iii) goodwill arising on the acquisition of Unibanca's shares which amounts to S/ 4,772 thousand.

According to SBS standards, such goodwill has been assessed by Management, concluding that there is no impairment as of September 30, 2018 and December 31, 2017.

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### 11. Property, Furniture, and Equipment, Net

This caption comprises the following:

<i>In thousands of soles</i>	Balance as of 01.01.2018	Additions	Disposals	Reclassification and/or adjustments	Balances as of 09.30.2018
<b>Cost</b>					
Land	132,075	-	(4,092)	-	127,983
Property and premises	761,241	13,706	(20,006)	11,375	766,316
Furniture, fixture, and IT equipment	424,831	15,990	(4,886)	4,547	440,482
Vehicles	3,593	159	(247)	-	3,505
Units in transit and replacing units	28,985	22,344	-	(5,957)	45,372
Work-in-progress	13,151	4,118	-	(13,214)	4,055
	<b>1,363,876</b>	<b>56,317</b>	<b>(29,231)</b>	<b>(3,249)</b>	<b>1,387,713</b>
<b>Accumulated depreciation</b>					
Property and premises	613,077	23,397	(19,934)	-	616,540
Furniture, fixture, and IT equipment	341,229	21,889	(4,810)	(18)	358,290
Vehicles	3,341	106	(247)	-	3,200
	<b>957,647</b>	<b>45,392</b>	<b>(24,991)</b>	<b>(18)</b>	<b>978,030</b>
	<b>406,229</b>				<b>409,683</b>

<i>In thousands of soles</i>	Balance as of 01.01.2017	Additions	Disposals	Reclassification and/or adjustments	Balances as of 09.30.2017
<b>Cost</b>					
Land	133,027	-	(394)	-	132,633
Property and premises	745,474	11,529	(3,389)	7,946	761,560
Furniture, fixture, and IT equipment	423,737	21,663	(28,445)	4,615	421,570
Vehicles	3,684	153	(331)	352	3,858
Units in transit and replacing units	13,964	21,556	-	(5,453)	30,067
Work-in-progress	2,832	12,389	-	(1,433)	13,788
	<b>1,322,718</b>	<b>67,290</b>	<b>(32,559)</b>	<b>6,027</b>	<b>1,363,476</b>
<b>Accumulated depreciation</b>					
Property and premises	580,066	23,287	(3,101)	6,613	606,865
Furniture, fixture, and IT equipment	339,442	22,848	(28,346)	1,557	335,501
Vehicles	3,829	74	(331)	-	3,572
	<b>923,337</b>	<b>46,209</b>	<b>(31,778)</b>	<b>8,170</b>	<b>945,938</b>
	<b>399,381</b>				<b>417,538</b>

According to current legislation, banks and finance companies in Peru cannot give as collateral the goods that are part of their property, furniture, and equipment, except for those acquired through the issuance of leasing bonds to carry out finance lease operations.

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**12. Other Assets, Net**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
<b>Financial instruments</b>		
Transactions in progress (a)	481,856	55,815
	<b>481,856</b>	<b>55,815</b>
<b>Non-financial instruments</b>		
Prepaid expenses (b)	137,195	116,779
Realizable and repossessed asset, net of accumulated depreciation and provision for impairment of S/ 148,971 thousand (S/ 141,241 thousand as of December 31, 2017)	87,755	87,683
Tax credit, net of income tax	25,189	51,297
Intangible assets, net of amortizations for S/ 270,652 thousand (S/ 260,296 thousand as of December 31, 2017)	23,330	26,672
Other	7,942	7,942
	<b>281,411</b>	<b>290,373</b>
	<b>763,267</b>	<b>346,188</b>

- (a) Transactions in progress are mainly those carried out during the last days of the month and are reclassified in the following month to their definitive respective accounts in the consolidated statement of financial position. These operations do not affect the results of the Scotiabank Group. As of September 30, 2018, transactions in progress mainly include treasury operations and invoices-in-transit amounting to S/ 467,555 thousand and S/ 4,552 thousand, respectively (S/ 30,762 thousand and S/ 4,382 thousand, respectively as of December 31, 2017).
- (b) As of September 30, 2018, prepaid expenses include mainly: i) deferred loan origination costs related to commissions paid to the external sales force for S/ 90,690 thousand (S/ 76,627 thousand as of December 31, 2017); ii) prepaid commissions of received borrowings for S/ 8,525 thousand (S/ 8,631 thousand as of December 31, 2017); iii) prepaid rent for S/ 4,978 thousand (S/ 4,396 thousand as of December 31, 2017); and iv) advertising and marketing services for S/ 2,331 thousand (S/ 2,757 thousand as of December 31, 2017), among other.

**13. Obligations and Deposits in Financial System Entities**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>		<b>12.31.2017</b>	
Corporate clients	18,870,035	48%	18,116,875	48%
Individuals	14,003,246	35%	14,082,733	37%
Non-profit organizations	4,762,174	12%	3,784,349	10%
Other	2,093,291	5%	1,878,470	5%
	<b>39,728,746</b>	<b>100%</b>	<b>37,862,427</b>	<b>100%</b>

Deposits and other obligations in U.S. dollars represent 37% of the total deposits as of September 30, 2018 and December 31, 2017, respectively. Deposits includes accounts pledged in favor of the Bank and CrediScotia for credit operations for S/ 574,248 thousand and US\$ 140,461 thousand as of September 30, 2018 (S/ 633,042 thousand and US\$ 196,062 thousand as of December 31, 2017).

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As of September 30, 2018 and December 31, 2017, the total deposits and obligations from individuals and non-profit legal entities for S/ 10,318,524 thousand and S/ 9,919,532 thousand, respectively, are covered by the Peruvian Deposit Insurance Fund (FSD), according to current legal regulations.

According to article 4 of SBS Resolution 0657-99, deposits covered by the FSD are the following:

- Registered deposits, under any modality, from individuals and private non-profit legal entities.
- Accrued interest on the above-mentioned deposits, as from their respective opening dates or their last renewal date; and
- Demand deposits corresponding to legal entities.

The maximum amount covered for each individual as of September 30, 2018, amounted to S/ 99 thousand (S/ 97 thousand as of December 31, 2017).

The Bank and CrediScotia freely establish deposits interest rates based on bid and demand, and the type of deposit. Effective rates as of September 30, 2018 and December 31, 2017, fluctuated as follows (annual effective rate):

	09.30.2018		12.31.2017	
	Local currency	Foreign currency	Local currency	Foreign currency
%				
Savings deposits	1.10 - 1.60	0.21 - 0.28	0.74 - 1.17	0.20 - 0.21
Time deposits	2.79 - 5.76	0.23 - 1.55	3.60 - 6.13	0.16 - 0.98
Severance payment deposits	3.14 - 6.22	1.13 - 1.83	3.06 - 6.49	1.14 - 2.12

As of September 30, 2018 and December 31, 2017, the scheduled maturity dates of the time deposits were as follows:

	09.30.2018			12.31.2017		
	Local currency	Foreign currency	Total	Local currency	Foreign currency	Total
<i>In thousands of soles</i>						
Up to 1 month	2,460,983	1,954,768	4,415,751	3,392,385	1,923,343	5,315,728
From 1 to 3 months	3,879,912	1,192,879	5,072,791	3,426,527	621,464	4,047,991
From 3 to 6 months	2,240,958	547,841	2,788,799	1,709,341	342,933	2,052,274
From 6 to 12 months	1,574,038	564,445	2,138,483	2,269,180	479,652	2,748,832
Over 12 months	1,149,307	566,958	1,716,265	1,197,115	554,367	1,751,482
	<b>11,305,198</b>	<b>4,826,891</b>	<b>16,132,089</b>	<b>11,994,548</b>	<b>3,921,759</b>	<b>15,916,307</b>
<b>Interest</b>	<b>107,201</b>	<b>11,104</b>	<b>118,305</b>	<b>138,258</b>	<b>6,584</b>	<b>144,842</b>
	<b>11,412,399</b>	<b>4,837,995</b>	<b>16,250,394</b>	<b>12,132,806</b>	<b>3,928,343</b>	<b>16,061,149</b>

Demand deposits, savings deposits and length of service legal compensation (CTS) have no contractual maturities.

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Notes to the Consolidated Interim Financial Statements

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**14. Borrowings and Debts**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Borrowings and financial obligations		
<b>Obligations in the country:</b>		
COFIDE (a)	1,063,421	1,174,000
<b>Ordinary loans from abroad</b>		
Related banks (b)	3,630,000	3,241,000
Other banks (c)	3,014,565	2,954,403
	<b>7,707,986</b>	<b>7,369,403</b>
Interest payable	29,765	19,257
	<b>7,737,751</b>	<b>7,388,660</b>
Securities and obligations (d)	2,273,149	2,302,962
	<b>10,010,900</b>	<b>9,691,622</b>

- (a) Corporación Financiera de Desarrollo S.A. (Finance Development Corporation – COFIDE) credit lines in the Bank and CrediScotia correspond to resources obtained for loans granting, mainly for mortgage financing programs of Fondo MiVivienda, which accrue a fixed interest rate adjusted to the VAC index.

As of September 30, 2018 and December 31, 2017, the Bank and CrediScotia maintain obligations with of COFIDE for S/ 576,206 thousand and S/ 613,070 thousand, respectively, which is guaranteed by mortgage loan portfolio, as detailed below:

<i>In thousands of</i>	<b>Currency</b>	<b>09.30.2018</b>		<b>12.31.2017</b>	
		<b>Net loans</b>	<b>Backed debt</b>	<b>Net loans</b>	<b>Backed debt</b>
<b>Detail</b>					
Mortgage loans-Fondo MiVivienda (*)	Sol	558,112	533,053	584,578	562,038
Mortgage loans-Fondo MiVivienda (*)	US dollars	14,912	13,077	17,772	15,746

(\*) The Bank and CrediScotia signed specific agreements on these loans which hold standard clauses of compliance on certain operating issues that, in the opinion of Management, are being met.

Likewise as of September 30, 2018 and December 31, 2017, another agreements for borrowing resources were agreed between the Bank and COFIDE for an amount of S/ 487,215 thousand and S/ 325,930 thousand, respectively, used to fund corporate and medium-business loans.

Additionally, CrediScotia held credit lines of COFIDE in local currency to be used as working capital on a short-term basis and were subject to specific agreements on the manner of using received funds, financial conditions that should be held and other administrative matters. As of December 31, 2017, obligations for this item amount to S/ 235,000 thousand and to date this debt was paid during March, 2018.

- (b) As of September 30, 2018 and December 31, 2017, ordinary loans with related banks include debts payable to Scotiabank Ltd. Bahamas amounting to US\$ 1,100,000 thousand, which accrue interest at annual rates ranging from 2.71% to 2.85% and have maturities between April 2018 and August 2020 (US\$ 1,000,000 thousand as of December 31, 2017, accruing interest at annual rates ranging from 1.88% to 2.66% and have maturities between July 2018 and December 2019).

