



BANGKO SENTRAL NG PILIPINAS

OFFICE OF THE GOVERNOR

CIRCULAR NO. 1150 Series of 2022

Subject: Prudential Framework for Large Exposures Monitoring Threshold

The Monetary Board, in its Resolution No. 1179 dated 11 August 2022, approved the amendments to the prudential guidelines on large exposures as embodied under Section 361 of the Manual of Regulations for Banks (MORB) and Section 341-Q of the Manual of Regulations for Non-Bank Financial Institutions (MORNBFI).

Section 1. Section 361/341-Q of the MORB/MORNBFI on large exposures are hereby amended to read, as follows:

Section 361/341-Q FRAMEWORK FOR LARGE EXPOSURES MONITORING THRESHOLD

Policy Statement. The Bangko Sentral is cognizant that risks arising from large exposures of banks/quasi-banks (QBs) or “covered banks/QBs” to a single counterparty or group of connected counterparties could pose concerns to the stability of each bank/QB and the financial system. In this light, covered banks/QBs shall identify, measure, monitor and control large exposures to protect covered banks’/QBs’ solvency from maximum possible losses in the event of sudden counterparty failure pursuant to Sec. 143/143-Q.

Scope of application. The large exposures framework shall be applicable to all universal/commercial banks (UBs/KBs) and their subsidiary banks and QBs or “covered banks/QBs”. Large exposures of covered banks/QBs shall be computed and compared with Tier 1 capital on both solo and consolidated bases.

Definition. For purposes of this Section, the following terms shall apply:

“Large exposures” shall refer to exposures to a single counterparty or a group of connected counterparties equal to or greater than ten percent (10%) of a covered bank’s/QB’s Tier 1 capital as defined under applicable and existing capital adequacy framework/Sec. 125-Q.

“Connected counterparties” refer to a group of counterparties that are connected through (a) direct or indirect control of one of the counterparties over the other(s) or (b) economic interdependencies and must be treated as a single counterparty. Control shall be determined in accordance with Item “d” of Section 131 (*Definition of Terms*)/Item “c” of Section 131-Q (*Definition of Terms*).

“Economic Interdependence” refers to a situation where counterparties are reliant on each other, such that if one of the counterparties experiences financial problems in repaying its obligations, the creditworthiness of the other/s would also likely deteriorate. Covered banks/QBs shall define in their credit policy criteria in determining connectedness based on economic interdependence, which shall consider, among others, significant dealings or transactions of one or

more counterparty/ies that impact the financial capacity or ability to repay the obligations of the other counterparty/ies.

In establishing connectedness based on economic interdependence, covered banks/QBs shall consider the following criteria:

- a. fifty percent (50%) or more of a counterparty's annual gross receipt or gross expenditures is derived from transactions with the other counterparty;
- b. one (1) counterparty has fully or partly guaranteed the exposure of the other counterparty, or is liable by other means, and the exposure is significant that the guarantor is likely to default if a claim occurs;
- c. fifty percent (50%) or more of a counterparty's production/output is sold to another counterparty, which cannot be easily replaced by other customers;
- d. the expected source of funds to repay the loans of both counterparties is the same and neither counterparty has another independent source of income from which the loans may be serviced and fully repaid;
- e. it is likely that the financial difficulties of one counterparty would cause difficulties for the other counterparty/ies in terms of full and timely repayment of liabilities;
- f. the insolvency or default of one counterparty is likely to be associated with the insolvency or default of the other counterparty/ies; or
- g. the counterparties rely on the same source for the majority of their funding and, in the event of the common provider's default, an alternative provider could not be found.

Covered banks/QBs shall identify possible connected counterparties on the basis of economic interdependence in all cases where the sum of all exposures to a single counterparty exceeds five percent (5%) of Tier 1 capital. Covered banks/QBs shall maintain adequate documentation of the basis of its determination of a connected counterparty group and the due diligence conducted based on the above criteria.

In cases where the covered bank/QB's assessment of the criteria differs from that of the Bangko Sentral, covered banks/QBs shall upon request, provide the basis for its assessment to the Bangko Sentral.

Large exposures monitoring threshold. Covered banks/QBs shall comply with the large exposures monitoring threshold of twenty five percent (25%) of Tier 1 capital, on a solo and consolidated basis.

The large exposures monitoring threshold shall be implemented to protect covered banks'/QBs' solvency from maximum possible losses in case of sudden failure of a counterparty or group of connected counterparties and to facilitate monitoring by the Bangko Sentral of concentration risks in the financial system.

Covered banks/QBs shall consider the large exposures monitoring threshold at the time of grant of new loan, credit accommodation, or guarantee, as well as renewal, restructuring or refinancing of existing credit exposures.

