



# *Bangko Sentral ng Pilipinas*

## OFFICE OF THE GOVERNOR

**Circular No. 494**  
**Series of 2005**

**Subject: Guidelines on the Adoption of Philippine Financial Reporting Standards and Philippine Accounting Standards**

The Monetary Board in its Resolution Nos. 1110 and 1194 dated 18 August 2005 and 8 September 2005, respectively, approved the following guidelines in adopting the provisions of the Philippine Financial Reporting Standards (PFRS) and Philippine Accounting Standards (PAS) effective the annual financial reporting period beginning 1 January 2005, both for purposes of prudential reporting and audited financial statements.

**Section 1. Statement of Policy.** It is the policy of the Bangko Sentral ng Pilipinas to promote fairness, transparency and accuracy in financial reporting. It is in this light that the BSP aims to adopt all Philippine Financial Reporting Standards (PFRS) and Philippine Accounting Standards (PAS) issued by the Accounting Standards Council (ASC) to the greatest extent possible.

**Section 2. Accounting Treatment for Prudential Reporting.** For prudential reporting, financial institutions shall adopt *in all respect* the PFRS and PAS except as follows:

- (a) In preparing consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Financial/non-financial allied/non-allied associates shall be accounted for using the equity method in accordance with the provisions of PAS 28 "Investments in Associates". For purposes of preparing separate financial statements, financial/non-financial allied/non-allied subsidiaries/associates, including insurance subsidiaries/associates, shall also be accounted for using the equity method; and
- (b) Financial institutions shall be required to meet the BSP recommended valuation reserves.

**PANANALAPING MATATAG, BANSANG PANATAG**

Notwithstanding these exceptions, the audited annual financial statements required to be submitted to the BSP in accordance with the provisions of Subsection X164.1 of the Manual of Regulations for Banks (MORB) and Section 4172Q of the Manual of Regulations for Non-Bank Financial Institutions (MORNBFI) shall *in all respect* be PFRS/PAS compliant: *Provided*, That financial institutions shall submit to the BSP adjusting entries reconciling the balances in the financial statements for prudential reporting with that in the audited annual financial statements.

**Section 3. Accounting Treatment of Specific Items.** The following rules and regulations shall govern the accounting treatment of specific items for purposes of prudential reporting and audited financial statements:

- (a) **Derivatives.** Derivatives shall be accounted in accordance with the provisions of PAS 39 "Financial Instruments: Recognition and Measurement" which states that derivatives shall be reported on balance sheet with any gain or loss from fair value changes reported in profit or loss. Derivatives and non-derivatives financial assets and liabilities qualifying for hedge accounting shall likewise conform with the guidelines of PAS 39.

Accordingly, Appendix 27 of the MORB and Appendix Q-17 of the MORNBFI on the accounting guidelines for derivatives are hereby superseded.

- (b) **Bank/Other Financial Institution Premises, Furniture, Fixture and Equipment.** Bank/ Other financial institution premises, furniture, fixture and equipment shall be accounted for using the cost model under PAS 16 "Property, Plant and Equipment."

Outstanding appraisal increment as of the effectivity of this Circular arising from mergers and consolidation shall be deemed part of the cost of the assets. However, appraisal increment booked in accordance with Subsection X606.1 of the MORB and Subsection 4651Q.1 of the MORNBFI shall be reversed.

Accordingly, Subsection X606.1 of the MORB and Subsection 4651Q.1 of the MORNBFI, which allow the booking of appreciation or increase in the book value of bank/NBQB premises and other fixed assets in cases where the market value of the property has greatly increased since the original purchase subject, among others, to the prior notification to the appropriate supervision and examination departments of the BSP are hereby deleted.