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These borrowings do not have guarantees nor compliance covenants.

- (c) As of September 30, 2018, the Bank also includes borrowings and financial obligations negotiated with other foreign banks for US\$ 913,504 thousand (US\$ 911,571 thousand as of December 31, 2017) accruing annual interest at average rates that range from 2.46% to 3.35% (1.63% to 2.96% as of December 31, 2017). These transactions contain standard clauses of compliance with financial ratios and other administrative matters. In the opinion of Management, those clauses do not affect the Bank's operations and are being met.

As of September 30, 2018 and December 31, 2017, the scheduled maturity dates of borrowings from banks and other financial institutions were as follows:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Up to 1 month	630,465	589,520
From 1 to 3 months	451,978	1,737,548
From 3 to 6 months	1,025,470	536,521
From 6 to 12 months	1,167,231	1,209,222
Over 12 months	4,462,607	3,315,849
	<b>7,737,751</b>	<b>7,388,660</b>

- (d) The detail of securities and bonds is as follows:

<i>In thousands of soles</i>	<b>Annual interest</b>	<b>Maturity</b>	<b>09.30.2018</b>	<b>12.31.2017</b>
Issuance				
Redeemable subordinated bonds				
1st Issuance, single series (i)	4.50%	2027	1,320,000	1,296,400
1st Issuance A – 1st Program - SBP (ii)	7.34%	2025	535,560	535,560
1st Issuance A – 1st Program - CSF (iii)	7.41%	2027	130,000	130,000
			<b>1,985,560</b>	<b>1,961,960</b>
Corporate bonds (iv)				
1st Issuance A – 3rd Program	4.56%	2021	104,790	-
3rd Issuance B – 2nd Program	5.56%	2019	100,000	100,000
5th Issuance B – 2nd Program	6.19%	2018	38,500	38,500
3rd Issuance A – 2nd Program	6.78%	2018	-	75,920
9th Issuance C – 2nd Program	5.03%	2018	-	100,000
			<b>243,290</b>	<b>314,420</b>
Other instruments representing debt				
Negotiable certificates of deposits			7,011	10,373
			<b>7,011</b>	<b>10,373</b>
			<b>2,235,861</b>	<b>2,286,753</b>
Interest payable and obligations			37,288	16,209
			<b>2,273,149</b>	<b>2,302,962</b>

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- i. In December 2012, the Bank issued subordinated bonds for US\$ 400,000 thousand which under SBS Resolution 8093-2012, qualifies as tier 2 capital. These bonds mature on December 2027 and accrue interest at an annual fixed rate of 4.500% during the first ten years; from the eleventh year, they will accrue interest at a variable rate of 3-month LIBOR rate plus a spread of 3.856% to be paid each six months. After the eleventh year, all these bonds can be redeemed without penalties. This issuance was performed in the international market and contains certain standard clauses of compliance with financial ratios and other operating matters, which in the opinion of Management, do not affect the Bank's operations and are being met.
- ii. Through SBS Resolution 2315-2015, dated April 24, 2015, the SBS authorized the issuance of the Scotiabank Peru's First Subordinated Bonds Program up to an amount of US\$ 400,000 thousand or the equivalent in soles; these bonds qualifies as a tier 2 capital. In May 2015, the Bank issued 53,556 subordinated bonds in local currency with a face value of S/ 10,000 each and a term of 10 years from the date of issuance. These bonds accrue an annual interest rate of 7.34375% to be paid each semester. This issue was private and held in the local market.
- iii. In July 2012, CrediScotia issued subordinated bonds in local currency for S/ 130,000 thousand which under SBS Resolution 4873-2012, qualifies as tier 2 capital. These bonds accrue interest at an annual fixed rate of 7.41%, with maturity in July 2027 and have put option from the tenth year if the terms and conditions of such issuance are met. The proceeds were exclusively destined to credit operations financing.
- iv. They correspond to corporate bonds issued by the Bank for S/ 243,290 thousand, with terms that range from 1 to 3 years and accrued interest rates that range from 4.56% to 6.19%. The proceeds were exclusively destined to credit operations financing.

As of September 30, 2018 and 2017, interest expenses on borrowings and financial obligations of the Scotiabank Group amount to S/ 285,012 thousand and S/ 256,575 thousand, respectively (note 20).

Subordinated bonds issued by the Bank do not have specific collateral; however, they have a generic guarantee on the equity of those entities.

As of September 30, 2018 and December 31, 2017 the maturities of issued securities were as follows:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Up to 3 months	73,160	108,218
From 3 to 6 months	2,628	7,992
From 6 to 12 months	103,843	120,268
Over 12 months	2,093,518	2,066,484
	<b>2,273,149</b>	<b>2,302,962</b>

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**15. Provisions and Other Liabilities**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
<b>Accounts payable</b>		
Repurchase agreements (a)	2,589,653	3,457,532
Other accounts payable	310,205	421,799
Short selling	123,881	197,478
Dividends, vacations, remunerations and profit sharing payable	40,054	40,821
	<b>3,063,793</b>	<b>4,117,630</b>
<b>Provisions</b>		
Provision for contingent loans and country risk	101,682	92,105
Provisions for litigations and legal claims (b)	39,080	65,158
Provisions for various contingencies (c)	59,945	60,134
Other provisions (d)	166,095	125,788
	<b>366,802</b>	<b>343,185</b>
<b>Other liabilities</b>		
Transactions in progress (e)	785,747	315,112
Deferred income on portfolio sale and other	47,703	52,785
	<b>833,450</b>	<b>367,897</b>
	<b>4,264,045</b>	<b>4,828,712</b>

- (a) Corresponds to obligations for foreign currency purchase transactions and negotiable deposits issued by BCRP, both with commitments of repurchase made with BCRP (note 5.c and note 6.d). As of September 30, 2018, these operations accrued interest ranging from 2.95% to 4.17% (3.97% to 6.31% as of December 31, 2017). Likewise, as of September 30, 2018 the maturities of these operations fluctuate between January 2019 and October 2019 (between January 2018 and July 2019, as of December 31, 2017).
- (b) As of September 30, 2018 and December 31, 2017, the Scotiabank Group has legal actions underway, which are related to civil and labor claims, among others. These legal actions resulted from activities and operations performed during the normal course of the operations of each of the companies of the Scotiabank Group; it is not anticipated they will have a significant impact on operations or results.
- (c) As of September 30, 2018, this account mainly comprises reversals or recoveries of provisions recorded in prior years against equity accounts for S/ 29,570 thousand (S/ 29,196 thousand as of December 31, 2017) which, according to SBS Official Letter 23797-2003, should be reassigned to other deficits in Bank's asset accounts. Also, the balance as of September 30, 2018 includes provisions recorded against profit or loss for various contingencies for S/ 30,285 thousand (S/ 30,873 thousand as of December 31, 2017).
- (d) As of September 30, 2018, the balance of other provisions mainly include: i) provisions for personnel expenses for S/ 137,552 thousand (S/ 95,680 thousand as of December 31, 2017); ii) provisions for marketing campaigns of liability products for S/ 8,573 thousand (S/ 8,843 thousand as of December 31, 2017), and iii) provisions related to credit and debit card transactions for S/ 18,402 thousand (S/ 19,783 thousand as of December 31, 2017).

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- (e) Transactions in progress are mainly those carried out during the last days of the month and are reclassified in the following month to their definitive accounts of the consolidated statement of financial position. These operations do not affect the results of Scotiabank Group. As of September 30, 2018, liability transactions in progress include mainly: i) S/ 496,644 thousand related to Treasury operations (S/ 161,785 thousand as of December 31, 2017), ii) S/ 81,154 thousand related to credit card transactions (S/ 56,511 thousand as of December 31, 2017) and iii) S/ 147,610 thousand corresponding to client deposits in transit (S/ 35,130 thousand as of December 31, 2017).

## 16. Equity

### A. General

The regulatory capital of the Bank and CrediScotia is determined in accordance with the Banking Law and is used to calculate legal limits and restrictions applicable to financial institutions in Peru. As of September 30, 2018, the regulatory capital of both companies amount to S/ 8,321,290 thousand and S/ 912,791 thousand, respectively (S/ 8,091,670 thousand and S/ 770,151 thousand as of December 31, 2017, respectively).

As of September 30, 2018, credit risk weighted assets and contingent credits determined by the Bank and CrediScotia according to the legislation applicable to financial institutions amount to S/ 53,656,062 thousand and S/ 4,699,785 thousand, respectively (S/ 48,287,100 thousand and S/ 4,463,748 thousand, as of December 31, 2017, respectively).

Shareholders' Meeting, held on March 23, 2017, conferred authority to the Board of Directors to commit on capitalizations of year 2017 profits, with the purpose that these can be included in the calculation of the regulatory capital of the Bank. In that sense, in July 2017, the Board approved the commitment to capitalize the results for the year 2017 for a total of S/ 339,000 thousand. However, in the Shareholders' Meeting, held on March 21, 2018, the Shareholders approved to capitalize the results of the year 2017 for a total of S/ 488,408 thousand, which S/ 339,000 thousand was approved in the Board held on July 2017 and S/ 149,408 thousand for the capitalization of retained earnings of year 2017.

As of September 30, 2018 and December 31, 2017, the Banking Law established as a global limit that the regulatory capital shall be equal to or greater than 10% of the total risk weighted assets and contingent credits, which corresponds to the sum of: the amount of regulatory capital requirements for market risk multiplied by 10, plus the amount of the regulatory capital requirements for operational risk multiplied by 10, plus the risk weighted credit related assets and contingencies. As of September 30, 2018, the regulatory capital of the Bank and CrediScotia represents 14.46% and 17.96% respectively, of the minimum capital requirements per market, operational and credit risk (15.47% and 15.95% respectively as of December 31, 2017).

Likewise, by means of Resolution 2115-2009, the SBS approved the rules for the Additional Regulatory Net Capital for Operational Risk. As of September 30, 2018 and December 31, 2017, the Bank and CrediScotia have applied the alternative standard method for the calculation of the regulatory capital requirement for operational risk.

By means of SBS Resolution 1889-2018 and 1890-2018, SBS authorized the Bank and CrediScotia, respectively, to use the alternative standard method for the calculation of the regulatory capital requirement for operational risk. It also pointed out that the Bank and CrediScotia shall apply an additional regulatory capital requirement to the one

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calculated using the basic indicator method and the alternative standard method, which shall be equivalent to 25% of the difference between the requirements calculated using the basic indicator method and the alternative standard method, from April 2016 to March 2017; and, equivalent to 50% of the difference, from April 2017 to March 2018.