Aggregation and measurement of exposures. A covered bank's/QB's exposure to all of its counterparties or connected counterparties, excluding those listed under this Section on *Exclusions* shall be subject to large exposures monitoring

threshold. An exposure to a counterparty shall include both on- and off-balance sheet exposures in the banking book and/or the trading book and instruments with counterparty credit risk. The exposure values shall be measured in accordance with the following:

- a. *On-balance sheet exposures in the banking book* such as loans, receivables or advances shall be measured at net carrying amount of the exposure (i.e., net of specific allowance, and unamortized discount/premium). Debt and equity securities shall be measured at fair value or net carrying amount (i.e., book value net of accumulated market gains/losses and specific allowance), as applicable, in accordance with Philippine Financial Reporting Standards (PFRS) 9 *Financial Instruments*. The netting of loans and deposits shall not be allowed;
- b. *Traditional off-balance sheet assets* (e.g., direct credit substitutes¹, transaction-related contingencies², trade-related contingencies arising from movement of goods³) shall be measured at their credit equivalent amount derived by multiplying the nominal amount by the appropriate credit conversion factor as provided in Part V of Appendix 59/Q-45 on Risk-Based Capital Adequacy Frameworks;
- c. *Over-the-counter (OTC) derivative contracts or instruments other than securities financing transactions (SFT)* that give rise to counterparty credit risk shall be measured at their credit equivalent amount derived by adding the current credit exposure (or replacement cost) and an estimate of the potential future credit exposure (or add-on) in accordance with Part V of Appendix 59/Q-45 on Risk-Based Capital Adequacy Framework;
- d. *Repo-style transactions or SFT*, (e.g., repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions) that give rise to counterparty credit risk shall be measured in accordance with Part V of Appendix 59/Q-45 on Risk-Based Capital Adequacy Framework;
- e. *Exposures held in the trading book* such as:
 - (1) Plain vanilla debt and equity instruments shall be measured at fair value;
 - (2) Derivative contracts (other than option contracts) such as swaps, futures, forwards and credit derivatives shall be decomposed into their individual legs. Only transaction legs representing exposures on the part of the covered bank/QB (i.e., receivable) shall be measured similar to item c above;
 - (3) In case of credit derivatives that represent sold protection, the exposure to the reference entity shall be based on the amount that is due in case the reference entity triggers the instrument minus the absolute fair value of the credit protection. From the perspective of a covered bank/QB as a protection seller, in case the fair value of the

¹ Guarantees and financial standby letters of credit (LC)

² Performance standby LCs (net of margin deposit), note issuance facilities and revolving underwriting facilities, and other commitments (e.g., formal standby facilities and credit lines with maturity of more than one year)

³ Trade related guarantees, sight LCs, usance LCs, deferred LCs, revolving LCs, other commitments with maturity of up to one (1) year

credit derivative is positive, it shall be considered as an exposure by the protection seller to the protection buyer.

For credit-linked notes, a covered bank/QB as a protection seller shall consider the positions measured at market value both in the bond of the note issuer and in the underlying asset referenced by the note;

- (4) Options shall be measured based on the change in option prices that would result from a default of the respective underlying instrument (i.e., loss in case of a “jump to default” of the underlying) as follows:

Option Position	Exposure Measurement Approach
Long call option	Option market value
Short call option	
Long put option	Option strike price minus option market value
Short put option	

The resulting positions shall in all cases be aggregated. A resulting negative net exposure must be set to zero.

- (5) Offsetting of positions in the trading book shall be allowed only in case of long and short positions in identical issues with exactly the same issuer, coupon, currency and maturity.

When the result of the offsetting is a net short position with a single counterparty, such net exposure need not be considered as an exposure for purposes of compliance with the framework for large exposures monitoring threshold.

Netting across banking and trading books is not permitted; and

- f. An exposure amount to a counterparty that is deducted from capital should not be added to other exposures to a counterparty for the purpose of this Section.

Eligible credit risk mitigation (CRM). The eligible CRM techniques shall be limited to those that meet the operational requirements for collaterals, guarantees and credit derivatives and eligibility criteria for CRM providers pursuant to Parts V and VI of Appendix 59/Q-45 on Risk-Based Capital Adequacy Framework.

A covered bank/QB shall be allowed to recognize a reduction in the value of the exposure to the original counterparty by the amount of the eligible CRM technique following the measurement approaches provided in the Risk-Based Capital Adequacy Framework. The recognized amount shall be:

- the value of the protected portion in case of unfunded credit protection;
- the value of the portion of a claim collateralized by the fair value of the recognized financial collateral using simple (substitution) approach for risk-based capital requirements; and
- the value of the collateral adjusted after applying the required haircuts under Part V of Appendix 59/Q-45 on Risk-Based Capital Adequacy Framework, in the case of financial collateral using the comprehensive approach for risk-based capital requirements.