- (c) **Real and Other Properties Acquired (ROPA)**

1. Real and other properties acquired (ROPA) in settlement of loans through foreclosure or dation in payment shall be booked initially at

the carrying amount of the loan (i.e., outstanding loan balance adjusted for any unamortized premium or discount less allowance for probable losses computed based on PAS 39 provisioning requirements) plus booked accrued interest less allowance for probable losses plus transaction costs incurred upon acquisition (such as non-refundable capital gains tax and documentary stamp tax paid in connection with the foreclosure/purchase of the acquired real estate property): *Provided*, That where the booked amount of ROPA exceeds the appraised value of the acquired property, an allowance for probable losses equivalent to the excess of the amount booked over the appraised value shall be set up: *Provided, further*, That if the carrying amount of ROPA exceeds P5 million, the appraisal of the foreclosed/purchased asset shall be conducted by an independent appraiser acceptable to the BSP.

2. The carrying amount of ROPA shall be allocated to land, building, other non-financial assets and financial assets (e.g., receivables from third party or equity interest in an entity) based on their fair values, which allocated carrying amounts shall become their initial costs.
3. Subsequently, ROPA shall be accounted for as follows:
  - (a) Land and buildings shall be accounted for using the cost model under PAS 40 "Investment Property";
  - (b) Other non-financial assets shall be accounted for using the cost model under PAS 16 "Property Plant and Equipment";
  - (c) Buildings and other non-financial assets shall be depreciated over a period not exceeding ten years and three years, respectively.
  - (d) Land, buildings and other non-financial assets shall be subject to the impairment provisions of PAS 36 "Impairment";
  - (e) Financial assets shall be initially booked and classified according to intention (i.e., HFT, DFVPL, AFS, HTM, INMES, Unquoted Debt Securities Classified as Loans or Loans and Receivable) and accounted for in accordance with the provisions of PAS 39;
  - (f) ROPAs that comply with the provisions of PFRS 5 "Non-Current Assets Held for Sale" shall be reclassified and accounted for as such.
4. Claims arising from deficiency judgments rendered in connection with the foreclosure of mortgaged properties shall be lodged under

the real account "Deficiency Judgment Receivable"; while probable claims against the borrower arising from the foreclosure of mortgaged properties shall be lodged under the contingent account "Deficiency Claims Receivable".

5. *Appraisal of Properties.* Before foreclosing or acquiring any property in settlement of loans, it must be properly appraised to determine its true economic value. If the amount of ROPA to be booked exceeds P5 million, the appraisal must be conducted by an independent appraiser acceptable to the BSP. An in-house appraisal of all ROPAs shall be made at least every other year: *Provided*, That immediate re-appraisal shall be conducted on ROPAs which materially decline in value.
6. *Non-Cash Payment for Interest.* Financial institutions that accept non-cash payments for interest on their borrowers' loans shall book the acquired assets as ROPA. The amount to be booked as ROPA shall be the booked accrued interest less allowance for probable losses: *Provided*, That where the booked amount of ROPA exceeds the appraised value of the acquired property, an allowance for probable losses equivalent to the excess of the amount booked over the appraised value shall be set up: *Provided, further*, That if the carrying amount of ROPA exceeds P5 million, the appraisal of the foreclosed/purchased asset shall be conducted by an independent appraiser acceptable to the BSP. The carrying amount of ROPA shall be allocated in accordance with Item (c)2 and shall be subsequently accounted for in accordance with Item (c)3 of this Section.
7. *Sales Contract Receivable (SCR)* shall be recorded based on the present value of the installments receivables discounted at the imputed rate of interest. Discount shall be accreted over the life of the SCR by crediting interest income using the effective interest method. Any difference between the present value of the SCR and the derecognized assets shall be recognized in profit or loss at the date of sale in accordance with the provisions of PAS 18 "Revenue" *Provided, furthermore*, That SCR shall be subject to impairment provision of PAS 39.

Accordingly, Section X611 and Subsections X611.1, X611.2 and X611.3 of the MORB and Section 4109Q and Subsections 4109Q.1, 4109Q.2 and 4109Q.3 of the MORNBF1 on the accounting treatment of ROPA are hereby superseded.