Finally, by means of SBS Resolution 8425-2011 and amendments, the SBS approved the methodology for the calculation of additional regulatory capital requirement, which establishes that this requirement shall be equal to the sum of the regulatory capital requirements, calculated for each of the following components: i) economic cycle, ii) concentration risk, iii) market risk concentration, iv) interest rate risk in the banking books, and v) other risks. As of September 30, 2018, additional regulatory capital of the Bank and CrediScotia amounted to S/ 1,217,868 thousand and S/ 148,484 thousand, respectively (S/ 1,126,962 thousand and S/ 138,527 thousand, as of December 31, 2017 respectively).

### B. Share capital

As of September 30, 2018, the Bank's capital stock authorized, subscribed and paid comprises 612,294,780 common shares (563,453,942 common shares as of December 31, 2017). All shares have voting rights and a par value of S/ 10.00 each. As of September 30, 2018 and December 31, 2017, the quotation value of common shares of the Bank was S/ 36.35 and S/ 32.30 per share, respectively.

Pursuant to the delegation conferred by the General Shareholders' meeting held on March 21, 2018 (note 16.a), the board approved the increase of capital stock arising from the capitalization or year 2017 retained earnings for S/ 488,408 thousand. As a result of both capitalizations, the capital stock increased to S/ 6,122,946 thousand and is represented by 612,294,780 common shares with a par value of S/ 10.00 each as of September 30, 2018.

Pursuant to the delegation conferred by the General Shareholders' meeting held on March 23, 2017, the board approved the increase of capital stock arising from the capitalization of year 2016, retained earnings for S/ 350,000 thousand and S/ 467,871 thousand. As a result of both capitalizations, the capital stock increase to S/ 5,634,539 thousand and is represented by 563,453,942 common share with a par value of S/ 10.00 each as of September 30, 2017.

Shares participation on the Bank's capital stock as of September 30, 2018 and December 31, 2017, is as follows:

Percentage of interest in capital	09.30.2018		12.31.2017	
	Number of shareholders	%	Number of shareholders	%
From 0.01 to 1	1,416	1.95	1,486	1.95
From 1.01 to 50	2	42.73	2	42.73
From 50.01 to 100	1	55.32	1	55.32
	<b>1,419</b>	<b>100.00</b>	<b>1,489</b>	<b>100.00</b>

Under the Banking Law, it is required that as of September 30, 2018, the capital stock reaches the minimum amount of S/ 27,072 thousand (S/ 26,686 thousand as of December 31, 2017), at constant value. This amount is annually updated at the closing date of every fiscal year, based on the wholesale price index (WPI), as published by the Instituto Nacional de Estadística e Informática (National Institute of Statistics).

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Notes to the Consolidated Interim Financial Statements

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### C. Additional paid-in capital

This additional paid-in capital balance comprises:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Issuance premium	393,159	393,159
Gain on treasury shares	1,304	1,304
	<b>394,463</b>	<b>394,463</b>

As of September 30, 2018 and December 31, 2017, the Bank holds 195 and 191 treasury shares, respectively.

### D. Legal reserve

In accordance with the Banking Law, the Bank is required to have a legal reserve of at least 35% of its capital stock. This reserve is created by an annual transfer of no less than 10% of after-tax profits, and supersedes the reserve referred to in the Companies Act. On the other hand, as stipulated in the Banking Law, the amount of this reserve may also be increased with contributions made by the shareholders for this purpose.

At the General Shareholders' Meeting, held on March 21, 2018 and March 23, 2017, it was decided to apply to legal reserve an amount of S/ 122,102 thousand and S/ 116,839 thousand corresponding to 10% of net profit for the year 2017 and 2016.

### E. Retained earnings

At General Shareholders' Meeting, held on March 21, 2018, the distribution of 2017 net profit for a total of S/ 1,221,021 thousand was approved, as follows:

- i. Cash dividends payment for S/ 610,510 thousand. Such payment was made in May 2018.
- ii. Allocate 10% of net profit, amounting to S/ 122,102 thousand to increase the legal reserve.
- iii. Remaining balance, amounting to S/ 488,408 thousand, will be held in 'retained earnings'.

At General Shareholders' Meeting, held on March 23, 2017, the distribution of 2016 net profit for a total of S/ 1,168,387 thousand was approved, as follows:

- i. Cash dividends payment for S/ 233,677 thousand. Such payment was made in May 2017.
- ii. Allocate 10% of net profit, amounting to S/ 116,839 thousand to increase the legal reserve.
- iii. Remaining balance, amounting to S/ 817,871 thousand, will be held in 'retained earnings'.

### F. Other comprehensive income

As of September 30, 2018 and December 31, 2017, it mainly includes unrealized results of available-for-sale investments, effects of cash flows hedges and share in other comprehensive income of associates, net of its deferred income tax effects.

## 17. Contingencies

Scotiabank Group has several pending court claims related to their ongoing activities. In the opinion of Management and their internal legal advisors, these claims will not result in liabilities additional to those recorded by Scotiabank Group; therefore, Management considers that no additional provision is necessary for these contingencies (note 15.b).

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### 18. Risks and Contingent Commitments

In the normal course of business, the Bank and CrediScotia perform contingent transactions under off-statement of financial position credit risk (contingent assets). These transactions expose the Bank and CrediScotia to additional credit risk, beyond the amounts presented in the consolidated statement of financial position. Credit risk for contingent transactions are accounted for in memoranda accounts of the consolidated statement of financial position and they relate to the probability that one of the participants of the respective contract does not comply with the agreed terms.

The related contracts consider the amounts that the Bank and CrediScotia would assume for credit losses in contingent transactions. The Bank and CrediScotia apply similar credit policies to evaluate and grant direct loans as indirect loans.

Many of the indirect loans are expected to expire without any withdraw required. The total committed amounts do not necessarily represent future cash outflows for the Bank and CrediScotia. Also, documentary credits, like export and import letters of credit and guarantees and stand-by letters of credit are conditional commitments issued by the Bank and CrediScotia to guarantee a customer obligation before a third party.

As of September 30, 2018 and December 31, 2017, the contingent accounts comprise the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>12.31.2017</b>
Contingent loans (note 7)		
Guarantees and stand-by letters of credit	7,687,725	8,588,934
Issued letters of credit	569,520	575,903
Due from bank acceptances	104,365	115,669
	<b>8,361,610</b>	<b>9,280,506</b>
Unused credit lines	26,593,108	21,130,602
Financial derivative instruments	10,768,542	5,947,971
	<b>45,723,260</b>	<b>36,359,079</b>

### 19. Interest Income

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Direct loan portfolio	3,534,241	3,386,223
Available-for-sale investments (note 6)	95,510	95,552
Cash and due from banks (note 5)	32,674	23,015
Investments at fair value through profit or loss (note 6)	5,314	6,385
Interbank funds	4,159	2,538
Other finance income	3,771	3,167
	<b>3,675,669</b>	<b>3,516,880</b>

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**20. Interest Expenses**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Deposits and obligations	468,333	462,284
Borrowings and debts (note 14)	285,012	256,575
Repurchase agreements	55,003	113,876
Commissions on borrowings and debts	14,979	29,072
Interbank funds	5,638	9,035
Deposits of financial entities	2,624	1,723
	<b>831,589</b>	<b>872,565</b>

**21. Income from Finance Services, Net**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
<b>Income</b>		
Income from commissions from collections services	156,814	143,474
Other fees and commissions from banking services	115,006	111,973
Income from deposit transactions, services and transfer fees	70,937	81,892
Income from portfolio recovery	51,650	53,124
Income from structuring and administration services	47,324	43,417
Income from remunerations of mutual funds and administration fees	37,493	30,162
Income from teleprocessing services	26,550	27,890
Income from commissions and brokerage services	4,776	4,096
Other various income	269,846	258,702
	<b>780,396</b>	<b>754,730</b>
<b>Expenses</b>		
Credit / debit card expenses	(90,053)	(81,575)
Deposit insurance fund premiums	(34,525)	(31,501)
Insurance services expenses	(4,153)	(4,710)
Other various expenses	(180,842)	(144,908)
	<b>(309,573)</b>	<b>(262,694)</b>
	<b>470,823</b>	<b>492,036</b>

**22. Results from Financial Transactions**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Gain on foreign exchange (note 4)	171,951	183,595
Gain (loss) on valuation of trading derivatives (note 8)	35,834	(19,451)
Gains on valuation of available-for-sale investments	20,115	41,548
Gain on associates	10,865	10,986
Dividends received from available-for-sale investments	1,351	1,281
(Loss) gain on valuation of investments at fair value through profit or loss	(3,239)	12,670
Others, net	756	2,796
	<b>237,633</b>	<b>233,425</b>

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**23. Administrative Expenses**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Personnel and board of directors expenses	663,521	645,469
Expenses for services received from third parties	531,912	491,028
Taxes and contributions	63,459	53,823
	<b>1,258,892</b>	<b>1,190,320</b>

**24. Other Income, Net**

This caption comprises the following:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Proceeds from sale of repossessed assets	6,787	7,427
Sale of non-financial services	6,400	9,017
Gain on sale of property, furniture, and equipment	4,556	3,924
Leasing of own goods	1,702	2,075
Reimbursements and recoveries	148	979
Other income (expenses), net	15,901	(16,499)
	<b>35,494</b>	<b>6,923</b>

**25. Tax Matters*****Income tax legislation***

- A. Scotiabank Group is subject to the Peruvian tax system. As of September 30, 2018 and 2017, corporate income tax is calculated on the basis of the net taxable income determined by the Scotiabank Group at a rate of 29.5%.

The income tax rate applicable to dividend distribution to 5%, in the case of profits generated and distributed since January 1, 2017.

It shall be presumed that the distribution of dividends or any other form of profit distribution correspond to the retained earnings or other items that could generate older taxable dividends.

- B. In accordance with current Peruvian tax legislation, non-domiciled individuals only pay taxes for its Peruvian source income. Thus, in general terms, revenues obtained by non-domiciled individuals from the services rendered in the country shall be subject to a 30% income tax on gross income, provided that no double tax treaties are applicable. On this concern, currently Peru has entered into double tax treaties with the Andean Community, Chile, Canada, Brazil, Portugal, Switzerland, Mexico and South Korea.

Concerning the technical assistance or digital services rendered by non-domiciled individuals to domiciled individuals, regardless of the place where the service is rendered, they shall be subject to a 15% and 30% income tax rate on gross income, respectively. Technical assistance will be subject to a 15% rate, provided that Income Tax Law requirements are met.

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**Income tax determination**

- C. Scotiabank Group computed its taxable base for the current three month period ended in September 30, 2018 and 2017, and determined income tax of S/ 376,720 thousand and S/ 343,141 thousand, respectively.

