



BANGKO SENTRAL NG PILIPINAS
OFFICE OF THE DEPUTY GOVERNOR
SUPERVISION AND EXAMINATION SECTOR

CIRCULAR LETTER NO.CL-2012 - 030

To : ALL BANKS

Subject : Limits on Borrowings of Local Government Units (LGUs)

Pursuant to the instruction of the Monetary Board (MB), in its Resolution No. 7.A dated 5 January 2012, all Banks are directed to adopt and adhere to the policy limits set by the Department of Finance (DOF) through the Bureau of Local Government Finance (BLGF) in granting loans and credit accommodations to the local government units (LGU).

Quoted hereunder is an excerpt from the 7 February 2012 letter of Officer-In-Charge and Executive Director of BLGF on the policy action used by BLGF in the issuance of the Certificate of Net Service Ceiling and Borrowing Capacity.

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Currently, BLGF is guided by the statutory provisions specifically Section 324 of the Local Government Code (LGC). Although the LGC did not provide a limit as to amount an LGU can borrow, the maximum debt service allocation in the local budget is pegged at 20% of regular income. In no case, shall both the existing and proposed loan amortization exceed 20% of the current estimated annual income from regular sources plus IRA, for the current year as estimated by the DBM.

This Bureau issues Certificate of Net Service Ceiling and Borrowing Capacity pursuant to Local Finance Circular No. 1-2000 dated January 19, 2000 and based on the formula presented below:

Computation for Debt Service and Borrowing Capacity

Debt service ceiling (DSC) is the maximum amount that an LGU can appropriate in the annual budget for the payment of statutory and contractual obligations computed as follows:

DSC = 20% x Annual Regular Income (ARI)

Net DSC = DSC – all loans which are payable during the year, including (principal, interest) amortizations, sinking fund, etc.

Note: Annual Regular Income (ARI) includes:

- *Real property taxes*
- *Business taxes*
- *Fees and other charges*
- *Income from economic enterprises*
- *Internal Revenue Allotment (IRA)*
- *Share in exploitation of national wealth when recurring*

On the other hand, borrowing Capacity (BC) is the maximum amount of statutory and contractual obligations that an LGU may incur over a period of one or more years at a specified rate of interest computed as follows:

$$BC = \text{Net DSC} \times \text{Net Present Value (NPV)}$$

Given this limitation, the BLGF has no legal authority to impose a cap on LGU borrowings. It may be more feasible for the GFIs, domestic private banks and other lending institutions to exercise prudence in the grant of loan to LGU taking into consideration their paying capacities and the viability of projects to be funded from the proceeds of the loan.

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(Sgd.) SALVADOR M. DEL CASTILLO
OIC-Executive Director"

Thus, all banks should require the submission of the Certificate of Net Service Ceiling and Borrowing Capacity issued by the BLGF from a LGU-borrower as part of its due diligence.

For guidance and strict implementation.


NESTOR A. ESPENILLA, JR.
Deputy Governor

 April 2012