When the exposure value to a counterparty is reduced due to the recognition of applicable CRM technique, the covered bank/QB shall also recognize an exposure to the CRM provider equal to the amount that the exposure value to the original counterparty was reduced.

Maturity mismatches in CRM shall be recognized only when the original maturities are equal to or greater than one (1) year and the residual maturity of the hedge is not less than three (3) months. If there is a maturity mismatch, the adjustment of the credit protection shall be determined using the same approach as prescribed in the Risk-Based Capital Adequacy Framework.

Exclusions. The following exposures shall be excluded from the large exposures monitoring threshold:

- a. Exposures to sovereigns and their central banks, including exposures to the extent guaranteed by or secured by financial instruments issued by sovereigns and their central banks;
- b. Exposures to intra-group companies (i.e., between covered bank/QB and its parent, subsidiaries, affiliates or related parties);
- c. Exposures to project finance as defined under Sec. 344/325-Q, including those that are funding green or sustainable projects;
- d. Exposures to finance infrastructure projects for public use as defined under Item "a" of Sec. 363-A of the MORB;
- e. Loans to micro, small and medium enterprises as defined under Sec. 332 of the MORB;
- f. Loans, other credit accommodations and guarantees that are excluded from the single borrower's limit (SBL) except item "g" under Sec. 362 (*Exclusions from loan limit*) /Sec. 342-Q;
- g. Interbank call loans as well as intraday and end-of-day interbank exposures arising from interbank payment and settlement processes shall be excluded from large exposures; and
- h. Such other exposures as may be approved by the Monetary Board.

Monitoring and reporting requirements. Covered banks/QBs shall have a system on the monitoring of large exposures and conducting the related due diligence in determining connected counterparties. The records or documentation thereof shall be made available to the Bangko Sentral for verification at any given time.

Covered banks/QBs shall likewise include the impact of material concentration risk from large exposures into their stress testing exercise for purposes of enhancing risk management system and assessing capital adequacy pursuant to *Guidelines on Internal Capital Adequacy Assessment Process (ICAAP)* under Appendix 94/Q-54.

Covered banks/QBs shall report to the Bangko Sentral on a semi-annual basis or every 30 June and 31 December of each year, its large exposures on both solo and consolidated bases using the prescribed format (Appendix A of this Circular). The following exposures shall be included in the said report:

- (1) all exposures that meet the definition of large exposures and net of allowed exclusions shall be measured in accordance with the foregoing provisions on *Aggregation and measurement of exposures*, and shall be reported in both gross and net of the effects of eligible CRM technique/s; and
- (2) all excluded exposures under item "(1)" and those excluded exposures with values equal to or above ten percent (10%) of covered bank's/QB's Tier 1 capital which are not captured under item "(1)".

The Report on Large Exposures shall be considered a Category A-1 report and shall be electronically submitted to the Department of Supervisory Analytics of the Bangko Sentral within fifteen (15) banking/business days from end of the reference semester. The submission of the Report on Large Exposures shall be subject to penalties provided under Sec. 171 (*Sanctions on Reports for Non-compliance with the Reporting Standards*)/Sec. 172-Q (*Reports*).

Section 2. Appendix 7 of the MORB on Reports Required of Banks and Appendix Q-3 of the MORNBF on List of Reports Required from Quasi-Banks are hereby amended to include the "Report on Large Exposures", a primary report applicable to universal and commercial banks and their subsidiary bank/quasi bank.

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure/ E-mail Address
A-1		Section 361/341-Q of the MORB/MORNBF	Report on Large Exposures	Semestral	15 banking/business days from end of reference semester	Department of Supervisory Analytics

Section 3. The guidelines governing the mode and submission of the semestral report on large exposures shall be covered by a separate issuance.

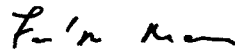
Section 4. Transitory Provision. The following provisions shall be incorporated as footnote to Section 361/341-Q of the MORB/MORNBF on framework for large exposures monitoring threshold.

For monitoring purposes, covered banks/QBs shall submit the reportorial template on large exposures, on both solo and consolidated bases, starting with the reporting period ending 31 December 2023.

Starting from the effectivity of the Circular up to the full implementation of the large exposures framework on 01 January 2024, covered banks/QBs are also expected to make the necessary adjustments or enhancements in its risk management system to ensure adherence to the foregoing guidelines particularly in determining connectedness of counterparties.

Section 5. This Circular shall take effect fifteen (15) calendar days following its publication either in the Official Gazette or in a newspaper of general circulation.