The current tax of the Scotiabank Group has been determined as of September 30, 2018 and 2017 as follows:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
Scotiabank Perú S.A.A.	288,585	273,355
CrediScotia Financiera S.A.	76,736	62,390
Scotia Fondos Sociedad Administradora de Fondos S.A.	8,245	1,109
Servicios, Cobranzas e Inversiones S.A.	2,838	6,040
Scotia Sociedad Titulizadora S.A.	285	104
Scotia Sociedad Agente de Bolsa S.A.	31	143
	<b>376,720</b>	<b>343,141</b>

Income tax expense comprises:

<i>In thousands of soles</i>	<b>09.30.2018</b>	<b>09.30.2017</b>
<b>Current income tax</b>		
Current year	384,273	367,338
Previous year adjustment	(7,553)	(24,197)
	<b>376,720</b>	<b>343,141</b>
<b>Deferred tax</b>		
Current year	(25,995)	(26,753)
Previous year adjustment	7,205	13,593
	<b>(18,790)</b>	<b>(13,160)</b>
<b>Net income tax expense</b>	<b>357,930</b>	<b>329,981</b>

The reconciliation of the tax rate and the effective tax rate is as follows:

<i>In thousands of soles</i>	<b>09.30.2018</b>		<b>09.30.2017</b>	
<b>Profit before taxes</b>	<b>1,326,123</b>	<b>100.00%</b>	<b>1,212,088</b>	<b>100.00%</b>
Income tax (theoretical)	391,206	29.50%	357,566	29.50%
Tax effect on additions and deductions				
Permanent differences	(32,928)	(2.48%)	(16,981)	(1.40%)
Previous year deferred tax adjustment	7,205	0.54%	13,593	1.12%
Previous year income tax adjustment	(7,553)	(0.57%)	(24,197)	(2.00%)
<b>Current and deferred income tax recorded as per effective rate</b>	<b>357,930</b>	<b>26.99%</b>	<b>329,981</b>	<b>27.22%</b>

**Income tax exemptions and exceptions**

- D. From year 2010, capital gains from the disposal or redemption of securities made in centralized trading mechanisms are subject to income tax. For this purpose, the value of securities has been established as computable cost at the closing of the taxable period 2009 (quotation value), acquisition cost, or increase in the equity value, as per procedure established in Supreme Decree 011-2010-EF.

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Accordingly, based on Law 30341 effective on January 1, 2016, the capital gain obtained from the disposal of shares and other securities representing shares are income tax exempt, provided that such disposal is negotiated through a centralized trading system supervised by the SMV, and in compliance with certain requirements established with such Law.

Legislative Decree 1262 became effective on January 1, 2017, extending the exemption until December 31, 2019 and included new assumptions that shall also be exempted: i) Debt securities, ii) Certificates of participation in mutual funds of investment in securities, iii) Certificates of participation in real estate investment (FIRBI, for its Spanish acronym) and certificates of participation in real estate trusts (FIBRA, for its Spanish acronym); and iv) negotiable invoices.

### ***Temporary tax on net assets***

- E. The Scotiabank Group is subject to Temporary Tax on Net Assets whose taxable base is composed of the prior period adjusted net asset value less depreciations, amortizations, legal cash reserve, and specific provisions for credit risk. The tax rate is 0.4% for years 2018 and 2017 and is applied to the amount of net assets exceeding S/ 1 million. It may be paid in cash or in nine consecutive monthly installments. The paid amount may be used as a credit against payments on account of income tax for taxable periods from March to December of the fiscal period for which the tax was paid until maturity date of each of the payments on account, and against the payment for regularization of income tax of the corresponding taxable period. In the event a remaining balance is not applied, its refund could be requested.

### ***Tax on financial transactions***

- F. Tax on Financial Transactions (ITF) for fiscal periods 2018 and 2017 was fixed at the rate of 0.005%. This tax is applied on charges and credits in bank accounts or movements of funds made through the financial system, unless the account is tax-exempt.

### ***Transfer pricing***

- G. For income tax purposes, transfer pricing for transactions carried out with economically-related parties, and with companies domiciled in territories with low or null taxation, shall be supported with documentation and information about the valuation methods used, and the criteria considered, for the pricing. Until fiscal year 2016, the formal obligations of Transfer Pricing were the presentation of a Local File Informative Affidavit, Master File Informative Affidavit, and Country by Country Informative Affidavit.

By means of Legislative Decree 1312, published on December 31, 2016 and effective January 1, 2017, the following formal obligations were established to replace the former ones: (i) presentation of a Local File (if accrued income exceeds 2,300 tax units (UIT, for its Spanish acronym)), (ii) presentation of a Master File (if accrued income of the group exceeds 20,000 UIT) and (iii) presentation of a Country-by-Country Reporting. The presentation of the Master File and the Country-by-country reporting will become obligatory in year 2018.

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According to Tax Authorities' resolution 014-2018-SUNAT, published on January 18, 2018, the Electronic Form 3560 was approved for presentation of the Local File, establishing the deadlines for its presentation and the content and format that should be therein included.

In April 2018, the Bank presented the Local Report for the year 2016, in accordance with the maturity schedule published by the Tax Authority. The Local Report for the year 2017 was presented in June 2018 according to the schedule of monthly tax obligations agreed for the tax period of May published by the Tax Authority.

The content and format of the Local File Informative Affidavit are stated in the Appendixes I, II, III and IV according to the Tax Authorities' resolution 014-2018-SUNAT.

In June 2018, by means of Tax Administration's 163-2018-SUNAT resolution, the rules for the presentation of the Master File and Country by Country Informative Affidavits (Electronic Forms 3561 and 3562) were approved, as well as the content and structure of each one of these obligations, and, the deadlines for submission of these statements during the month of November 2018. Finally, through Tax Administration's 246-2018-SUNAT resolution, the submission dates of the Country by Country Informative Affidavit were postponed for the month of March 2019, only for Peruvian subsidiaries of multinational groups whose parent companies are obliged to present the Country by Country Report in their countries of origin. In November 2018, the Bank presented the Master Report for 2017 according to the deadlines for submission published by the Tax Administration.

Likewise, the Decree 1312 also established that intra-group services with low added value shall not have a margin greater than 5% of their total costs and expenses. Concerning the services rendered between related parties, taxpayers must pass the benefit test and hold specific documentation and information under specific conditions for the deduction of these costs and expenses.

Legislative Decree 1116 established that Transfer Pricing Standards are not applicable for sales tax purposes.

### ***Tax assessment***

- H. The tax authorities has the right to audit and, if applicable, to modify the income tax calculated by the Scotiabank Group within the four years following the year of the tax return filing. The Scotiabank Group's income tax and sales tax returns for the years 2013 through 2017 are open for review by the Peruvian tax authorities. As of the date of this report, the Tax Authority is reviewing the Bank's non-domiciled income tax return for period 2013. It has also initiated the review of the income tax and transfer pricing for period 2013. **In the opinion of management and its legal advisors, these tax proceedings will not generate significant liabilities that may impact on the Bank's financial results.**

**SCOTIABANK PERÚ S.A.A. AND SUBSIDIARIES**

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	<b>Tax returns subject to audit</b>	<b>Tax returns being audited</b>
Scotiabank Perú S.A.A.	2014 through 2017	2013
CrediScotia Financiera S.A.	2013 through 2017	2011
Servicios, Cobranzas e Inversiones S.A.	2013 through 2017	2016
Scotia Fondos Sociedad Administradora de Fondos S.A.	2013 through 2017	-
Scotia Sociedad Agente de Bolsa S.A.	2014 through 2017	-
Scotia Sociedad Titulizadora S.A.	2013 through 2017	-
Trust Property on real estate – Depsa	2013 through 2017	-

Concerning tax returns for fiscal years 2006 through 2009, the Tax Authority issued various Tax Assessment and Fine Resolutions on the determination of corporate income tax for said years, which were challenged by the Bank. In relation to years 2006, 2007, 2008 and 2009, the Bank has filed an appeal which is pending resolution by the Tax Court.

Tax Authority has sent to the Bank, Tax Assessment and Fine Resolutions related to non-domiciled income tax for the periods 2008 and 2011 and related to Essalud contributions for the periods 2011 and 2012, which are being appealed. In the opinion of Management and its legal advisors, these tax proceedings will not generate significant liabilities that may impact on the Bank's financial results.

In January 2018, the Tax Authority issued Tax Assessment and Fine Resolutions on the determination of income tax for fiscal year 2010, which will be challenged by the Bank.

Due to the possibility of various interpretations of the current legal regulations by the tax authorities, it is not possible to determine, to date, whether a future tax audit will result or not in liabilities for the Bank; therefore, any major tax, surcharges, and sanctions that might arise from eventual tax audits would be applied to profit or loss of the period in which they are recognized. However, it is the opinion of Management and its legal advisors that, any possible additional settlement of taxes would not be significant for the financial statements of the Bank as of September 30, 2018 and December 31, 2017.

Concerning to CrediScotia, the Tax Authority has completed the audit processes for fiscal years 2008, 2009, 2010 and 2011, issuing Tax Assessment and Fine Resolutions on the determination of income tax for said years, which were challenged by CrediScotia. In relation to the results from the tax assessment of fiscal years 2008 and 2009, CrediScotia has filed an appeal for the received actions related to the Income Tax of those years.

***Tax regime applicable to sales tax***

- I. Legislative Decree 1347, published on January 7, 2017, established the possibility to reduce one percentage point in the Sales Tax as from July 1, 2017, provided that the goal of annual sales tax collection as of May 31, 2017 is reached, net of internal refunds of 7.2% of gross domestic product. In other words, if the aforementioned is met, the Sales Tax rate (including the municipal tax) will be reduced from 18% to 17%.

However, the estimated collection goal was not met at the end of the term, so the Sales Tax rate shall be held at 18%.

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**26. Deferred Taxes**

Deferred tax assets have been calculated applying the liability method per each entity (note 3.p). The consolidated deferred tax asset as of September 30, 2018 and 2017 is mainly composed of:

<i>In thousands of soles</i>	<b>Balances as of 01.01.17</b>	<b>(Debit) Credit equity</b>	<b>(Debit) credit profit or loss</b>	<b>Balances as of 09.30.17</b>	<b>Balances as of 01.01.18</b>	<b>(Debit) credit profit or loss</b>	<b>Balances as of 09.30.18</b>
Generic provision for direct/indirect loans	188,189	-	12,675	200,864	201,809	14,280	216,089
Provision for accounts receivable	25,331	-	1,476	26,807	26,641	3,403	30,044
Provision for vacations	13,667	-	(1,527)	12,140	16,586	3,324	19,910
Provision for repossessed assets	9,711	-	2,942	12,653	13,327	1,975	15,302
Provision for credit and debit card rewards	5,273	-	(4,576)	697	5,584	-	5,584
Finance lease operations, net	11,710	-	147	11,857	8,967	(7,967)	1,000
Investment in subsidiaries	940	-	-	940	940	-	940
Valuation of available-for-sale investments	4,884	(261)	(4,623)	-	-	-	-
Intangible assets	-	-	(3,705)	(3,705)	(5,297)	3,094	(2,203)
Other	(2,104)	245	10,351	8,492	(12,730)	681	(12,049)
<b>Deferred tax assets, net</b>	<b>257,601</b>	<b>(16)</b>	<b>13,160</b>	<b>270,745</b>	<b>255,827</b>	<b>18,790</b>	<b>274,617</b>

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### **27. Employees' Profit Sharing**

According to Legislative Decree 677, bank's employees are entitled to a profit-sharing plan computed at 5% of the net profit, similarly to employees of the companies of the Scotiabank Group. This profit sharing is considered as a deductible expense for income tax calculation purposes. As of September 30, 2018 and 2017 Scotiabank Group have determined legal employees' profit sharing for S/ 67,028 thousand and S/ 59,943 thousand, respectively, included under administrative expenses in the consolidated statement of income.