8. *Transitional Provisions.* The provisions of Section 3(c) shall be applied to real and other properties acquired on 1 January 2005 and thereafter. *Provided*: That (a) Section 3(c)3(e) of this Circular shall be immediately adopted for all outstanding financial assets

acquired before 1 January 2005; and (b) Section 3(c)7 of this Circular shall be immediately adopted for all outstanding Sales Contract Receivables entered into before 1 January 2005. *Provided, further,* That all land, buildings and other non-financial assets acquired before 1 January 2005 shall continue to be provided with valuation reserves in accordance with the schedule in Appendix 18 of the MORB and Appendix Q-10 of the MORNBFi.

- (d) **Goodwill.** Goodwill shall be accounted for in accordance with the provisions of PFRS 3 "Business Combination", and shall be subject to impairment provisions of PAS 36 "Impairment". In this regard, financial institutions with outstanding goodwill arising from mergers and consolidation approved by the Monetary Board shall apply PFRS 3 prospectively. Therefore the financial institution shall:

1. beginning the annual period beginning on 1 January 2005 shall discontinue amortizing such goodwill;
2. at the beginning of the annual period beginning on 1 January 2005, eliminate the carrying amount of the related accumulated amortization with a corresponding decrease in goodwill; and
3. from the beginning of the first annual period beginning on 1 January 2005 test the goodwill for impairment in accordance with PAS 36.

Accordingly Subsection X112.e of the MORB and Appendix 4112Q.e of the MORNBFi are hereby deleted.

- (e) **Foreign Exchange Transactions.** Foreign exchange transactions shall be accounted for in accordance with the provisions of PAS 21 "Effects of Changes in Foreign Exchange Rates". In this regard, revaluation of foreign currency monetary items shall be done at least monthly, using the Philippine Dealing System (PDS) Peso/US Dollar closing rate and the New York US Dollar/Third currencies closing rates. Foreign borrowings booked under bills payable, the foreign exchange risk of which is shouldered by the National Government and past due accounts shall be revalued in accordance with the provisions of PAS 21.

- (f) **Redeemable Preferred Shares.** Redeemable preferred shares and preferred shares of similar nature shall be accounted for as a liability or equity instrument in accordance with the provisions of PAS 32 "Financial Instruments: Disclosure and Presentation." For this purpose, mandatorily redeemable preferred shares and preferred shares of similar nature accounted for as a financial liability shall be booked as a debt instrument in the books of both the issuer and the investor.

- (g) **Interest Accrual on Past Due Loans.** Interest income on past due loans arising from discount amortization (and not from the contractual interest of the accounts) shall be accrued as provided in PAS 39.

Accordingly, Subsections X305.4 and X320.5 of the MORB and Subsections 4307Q.7, 4311Q.2 and 4301N.5 are hereby amended.

- (h) **Fair Value Option.** The use of the fair value option in accordance with the criteria set forth in the amendments to PAS 39 shall be allowed subject to the following conditions:

1. Financial institutions shall have in place appropriate risk management systems (including related risk management policies, procedures and controls) prior to initial application of the fair value option for a particular activity or purpose and on an ongoing basis;
2. Financial institutions shall apply the fair value option only to instruments for which fair values can be reliably estimated; and
3. Financial institutions shall provide BSP with supplemental information as may be necessary, to enable BSP to assess the impact of the financial institution's utilization of the fair value option.

- (i) **Other Clarifications on Circular No. 476 dated 16 February 2005**

1. Only quoted debt securities can be classified under HTM. Unquoted debt securities that are not classified as HFT nor DFVPL nor AFS or other than those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as AFS, may be booked under the account Unquoted Debt Securities Classified as Loans.

Accordingly, securities held in compliance with BSP regulations may likewise be classified under the said account.

2. Credit Linked Notes (CLNs) may be booked under HFT or DFVPL or if the embedded derivative is separated from the host instrument, under AFS, but not under HTM nor Unquoted Debt Securities Classified as Loans.
3. A *puttable bond* (i.e., a debt security with an embedded put option giving the holder of the note the right to require the issuer to repay or redeem the security before maturity) cannot be classified under HTM.
4. A debt security that is *callable by the issuer* can generally be classified as HTM as long as the holder intends and is able to hold the security until it is called or until maturity. However, the holder is

precluded from classifying the said callable bond under HTM, if the holder would not be able to recover substantially all of the carrying amount of its investment.