FOR THE MONETARY BOARD:


FELIPE M. MEDALLA
Governor

23 August 2022

Appendix A

Submission Original copy to the
Department of
Supervisory Analytics

Category: A-1

Deadline: 15 banking days after
end of reference
semester

(Name of Covered Bank/Quasi-bank)	(Code)
(Address)	

REPORT ON LARGE EXPOSURES

(Indicate if for Solo Basis or Consolidated Basis)

As of _____ (Semester-End)

We hereby certify that all matters set forth in this report and all its supporting schedules are true and correct, to the best of our knowledge and belief.

(Signature over Printed Name of Chief Executive
Officer or Executive Vice President and
Comptroller/Chief Accountant)

(Name of Covered Bank/Quasi-bank)
Report on Large Exposures to Single Counterparty or Group of Connected Counterparties
Large exposures net of allowed exclusions, before and after considering the effects of eligible credit risk mitigation (CRM)
For the Semester ending [30 June 20./31 December 20.]

No.	Name of Counterparty/Counterparty Group	Type of Counterparty (i.e., Single or Group of Connected Counterparties) ^a	Gross Exposures				Eligible Credit Risk Mitigation (CRM) Techniques ^e				Net Exposures	Tier 1 Capital	% to Tier 1 Capital
			On-Balance Sheet ^b	Off-Balance Sheet ^c	Other Exposures ^d	Total	Financial Collaterals	Guarantees	Others	Total			
1	2	3	4	5	6	7 (sum of columns 4 to 6)	8	9	10	11 (sum of columns 8 to 10)	12 (Column 7 - 11)	13	14 (column 12 / 13)
[To be presented from largest to smallest based on the net amount of exposures in relation to Tier 1 Capital (i.e., Column 14)]													
- add rows as necessary -													

a. Indicate if single or group of connected counterparties pursuant to the criteria in assessing connectedness based on economic interdependence under Section 361/341-Q of the Manual of Regulations for Banks/Non-Bank Financial Institutions (MORB/MORNBFI).

b. Please refer to item "a" for on-balance sheet exposures in the banking book under Aggregation and Measurement of Exposures of Section 361/341-Q of the MORB/MORNBFI.

c. Please refer to item "b" for off-balance sheet exposures under Aggregation and Measurement of Exposures of Section 361/341-Q of the MORB/MORNBFI.

d. Please refer to other exposures on items "c to e" under Aggregation and Measurement of Exposures of Section 361/341-Q of the MORB/MORNBFI.

e. Report the value of the protected portion of exposures following the approach under Eligible Credit Risk Mitigation of Section 361/341-Q of the MORB/MORNBFI.

f. Please refer to total tier 1 capital as reflected in the Risk-Based Capital Adequacy Ratio Report.

Schedule B

(Name of Covered Bank/Quasi-bank)
Report on Large Exposures to Single Counterparty or Group of Connected Counterparties
All excluded exposures
For the Semester ending [30 June 20__/31 December 20__]

No.	Name of Counterparty	Type of Counterparty (i.e., Single or Group of Connected Counterparties) ^a	Name of Related Counterparty Group	Gross Exposures on Reporting Date				Eligible Credit Risk Mitigation (CRM) Techniques ^e	Net Exposures (after considering the effect of CRM)	Tier 1 Capital ^f	% to Tier 1 Capital		Rationale/Justification for Not Aggregating ^g
				On-Balance Sheet ^b	Off-Balance Sheet ^c	Other Exposures ^d	Total				Before Considering Eligible CRM techniques	After Considering Eligible CRM techniques	
1	2	3	4	5	6	7	8 (sum of 5 to 7)	9	10 (column 8 - 9)	11	12 (column 8/11)	13 (column 10 / 11)	

Total

- a. Indicate if single or group of connected counterparties pursuant to the criteria in assessing connectedness based on economic interdependence under Section 361/341-Q of the MORB/MORNBFI.
- b. Please refer to item "a" for on-balance sheet exposures in the banking book under Aggregation and Measurement of Exposures of Section 361/341-Q of the MORB/MORNBFI.
- c. Please refer to item "b" for off-balance sheet exposures under Aggregation and Measurement of Exposures of Section 361/341-Q of the MORB/MORNBFI.
- d. Please refer to other exposures on items "c to e" under Aggregation and Measurement of Exposures of Section 361/341-Q of the MORB/MORNBFI.
- e. Report the value of the protected portion of exposures following the approach under Eligible Credit Risk Mitigation of Section 361/341-Q of the MORB/MORNBFI.
- f. Please refer to the total tier 1 capital as reflected in the Risk-Based Capital Adequacy Ratio Report.
- g. Please cite the type of exclusions or reason for not aggregating based on economic interdependence. For exposures to micro, small and medium enterprises (MSMEs), please report the total amount of exposures only.