### **28. Trust Fund Activities**

Scotiabank Group offer structuring and administration services of trust operations and trust fees, and are in charge of the preparation of agreements related to these operations. Assets kept in trust are not included in the consolidated interim financial statements. The Scotiabank Group is responsible for the appropriate management of these trusts based on the limits established by applicable laws and the respective agreement. As of September 30, 2018, the allocated value of assets in trusts and trust fees amounts to S/ 4,695,314 thousand (S/ 3,270,509 thousand as of December 31, 2017).

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### 29. Related Party Transactions

As of September 30, 2018 and December 31, 2017, the consolidated interim financial statements include transactions with related parties, which, as established by IAS 24, comprise the parent company, related parties, associates, other related parties, and the Bank's directors and key management. All related party transactions are conducted in accordance with market conditions applicable to non-related third parties.

A. The balances of the Scotiabank Group's consolidated statement of financial position arising from related parties were as follows:

<i>In thousands of soles</i>	09.30.2018					12.31.2017				
	Parent company	Related parties (i)	Associates	Key personnel & directors	Total	Parent company	Related parties (i)	Associates	Key personnel & directors	Total
<b>Assets</b>										
Cash and due from banks	-	27,989	-	-	27,989	-	60,558	-	-	60,558
Loan portfolio, net	-	231,921	9,835	17,416	259,172	-	10,395	11,365	19,165	40,925
Held-for-trading derivative	-	32,345	-	-	32,345	-	21,314	-	-	21,314
Other assets, net	16	101,706	82,334	7	184,063	-	23,519	76,005	67	98,511
<b>Total assets</b>	<b>16</b>	<b>393,961</b>	<b>92,169</b>	<b>17,423</b>	<b>503,569</b>	<b>-</b>	<b>115,786</b>	<b>87,370</b>	<b>19,232</b>	<b>222,388</b>
<b>Liabilities</b>										
Deposits and obligations in financial system entities	1,166,592	587,805	13,218	15,884	1,783,499	783,293	502,779	16,295	26,015	1,328,382
Borrowings and financial obligations	253,390	3,640,023	-	-	3,893,413	253,630	3,248,913	-	-	3,502,543
Held-for-trading derivative	-	33,103	-	-	33,103	-	45,248	-	-	45,248
Provisions and other liabilities	20	103,796	4,245	12	108,073	-	24,661	5,678	255	30,594
<b>Total liabilities</b>	<b>1,420,002</b>	<b>4,364,727</b>	<b>17,463</b>	<b>15,896</b>	<b>5,818,088</b>	<b>1,036,923</b>	<b>3,821,601</b>	<b>21,973</b>	<b>26,270</b>	<b>4,906,767</b>
<b>Off-balance sheet accounts</b>										
Contingent loans	-	516,669	70,684	-	587,353	-	324,690	67,729	-	392,419
Financial derivative instruments	-	6,058,851	-	-	6,058,851	-	2,978,276	-	-	2,978,276

(i) Related parties include balances and transactions with 'other related parties' as defined by IAS 24.

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B. Consolidated of income statement arising from related party transactions were as follows:

<i>In thousands of soles</i>	09.30.2018					09.30.2017				
	Parent company	Related parties (i)	Associates	Key personnel & directors	Total	Parent company	Related parties (i)	Associates	Key personnel & directors	Total
Interest income		5,855	337	905	7,097		3,851	143	903	4,897
Interest expenses	(15,090)	(95,829)	(196)	(318)	(111,433)	(15,051)	(58,789)	(2,009)	(268)	(76,117)
	<b>(15,090)</b>	<b>(89,974)</b>	<b>141</b>	<b>587</b>	<b>(104,336)</b>	<b>(15,051)</b>	<b>(54,938)</b>	<b>(1,866)</b>	<b>635</b>	<b>(71,220)</b>
Income from finance services	18	2,624	506	147	3,295	17	1,882	537	131	2,567
Expenses on finance services	-	(2,753)	(11,137)	(22)	(13,912)	-	(1,439)	(11,985)	(12)	(13,436)
	<b>18</b>	<b>(129)</b>	<b>(10,631)</b>	<b>125</b>	<b>(10,617)</b>	<b>17</b>	<b>443</b>	<b>(11,448)</b>	<b>119</b>	<b>(10,869)</b>
Net results from financial transactions	-	(18,970)	10,865	-	(8,105)	-	(4,177)	10,986	-	6,809
Administrative expenses (ii)	-	(4,355)	(1,506)	(66)	(5,927)	-	(2,125)	(2,721)	(26)	(4,872)
Other income, net	-	(7)	-	(1)	(8)	-	-	(2)	-	(2)
<b>Net profit</b>	<b>(15,072)</b>	<b>(113,435)</b>	<b>(1,131)</b>	<b>645</b>	<b>(128,993)</b>	<b>(15,034)</b>	<b>(60,797)</b>	<b>(5,051)</b>	<b>728</b>	<b>(80,154)</b>

(i) Related parties include balances and transactions with 'other related parties' as defined by IAS 24.

(ii) It does not include personnel expenses.

C. Remuneration of key personnel and directors were as follows:

<i>In thousands of soles</i>	09.30.2018	09.30.2017
Remuneration to key personnel	23,153	20,857
Remuneration to members of the Board of Directors	1,122	965
	<b>24,275</b>	<b>21,882</b>

As of September 30, 2018 and 2017 the remuneration pending to pay to key personnel amounted to S/ 6,493 thousand and S/ 7,568 thousand, respectively.

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### 30. Classification of Financial Instruments

Management classifies its financial assets and liabilities in categories as described in note 3.B. As of September 30, 2018 and December 31, 2017 financial assets and liabilities are classified as follows:

	09.30.2018						
	At fair value through profit or loss	Loans and items receivable	Available-for-sale investments		Liabilities at amortized cost	Other liabilities (b)	Total
	At amortized cost (a)	At fair value					
<i>In thousands of soles</i>							
<b>Assets</b>							
Cash and due from banks (note 5)	-	9,379,948	-	-	-	-	9,379,948
Interbank funds	-	94,021	-	-	-	-	94,021
Investments at fair value through profit or loss:							
Capital instruments (note 6)	11,171	-	-	-	-	-	11,171
Debt instruments (note 6)	123,459	-	-	-	-	-	123,459
Available-for-sale investments:							
Instruments representing capital (note 6)	-	-	7,436 (c)	740	-	-	8,176
Instruments representing debt (note 6)	-	-	-	2,975,342	-	-	2,975,342
Loan portfolio (note 7)	-	46,783,334	-	-	-	-	46,783,334
Held-for-trading derivative instruments (note 8)	62,615	-	-	-	-	-	62,615
Accounts receivable (note 9)	-	392,833	-	-	-	-	392,833
Other assets (note 12)	-	481,856	-	-	-	-	481,856
	<b>197,245</b>	<b>57,131,992</b>	<b>7,436</b>	<b>2,976,082</b>	-	-	<b>60,312,755</b>
<b>Liabilities</b>							
Obligations and deposits and other obligations (note 13)	-	-	-	-	-	39,437,052	39,437,052
Interbank funds	-	-	-	-	-	60,014	60,014
Deposits of financial entities and international financial entities (note 13)	-	-	-	-	-	291,694	291,694
Borrowings and debts (note 14)	-	-	-	-	10,010,900	-	10,010,900
Held-for-trading derivative instruments (note 8)	47,820	-	-	-	-	-	47,820
Accounts payable	-	-	-	-	-	3,027,537	3,027,537
Other liabilities (note 15)	-	-	-	-	-	785,747	785,747
	<b>47,820</b>	-	-	-	<b>10,010,900</b>	<b>43,602,044</b>	<b>53,660,764</b>

(a) Including financial assets measured at costs.

(b) Including financial liabilities whose fair value correspond to carrying amounts.

(c) Correspond to unlisted shares (note 6).

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	12.31.2017						
	At fair value through profit or loss	Loans and items receivable	Available-for-sale investments		Liabilities at amortized cost	Other liabilities (b)	Total
			At amortized cost (a)	At fair value			
<i>In thousands of soles</i>							
<b>Assets</b>							
Cash and due from banks (note 5)	-	9,376,539	-	-	-	-	9,376,539
Interbank funds	-	406,108	-	-	-	-	406,108
Investments at fair value through profit or loss:							
Capital instruments (note 6)	11,116	-	-	-	-	-	11,116
Debt instruments (note 6)	558,707	-	-	-	-	-	558,707
Available-for-sale investments:							
Instruments representing capital (note 6)	-	-	5,390(c)	556	-	-	5,946
Instruments representing debt (note 6)	-	-	-	4,827,953	-	-	4,827,953
Loan portfolio (note 7)	-	42,631,366	-	-	-	-	42,631,366
Held-for-trading derivative instruments (note 8)	41,658	-	-	-	-	-	41,658
Accounts receivable (note 9)	-	583,783	-	-	-	-	583,783
Other assets (note 12)	-	55,815	-	-	-	-	55,815
	<b>611,481</b>	<b>53,053,611</b>	<b>5,390</b>	<b>4,828,509</b>	-	-	<b>58,498,991</b>
<b>Liabilities</b>							
Obligations and deposits and other obligations (note 13)	-	-	-	-	-	37,523,236	37,523,236
Interbank funds	-	-	-	-	-	150,040	150,040
Deposits of financial entities and international financial entities (note 13)	-	-	-	-	-	339,191	339,191
Borrowings and debts (note 14)	-	-	-	-	9,691,622	-	9,691,622
Held-for-trading derivative instruments (note 8)	68,011	-	-	-	-	-	68,011
Accounts payable	-	-	-	-	-	4,054,333	4,054,333
Other liabilities (note 15)	-	-	-	-	-	315,112	315,112
	<b>68,011</b>	-	-	-	<b>9,691,622</b>	<b>42,381,912</b>	<b>52,141,545</b>

(a) Including financial assets measured at cost.

(b) Including financial liabilities whose fair value correspond to carrying amounts.

(c) Correspond to unlisted shares (note 6).

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### **31. Financial Risk Management**

The Scotiabank Group has a strong risk culture throughout the entire organization; the risk management is a responsibility shared by all employees, being a main element the risk diversification across different lines of business, products and industries.