5. Quoted loans and receivables shall be classified as debt securities which may be booked under HFT, DFVPL, AFS or HTM.

**Section 4.** The following sections of the MORB/MORNBFI are likewise hereby amended:

- (a) **Subsections X161.2 of the MORB and Subsections 4161Q.2/4161S.2/ 4161P.2 of the MORNBFI.** *Philippine Financial Reporting Standards/Philippine Accounting Standards*

"Banks/Financial institutions shall adopt the Philippine Financial Reporting Standards (PFRS) and Philippine Accounting Standards (PAS) which are in accordance with generally accepted accounting principles in recording transactions and in the preparation of financial statements and reports to BSP. However, in cases where there are differences between BSP regulations and PFRS/PAS as when more than one (1) option are allowed or certain maximum or minimum limits are prescribed by the PFRS/PAS, the option or limit prescribed by BSP regulations shall be adopted by all banks/financial institutions.

"For purposes hereof, the PFRS/PAS shall refer to issuances of the Accounting Standards Council and approved by the Professional Regulation Commission."

- (b) 1. **Subsection X162.9 of the MORB.** *Publication, Posting of Statement of Condition.*

"x x x.

"a(1)(a) The CSOC of the banks and its subsidiaries and associates shall conform with the guidelines of PAS 27 "Consolidated and Separate Financial Statements", except that for purposes of consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Financial/non-financial allied/non-allied associates shall be accounted for using the equity method in accordance with the provisions of PAS 28 "Investments in Associates". For purposes of separate financial statements, investments in financial/non-financial allied/non-allied subsidiaries/associates, including insurance subsidiaries/associates, shall be accounted for using the equity method. x x x"

## 2. Section 4181Q of the MORNBFJ. *Publication Requirements.*

"The quarterly consolidated statement of condition of an NBQB/trust entity and its subsidiaries and associates shall be published side-by-side with the statement of condition of its head office and its branches/other offices as of such dates as the BSP may require, within twenty (20) working days from receipt of call letter, in any newspaper of general circulation in the country in the prescribed format.

"The consolidated statement of condition of an NBQB/trust entity and its subsidiaries and associates shall conform with the guidelines of PAS 27 "Consolidated and Separate Financial Statements", except that for purposes of consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Financial/non-financial allied/non-allied associates shall be accounted for using the equity method in accordance with the provisions of PAS 28 "Investments in Associates". For purposes of separate financial statements, investments in financial/non-financial allied /non-allied subsidiaries/associates, including insurance subsidiaries/associates, shall be accounted for using the equity method.

"a. The following information shall be disclosed in the Statements of Condition : x x x."

Appendix Q-3-b of the MORNBFJ is hereby deleted.

### (c) **Subsection X162.10 of the MORB. *Consolidated financial statements of banks and their subsidiaries engaged in financial allied undertakings.***

" x x x For purposes of this Subsection, the consolidated financial statements shall conform to the guidelines of PAS 27 "Consolidated and Separate Financial Statements" except that for purposes of consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Financial/non-financial allied/ non-allied associates shall be accounted for using the equity method in accordance with the provisions of PAS 28 "Investments in Associates". x x x"

Appendix 9 of the MORB is hereby deleted.

(d) **Subsections X164.2 of the MORB and 4172Q.1 of the MORNBF.**  
***Posting of Audited Financial Statements.***

" x x x shall post in a conspicuous place in all their branches and other banking offices, their latest audited financial statements consisting of the following:

- (a) Balance Sheet;
- (b) Income Statement;
- (c) Statement of Changes in Equity;
- (d) Cash Flow Statement;
- (e) Notes to Financial Statements, which shall include, among other things, disclosure of the volume of past due loans as well as loan-loss provisions; and
- (f) Auditor's Opinion."

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

**FOR THE MONETARY BOARD:**

  
**AMANDO M. TETANGCO, JR.**  
**Governor**

20 September 2005