



Bangko Sentral ng Pilipinas
MAYNILA, PILIPINAS

**OFFICE OF THE DEPUTY GOVERNOR
SUPERVISION AND EXAMINATION SECTOR**

MEMORANDUM NO. M - 2010-037

TO : ALL BANKS AND NON-BANK FINANCIAL INSTITUTIONS

SUBJECT: Moratorium on the Approval of Hybrid Tier 1, Tier 2 and Other Redeemable Capital Instruments

The Monetary Board has taken notice of changes being proposed by the oversight body of the Basel Committee on Banking Supervision, the Group of Central Bank Governors and Heads of Supervision, that announced at its 12 September 2010 meeting agreements that comprise key facets of what is commonly referred to today as Basel 3.

1. The agreements tightened the definition of instruments that would be eligible as bank capital and formalized the policy intention for banks to rely more on common equity in complying with the minimum capital adequacy ratio.
2. The reforms of the market architecture leaves the possibility that Tier 1 and Tier 2 instruments may still qualify as bank capital in the future. To distinguish against existing instruments, enhanced variants of Tier 1 and Tier 2 are envisioned to comply with more stringent requirements that will be uniformly defined across jurisdictions. This facet of the reform agenda, however, is still being finalized.
3. In general, Tier 1 instruments will be defined as those with complete ability to absorb losses while the bank retains full discretion over dividends. This will principally be common equity but would also include retained earnings and selected reserve accounts while deducting other accounts such as intangibles and goodwill.
4. The distinction between upper and lower Tier 2 capital will be removed. As proposed, all Tier 2 capital will need to meet certain minimum standards which include, among others, being subordinated to depositors and general creditors, have an original maturity of at least 5 years with no incentive to be redeemed. Additional features have been proposed to apply to systemically

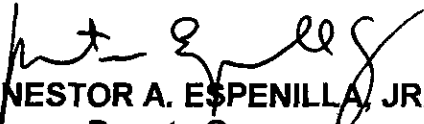
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important banks to ensure loss-absorbency at the point of "non-viability". A consultative document has been issued for the proposed additional features but no timetable has been set.

5. Under current BSP guidelines, Hybrid Tier 1 (i.e., perpetual preferred stock and perpetual unsecured subordinated debt) fall under Tier 1 capital that would not be part of common equity. In addition, redeemable capital instruments (i.e., unsecured subordinated debt and other lower Tier 2 capital) are categorized as Tier 2.
6. Existing capital accounts which do not meet the tighter definition under the Basel 3 agreement may be phased out over a ten (10) year period, if issued before 12 September 2010. Those issued after this cut-off date will not be eligible for the phase out period and will no longer qualify as capital.

To avoid the unwarranted uncertainty with the adoption of the Basel 3 reform package *en toto*, a moratorium on approvals of Hybrid Tier 1, Tier 2 and/or other redeemable capital instruments is hereby imposed effective immediately. The moratorium shall be in effect until December 31, 2010 to allow for the formulation of revised capital definitions applicable to banks and other financial institutions under BSP supervision. Issuers of potentially non-compliant capital instruments that are approved but still unissued to date are advised to defer their issuance to ensure conformity to forthcoming revised capital guidelines and hence their eligibility as regulatory capital.

For information and guidance.


NESTOR A. ESPENILLA, JR.
Deputy Governor

21 October 2010