It comprises the management of the following main risks:

- A. Credit risk: It is the risk of loss due to debtors, counterparties or third parties' incapacity or weakness of compliance with their contractual obligations.
- B. Market risk: It is the risk of loss in on-balance or off-balance sheet positions arising from the market conditions variations. It generally includes the following types of risk: exchange rate, interest on fair value, price, among other risks.
- C. Liquidity risk: It is the risk of loss due to noncompliance with borrowing requirements and applications of funds arising from cash flow mismatches.
- D. Operational risk: It is the direct or indirect risk of loss to which Scotiabank Group are exposed due to external events, human error or deficiencies or failures in processes, procedures, systems or controls. This operational risk includes legal risk, but excludes the strategic and reputational risks.

Current risk management allows identification, measurement and evaluation of the return on risk, seeking to obtain greater value to shareholders. In order to ensure that strategic objectives are met, risk management is governed by the Risk Appetite Framework approved by the organization, ensuring an appropriate balance between risk and profitability. The Risk Appetite Framework's main purpose is to provide an integrated set of policies, guidelines and principles in order to ensure application of processes to monitor and mitigate the risks to which the Scotiabank Group is exposed, determining the amount and types of risks faced by the Bank.

For proper risk management, it has a series of fundamentals, such as (i) adequate corporate governance, (ii) aligned and updated risk policies and limits, and (iii) risk monitoring.

#### ***i. Adequate corporate governance***

The bodies supporting corporate governance are:

##### ***Board of Directors***

The Board of Directors is responsible to set the main guidelines to maintain an effective risk management supported by the Parent Company, establishing an integral risk management and providing an internal environment that facilitates the development of risk management relying on the Risk Management Committee and the Audit Committee.

##### ***Executive committees***

They are composed by the following committees: The Assets and Liabilities committee (ALCO), Retail Loan Policy committee and the Operational Risk committee.

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### ***Risk senior management***

It is responsible for proposing and implementing the policies, methodologies and procedures for an integral risk management to identify, monitor, mitigate and control the different types of risks to which the Scotiabank Group is exposed. Also, it is involved in the definition and design of the strategy and communicates and strengthens risk culture throughout the Group.

Risk Senior Management has the following units: Corporate and Commercial Loans, Retail Loans, Special Banking, Integral Risk Management and Provisions, Collection, Market Risk, and Operational and Technological Risk.

### ***ii. Aligned and updated risk policies and limits***

Policies are based on recommendations from the different risk units, internal audit, business lines, and industry best practices, regulatory and Parent Company requirements, as well as the recommendations of top management. Policies are guided by the Risk Appetite Framework, and set the limits and controls within which it can operate.

The policies are reviewed and approved by the Board of Directors, either directly or through its committees. These provide a description of the types of exposure, responsibilities and conditions that they are able to do business, in order to ensure proper understanding of customers, products, markets and fully understand the risks associated with each activity.

### ***iii. Risk monitoring***

Risk Division has developed a set of policies to identify measure and communicate the evolution of risk in different products and banking, which allow anticipation of impairment loss of any portfolio in order to take corrective actions.

Main activities and processes applied to have an appropriate risk management are described below:

#### **A. Credit risks**

##### **▪ *Life cycle: admission, monitoring and collection***

The Risk Units are responsible for designing and implementing strategies and policies to achieve a credit portfolio in accordance with the parameters of credit quality and Risk Appetite.

Credit adjudication units analyze and evaluate credit approval from different business segments, with different levels of delegation granted to other teams for their approval, from a risk (measured based on a rating or score) versus profitability perspective. Also, for portfolio managing purposes, the loans are monitored in order to minimize future losses. Concerning the collection models, these customers are segmented by Corporate and Commercial banking and Retail banking. For Corporate and Commercial Portfolio, collections are managed on a case by case basis, transferring it to the Special Bank area, as per policies and red flags, resulting from the monitoring of the portfolio. For Retail portfolio, risk-based strategies (score) are established to optimize available resources for collection seeking to reach greater effectiveness.

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### ▪ **Credit risk mitigation - collateral**

Management has a number of policies and practices to mitigate credit risk. One of them is the use of collaterals; however, the credits are not granted for the amount or quality of guarantees but for the debtor's repayment ability. While the guarantees reduce the risk of loss, they should not be linked to the primary source of repayment.

The value of collaterals is established by means of updated appraisals, which are held regularly and consider market fluctuations. Such valuations are performed by qualified independent experts; they shall meet the required standards and best practices. Additionally, when prices are volatile, margins are applied to compensate for this fluctuation.

Periodical certifications of price, value and fluctuations of the collaterals are conducted; and, if necessary, actions are taken to mitigate the risk associated with the value of these collaterals.

Management of appraisals and collaterals is conducted by an independent unit from the Risk Division.

The types of collateral include residential mortgages, special liens on the business assets, such as inventory, premises and accounts receivable, and special liens on financial instruments such as debt instruments and equity securities.

Additionally, collaterals are classified as established in SBS Resolution 11356 - 2008 *Regulation for the Evaluation and Classification of the Debtor and Provisions Requirement*, as follows:

- Preferred collaterals.
- Preferred easily realizable collaterals.
- Preferred readily realizable collaterals.

### ▪ **Credit rating**

The Scotiabank Group operates an internal credit rating differentiated by banking, which is in line with the Parent Company's. For Corporate and Commercial Credits, it uses the AIRB rating system; based on this internal rating, it assigns the limits of credit autonomy.

For Retail segment, an internal score that reflects the strength of customers based on the probability of default and repay is used. Also, this score determines the strategies to be used with customer based on the risk of each one.

Additionally to these ratings, regulatory debtors' credit rating is used, which determines the provision requirement of customers.

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### ▪ **Debtor regulatory credit rating**

The debtor regulatory credit rating is conducted in accordance with criteria and parameters established by SBS through SBS Resolution 11356 - 2008 *Regulation for the Evaluation and Classification of the Debtor and Provisions Requirement*, which establishes five categories to classify debtors of: Wholesale loan portfolio (corporate, large- and medium-business loans) and Retail loan portfolios (small-business loans, Micro-business loans, consumer and mortgage):

- Standard (0).
- Potential problem (1).
- Substandard (2).
- Doubtful (3).
- Loss (4).

### ▪ **Loan portfolio impairment loss**

As of September 30, 2018 and December 31, 2017, based on SBS Resolution 7036-2012, the Bank and CrediScotia have classified impaired and not impaired loans considering the following criteria:

- Neither past due nor impaired loans  
It comprises those direct loans that currently do not have characteristics of default and relate to client's loans with risk category rated as 'standard' or 'potential problem'.
- Past due but not impaired loan  
It comprises past due client's loans with risk category rated as 'standard' or 'potential problem'.
- Impaired loans:  
For wholesale portfolio, it comprises client's loans rated as 'substandard', 'doubtful' or 'loss', and the refinanced, restructured and lawsuit loans.  
  
For wholesale portfolio, it comprises client's loans overdue 90 days or more, with risk rated as 'substandard', 'doubtful' or 'loss', and the refinanced, restructured and lawsuit loans.

## **B. Market risk**

Market risk is the risk arising from fluctuations in market prices, such as interest rates, equity shares prices, foreign exchange rates and credit spreads that affect the income or the value of its holdings of financial instruments. The objective of the market risk management is to identify, evaluate and control market risk exposure within risk tolerance and appetite parameters, acceptable for the Board of Directors, in order to ensure the solvency while optimizing the return adjusted by risk.

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### **(a) Management of market risk**

Management separates its exposure to market risk between trading and non-trading. Trading portfolios are managed by the Trading unit, and include positions arising from market making and own positions, together with financial assets and liabilities that are managed on a market value basis.

All foreign exchange positions are managed by Treasury. Accordingly, the foreign exchange positions are treated as part of the trading portfolios for risk management purposes.

Management employs different tools to monitor and limit market risk exposures. These are discussed below, separately for trading and non-trading portfolios.

### **(b) Exposure to market risks – Trading portfolio**

The principal tool used to measure and control market risk exposure within the Group's trading portfolio is value at risk (VaR). The VaR is the estimated loss that will arise on the portfolio over the holding period or specific time horizon, due to an adverse market movement with a probability determined by the confidence level, under normal market conditions. The VaR model used by the Group is based upon a 99% confidence level and assumes a 1-day holding period. Considering market data from the previous 300 days, relationships between different markets and prices are observed, the model generates a wide range of plausible future scenarios for market price movements.

Although VaR is an important tool for measuring market risk, the assumptions on which the model is based generate some limitations, including the following:

- A 1-day holding period assumes that it is possible to hedge or dispose of positions within that period. This may not be the case for liquid assets or in situations in which there is severe general market illiquidity.
- A 99% confidence level does not reflect losses that may occur beyond this level. Even within the model used, there is a 1% probability that losses could exceed the VaR.
- VaR is calculated on an end-of-day basis and does not reflect exposures that may arise on positions during the trading day.
- The use of historical data as a basis for determining the possible range of future outcomes may not always cover all possible scenarios, especially those of an exceptional nature.
- The VaR measure depends upon the Scotiabank Group's position and the volatility of market prices. The VaR of a static position reduces if market price volatility declines and vice versa.

Management uses VaR limits for total market risk and interest rate and foreign exchange risks. The overall structure of VaR limits is subject to approval by ALCO and is allocated to trading portfolios. VaR is measured at least daily and monitored through daily reports of use which are submitted from local Market Risk Unit to Treasury and parent company, and monthly reports are submitted to ALCO.

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VaR methodology limitations are recognized by complementing VaR limits with other position and sensitivity limits structures. In addition, a wide range of stress tests is used to model the financial impact of different trading portfolio scenarios. Management determines hypothetical scenarios considering potential macroeconomic events, for example, prolonged market illiquidity periods, reduced fungibility of currencies, natural disasters and other catastrophes. The analysis of scenarios and stress tests are reviewed by ALCO.

The VaR models are subject to regular validation to ensure that they continue to perform as expected and that assumptions used in model development are still appropriate. As part of the validation process, the potential weaknesses of the models are analyzed using statistical techniques, such as back-testing.

Sensitivity analysis in trading portfolio is used to measure the effect of change in the risk factors, including rates and differentials on products and portfolios. These measures are applied by type of product and allow appropriate monitoring, reporting and management.

### **(c) *Exposure to market risks – Non-trading portfolio***

The principal risk to which non-trading portfolios are exposed is the risk of loss due to future cash flows or financial instruments fair values fluctuations because of a change in market interest rates. Interest rate risk is managed through monitoring interest rate gaps and establishing limits by currency for each term. ALCO monitors compliance of these limits and is assisted by Market Risk unit.

Equity price risk is subject to periodical monitoring by the Board of Directors, through the Risk Management Committee, but is not significant in relation to the results and financial position.

The effect of structural foreign exchange positions is managed from the Trading Unit within its limits of position by currency.

The main market risks to which it is exposed are: interest rate risk, currency risk and risk in investment portfolios, which are detailed below:

#### ***Interest rate risk***

This comprises the risk of loss due to interest rates variations. The Scotiabank Group actively manages interest rate exposure risk in order to improve the net interest income according to established risk tolerance policies.

Market risk arising from financing and investment activities are identified, managed, and controlled as part of the Scotiabank Group's assets and liabilities management process, specially liquidity and interest rate risks. Sensitivity analysis assesses the effect of interest rates changes on earnings and the economic value of equity. This sensitivity analysis uses variations of interest rate curves originated by positive and negative parallel shifts, as well as by changes in non-parallel shifts.

Gap analysis is used to assess the interest rate sensitivity of re-pricing mismatches in non-trading operations. Under gap analysis, off-balance sheet assets and liabilities are distributed within repricing dates.

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Products with a contractual maturity are assigned to an interest rate gap term based on the shorter of the contractual maturity date and the next re-pricing date. Products without contractual maturity are assigned an interest rate gap based on observed historical consumer behavior.

Interest rate risks in the non-trading portfolios are mainly driven by the terms and currency of the loan portfolio mismatches. The interest rate risk is managed within the framework of policies approved by the Board of Directors and global limits included in the Risk Appetite Framework and aims to keep under control the risk originated by the effects of net interest income and equity value fluctuations.

Interest rate risk report is presented on a monthly basis by the ALCO to the Risk Control Committee and the Board of Directors, detailing the exposure to such risk by currency, as well as the results of measurement tools, use of limits and interest rate risk stress tests, among other issues related to market risk management in compliance with regulatory provisions of the Parent Company and the Scotiabank Group.

Gap analysis, sensitivity analysis, simulation modeling, and stress testing are used for monitoring and planning purposes.

Models defined by the SBS for interest rate risk assessment for the banking book are as follows:

Equity Value at Risk (EVAR) and Earnings at Risks (EaR) indicators are focused on the potential impact of interest rate changes on value generation, specifically through the financial margin, and the equity value of the Bank and CrediScotia. This methodology is applied under normal and stressed market conditions.

**EVAR:** This indicator is focused on the potential impact of interest rate changes on value generation, specifically, through the financial margin, and the Bank's equity value; measures the percentage of regulatory capital exposed to interest rate risk as a result of marginal mismatches weighted by their respective sensitivity for all temporary bands.

**EaR:** This indicator measures the percentage of regulatory capital exposed to interest rate risk as a result of mismatches accumulated up to one year; this should not exceed 5%.

These methodologies have been determined by the SBS and are applied under normal and stressed market conditions.

### ***Exchange rate risk***

This is the risk of loss due to exchange rates adverse variations of currencies in which the Scotiabank Group negotiates. This risk is managed by the Trading Unit.

The Trading Unit is responsible of administration of foreign exchange operations and forwards portfolio, in accordance with policies, procedures and controls designed to ensure profitable business opportunities, while considering adequate levels of risk and volatility of the market variables professionally and cautiously.

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Market risks are measured and managed within VaR internal limits of global net position in combination with stress tests based on market variables. The consistency of these results is validated through periodical backtesting analysis which compares actual gains or losses with those obtained through the model.

Management calculates the VaR using historical simulation based on 300 days of market data to measure the maximum expected loss from fluctuations in the exchange rate, considering as variables the net asset position in foreign currency and exchange rate volatility. As of September 30, 2018 and December 31, 2017, the net liabilities and assets position of the consolidated statement of financial position in foreign currency amounted to US\$ 303,118 thousand and US\$ 427,121 thousand, respectively (note 4).

As of September 30, 2018, global position of overbought in the Bank amounted to S/ 191,687 thousand (S/ 221,691 thousand as of December 31, 2017).

### ***Investment portfolio risk***

The own investment portfolio and trading portfolio are managed by the ALM Unit and Trading Unit, respectively.

The own investment portfolio is administered in order to manage liquidity and the interest rate risks, and long-term capital investment with attractive returns, and administered within approved policies and limits: limits per type and terms of investment. On the other hand, trading portfolio is acquired with the intention of short-term profit-taking, arising from fluctuations prices.

Investment portfolios are composed of liquid instruments, mainly certificates of deposits issued by the Peruvian Central Reserve Bank and Peruvian Government Treasury Bonds issued in local and foreign currency.

### **C. Liquidity risk**

Liquidity risk is the risk that the Bank is unable to meet in short-term financial obligations and is obliged to borrow money or sell assets in unusually unfavorable conditions.

The approach to managing liquidity is to ensure, as far as possible, that it will always have enough liquidity to meet its obligations when due, under both normal and stressed conditions, without incurring unacceptable losses or damage to the reputation of the Scotiabank Group. The key elements of the liquidity strategy are as follows:

- Maintaining a diversified funding base which consist in customer deposits (both retail and corporate) and wholesale market deposits and maintaining contingent facilities.
- Carrying a portfolio of highly liquid assets, diversified by currency and maturity.
- Monitoring liquidity ratios, maturity mismatches, behavior characteristics of the financial assets and liabilities, and the extent to which the own assets are encumbered and so available as potential collateral for obtaining funding.
- Carrying out stress testing of the liquidity position.

Regular liquidity stress testing is conducted under different scenarios covering normal and stress market conditions. The scenarios are developed using group- specific events (e.g. a rating downgrade) and market-related events (e.g. prolonged market illiquidity, reduced fungibility of currencies, natural disasters or other catastrophes).

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Liquidity ratios are indicators that relate liquid assets to short-term liabilities under one year. The SBS has determined that this relation shall be greater than 8% and 20%, in the case of local and foreign currency, respectively. As of September 30, 2018, the Bank's ratios in local and foreign currencies were 13.9% and 40.2%, respectively (24.9% and 38.7%, respectively as of December 31, 2017).

In the case of CrediScotia, this relation between liquid assets and short-term liabilities shall be greater than 10% and 25%, in the case of local and foreign currency, respectively, given the level of deposits of CrediScotia. As of September 30, 2018, CrediScotia ratios in local and foreign currencies were 23.53% and 131.71%, respectively (21.2% and 134.7%, respectively as of December 31, 2017).

Liquidity Coverage Ratio (LCR) is an indicator of liquidity level in a hypothetical stress scenario; it indicates if the entity have sufficient liquidity to withstand liquidity disruptions for up to 30 days, without the need of turning to the market. As of September 30, 2018, the minimum amount required by the regulator was 80% and the Bank presented comfortable levels of liquidity reaching 100.02% in local currency and 100.39% in foreign currency (107.3% in local currency and 114.5% in foreign currency as of December 31, 2017).

### **D. Operational and technological risk**

The Operational Risk Management Framework sets out an integrated approach to identify, assess, control, mitigate and report operational risks based on key components such as the Internal Governance, Risk Appetite, Measurement, Monitoring and Reporting, among other approaches.

The Scotiabank Group recognizes that an efficient and integrated operational risk management is a key component of risk management best practices; therefore the Bank, in order to have a solid internal governance of operational risk, adopted a three-line of defense model, establishing the responsibilities of operational risk management.

#### ***Operational risk appetite***

During 2017, as in previous years, the operational risk appetite was determined based on limits of losses for operational risk at the level of the entire Scotiabank Group, which was in turn distributed at the level of the companies that compose it, among them, the Bank and CrediScotia. Likewise, a distribution of this loss limit was made to the main Vice Chairs of the Bank and first-line Management of CrediScotia. These loss limits also are included within the balance scorecards of each management areas indicated above.

In addition, a formal procedure for the distribution of the operational risk loss limit has been regulated; this procedure is included in the Operational Risk Policy.

During 2017, the development of operational risk management methodologies for the Scotiabank Group have continued in order to incorporate aspects to strengthen management.

The regulatory capital requirement imposed by the SBS in 2016 was eliminated; in that year, the authorization for the application of the alternative standard method for the calculation of the regulatory capital requirements for operational risk under the SBS regulatory standard was obtained.

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Main methodologies are the following:

- (a) Operational risk event methodology.
- (b) Key risk indicators – (KRIs) methodology.
- (c) Business Continuity Management – BCM- methodology.
- (d) Operational Risk and Controls Assessment methodology; Risk Control Assessment and Risk Control Self-Assessment (RCSA).
- (e) Risk assessment of new initiatives and/or significant changes, among others.

**(a) Loss event methodology**

The Bank follows up relevant data of operational risk losses relevant for the Business Line, in accordance with the Basel loss event types. Losses are reported by Operational Risk Managers (ORM) designated in the various decentralized and specialized units of the Bank and identified in the accounting books. Through reviews by the Operational and Technological Risk Unit, these losses are included in loss event data base for operational risk. This database is used to determine trends, conduct analysis, identify and mitigate risks, and prepare reports of operational risk losses intended for Senior Management and the Board of Directors.

Loss data collection exercise ensures consistent management across Scotiabank Group which allows classifying loss event data per line of business, type of event and effect type, as per Basel definitions and according to the Regulations for Operational Risk Management approved by the local regulator.

Losses are also classified by significant internal units and types of risk, according to the Scotiabank Group's standard inventory of operational risks. On the other hand, loss event data serves as information source and reference for Risk and Control Assessment and Key Risk Indicators, it also allows providing analysis and generating awareness on internal and external operational risks.

As in previous years, ORMs' performances were assessed considering the opportunity, availability, quality of the provided information and implementation of risk mitigation measures; also, following-up the obtained results from the management, where ORMs' performance is highlighted, indicating opportunities for improvement, as well as the obtained rating.

As of the closing of year 2017, there are 40 Operational Risk Managers and 3 Liaison Officers at the Scotiabank Group level, whereas at the bank level there are 35 Risk Managers for the management of loss events. In addition, throughout the year 2017, the Scotiabank Group's results reports were periodically presented to the Global Operational Risk of the Parent Company, Operational Risk Committee, Risk Control Committee, Board of Directors of the Bank, as well as the first-line Vice Chairs and Management of the Bank and CrediScotia.

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### **(b) Key risk indicators (KRIs)**

The Key Risk Indicator methodology is a measure to report on potential risks, current status or trend of operational risk exposures.

The Key Risk Indicators methodology provides information to the first two lines of defense in order to promote proactive managing of risk exposures through the monitoring and communication of risks and operational trends to ensure adequate and timely response of Management. The existence of efficient Key Risk Indicators will serve as an early warning system of possible changes in the operational risk profile of the business.

The Key Risk Indicators methodology provides a systematic approach to coordinate the supervision of the key factors of operational risks and provides a focus, structure and terminology in common to implement and manage the selection of Key Risk Indicators across the Scotiabank Group.

During 2017, the activities developed within the methodology were:

- Creation of 12 corporate indicators, transversal to all areas of the Scotiabank Group, which are also monitored.
- Monitoring of the 47 executive risk indicators (25 of the Bank and 22 of CrediScotia) 53% of KRIS have risk thresholds, in cases where the accepted risk levels were exceeded, they generated the implementation of action plans and corrective measures.
- 33 informative indicators were monitored, of which 94% have a threshold.
- Indicators were analyzed, and if necessary, their accepted risk levels (risk thresholds) were assessed with the business owners/managers per appetite levels: acceptable (green), with potential risk (amber), critical (red).
- Following-up and monitoring of the action plans derived from the Risk Indicators methodology.
- Making presentations to the main Vice Chairs of the Bank and CrediScotia, Risk Control Committee, Operational Risk Committee, Board of Directors and Parent Company.
- Mapping indicators for types of loss events and risk categories defined for the Bank.

### **(c) Business Continuity Management – BCM**

The Bank and CrediScotia have 99 and 14 current and deployed Business Continuity Plans (BCPs) in its Vice chairs and/or main management areas, subsidiaries and special agencies.

In January, February, July, August and November 2017, face-to-face trainings and workshops were carried out for 190 business continuity planners of the Bank and 30 business continuity planners of CrediScotia. The objective of these trainings was to strengthen the Business Continuity culture in the company and also to assist them in the process of updating and executing annual tests of their Business Continuity Plans (BCPs).

To date, Business Continuity Management is part of the Bank's general induction program.

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The process of updating the Business Continuity plans was carried out in a massive way, meeting the Scorecard of April and October of 2017. The business units updated their plan strategy, BIA analysis and guide to pandemic. They also performed corresponding tests (Walkthrough exercise, call chain test, quarterly review of the call chain and the complete simulation test at the alternate site).

The Scotiabank Group has an alternate site to support their most critical processes; which remains ready and operational 24 hours a day, 7 days a week providing support to the most sensitive processes. To date, there are 103 physical working positions. During the fourth quarter of 2017, simulation tests of continuity plans TYPE I and II (containing critical process sensitive to the time) were favorably completed. The objective of these tests is to ensure the proper functioning of the working positions in case these were required due to a contingency, disaster or emergency.

On August 24, 2017, the Bank participated in the II Sector-wide Business Continuity Exercise announced by the SBS. The scenario of the exercise was an earthquake in Lima of 8.5 degrees with tsunami, with the participation of 13 financial entities, 6 insurance companies, 2 transport companies, 3 authorities; totaling 600 people, among them 120 first-line managers. The organizational structure for crisis management led by the Local Incident Management Team (LIMT) became operative from the Emergency Operations Center; and the OPERA Plan (protocols for action in the face of crisis) was deployed.

**(d) *Operational Risk and Controls Assessment methodology: Risk Self-Assessment and Risk Control Self Assessment (RCSA)***

Operational Risk and Controls Assessment methodology aims at reviewing and diagnosis the internal control system by identifying the main risks to which activities are exposed, the existing controls to mitigate them and the opportunities for improvement in the risk management process.

The process is a basic component and an efficient tool that provides advantages such as:

- It strengthens the risk and control culture in the organization by promoting an understanding of business risks and responsibilities in the mitigation process.
- It promotes a continuous critical thinking, motivating the support and business units to design, construct and maintain more effective control systems.
- It contributes to increase the quantity and quality of reliable information on the situation of control of the existing risks.
- It contributes to strengthening the internal control system; thus minimizing distrust of subsequent audits.
- It allows to focus on the most significant risks for the entity and to reduce costs in recurring reviews.

The universe for the application of risk and control assessment is composed by:

1. Business lines: approach per product family.
2. Support units: per unit approach.

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The Operational Risk and Controls Assessment methodology is composed of the following stages:

- Risk identification.
- Inherent risk assessment.
- Identification and assessment of controls.
- Determination of residual risk.
- Treatment.

During 2017, methodological improvements were incorporated making it possible to strengthen the risk assessment program by incorporating scales for risk assessment and determination of exposure levels. This resulted in six risk assessments, one of them at the unit's overall level as part of the Parent Company's corporate methodology. Likewise, risk self-assessments have been managed in sixty-five (65) risk matrices with an approach per product family in business lines and support units.

The risk and control self-assessment matrix is the local tool for identification and assessment of operational risks of products and support areas. To complement this, the RCSA tool (Risk Control Self-Assessment) is being used to report operational risks to the Parent Company.

### **(e) *Management of new initiatives and major changes in the business, operating and systems environment.***

- i. The Scotiabank Group has established policies for comprehensive risk assessment of new products and in case of major changes in the business, operational or systems environment; these policies describe the general principles applicable to the review, approval and implementation of new products and services within the Bank. The principles are intended to provide guidance to Business Lines in the development of processes and guidelines of risk assessment to be integrated into the policies and procedures on new products. All new products or major change in the business, operational or system environment shall have a comprehensive risk assessment prior to its development, and it shall be updated after its implementation.
- ii. In order for an initiative to be approved, it is required that the initiative has a risk self-assessment conducted by the Leader or Sponsor, being the Operational and Technological Risk Unit the responsible for contrasting / challenging the results and other control functions such as Compliance and Legal Advisory units, among others.
- iii. The Operational Risk Committee provides oversight to ensure that all Business Lines implement principles and conduct products risk assessments consistently.
- iv. The Operational and Technological Risk Unit also provides advice to the owner of the initiative during the Integral Risk Assessment process.

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**(f) Training and awareness**

Throughout 2017, training on Technological and Operational Risk and Business Continuity has been provided to personnel of agencies, business officers, specialized units, Operational Risk managers and new staff joining the Scotiabank Group.

**32. Fair Value**

The table below shows a comparison of carrying amounts and fair values of the Scotiabank Group's financial instruments per item in the consolidated statement of financial position as of September 30, 2018 and December 31, 2017:

<i>In thousands of soles</i>	<b>Carrying amount</b>		<b>Fair value</b>	
	<b>09.30.2018</b>	<b>12.31.2017</b>	<b>09.30.2018</b>	<b>12.31.2017</b>
<b>Assets</b>				
Cash and due from banks	9,379,948	9,376,539	9,379,948	9,376,539
Interbank funds	94,021	406,108	94,021	406,108
Investments at fair value through profit or loss				
Capital instruments	11,171	11,116	11,171	11,116
Debt instruments	123,459	558,707	123,459	558,635
Available-for-sale investments				
Instruments representing capital	8,176	5,946	8,176	5,946
Instruments representing debt	2,975,342	4,827,953	2,975,342	4,827,510
Loan portfolio	46,783,334	42,631,366	46,783,334	42,631,366
Held-for-trading derivative	62,615	41,658	62,615	41,658
Accounts receivable	392,833	583,783	392,833	583,783
Other assets	481,856	55,815	481,856	55,815
	<b>60,312,755</b>	<b>58,498,991</b>	<b>60,312,755</b>	<b>58,498,476</b>
<b>Liabilities</b>				
Deposits and obligations	39,437,052	37,523,236	39,437,052	37,523,236
Interbank funds	60,014	150,040	60,014	150,040
Deposits of financial entities and international financial entities	291,694	339,191	291,694	339,191
Borrowings and debts	10,010,900	9,691,622	11,270,318	9,838,689
Held-for-trading derivative	47,820	68,011	47,820	68,011
Accounts payable	3,027,537	4,054,333	3,024,221	4,112,687
Other liabilities	785,747	315,112	785,747	315,112
	<b>53,660,764</b>	<b>52,141,545</b>	<b>54,734,028</b>	<b>52,346,966</b>

Fair value or market estimate is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable and willing parties in an arm's length transaction, under the presumption that the entity is a going concern.

When a financial instrument is traded in a liquid and active market, its published price quotation is the best evidence of its fair value.

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When a price quotation is not available, or may not be a reliable fair value of a financial instrument, its fair value could be estimated based on price quotation similar instruments, using discounted cash flow analysis or other estimation techniques. Due to these techniques are based on subjective factors and, in some cases, on inexact factors, any change in them or in the estimation methodology used could have a material effect on the fair values of financial instruments. Even though management has used its best judgment in estimating the fair values of these financial instruments, a fair value is not an indication of net realizable gain or liquidation value.

Methodology and assumptions used depend on the terms and risks characteristics of the different financial instruments, as shown below:

- (a) Cash due from banks and interbank funds represent cash and short-term deposits that are not considered to be a significant credit risk.
- (b) Investments at fair value through profit or loss are recorded at their estimated market value, which is the same as the carrying amount.
- (c) Available-for-sale investments are generally listed or have a market value through future discounted cash flows.
- (d) Market values of loan portfolio are the same as the carrying amount.
- (e) Market values of deposits and obligations are the same as the carrying amount.
- (f) Debts to banks and correspondent banks accrue interest at fixed and floating rates and have short- and long- term maturities. The fair value of these financial instruments has been calculated using discounted cash flows considering the funding curve.
- (g) Securities, bonds and obligations issued accrue interest at fixed rates. The fair value of these financial instruments has been calculated using discounted cash flows considering the same methodology of item (f).
- (h) Forward foreign currency agreements are recorded at estimated market value; therefore there are no differences with their corresponding fair values.

Consequently, as of September 30, 2018 and December 31, 2017, fair or estimated market values of the financial instruments do not differ significantly from their corresponding carrying amount.

### ***Fair value hierarchy***

The Scotiabank Group classifies financial instruments carried at fair value based on their hierarchy or valuation techniques applied. This classification has three levels as described below:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Valuation techniques that use significant inputs data and variables with material effect on fair value estimation that are directly or not directly observable in the market.
- Level 3: Valuation technique, where some of the input data and variables are not observable in the market.

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The table below shows the valuation levels applied as of September 30, 2018 and December 31, 2017, to determine the fair value of financial instruments:

<i>In thousands of soles</i>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>2018</b>				
<b>Assets</b>				
Investments at fair value through profit or loss:				
Instruments representing capital	-	11,171	-	11,171
Instruments representing debt	-	123,429	-	123,429
Available-for-sale investments:				
Instruments representing capital	722	-	7,454	8,176
Instruments representing debt	-	2,975,119	-	2,975,119
Held-for-trading derivative	-	62,615	-	62,615
	<b>722</b>	<b>3,172,334</b>	<b>7,454</b>	<b>3,180,510</b>
<b>Liabilities</b>				
Held-for-trading derivative	-	47,820	-	47,820
	-	<b>47,820</b>	-	<b>47,820</b>
<b>2017</b>				
<b>Assets</b>				
Investments at fair value through profit or loss:				
Instruments representing capital	-	11,116	-	11,116
Instruments representing debt	-	558,635	-	558,635
Available-for-sale investments:				
Instruments representing capital	538	-	5,408	5,946
Instruments representing debt	-	4,827,510	-	4,827,510
Held-for-trading derivative	-	41,658	-	41,658
	<b>538</b>	<b>5,438,919</b>	<b>5,408</b>	<b>5,444,865</b>
<b>Liabilities</b>				
Held-for-trading derivative	-	68,011	-	68,011
	-	<b>68,011</b>	-	<b>68,011</b>