



Bangko Sentral ng Pilipinas
MAYNILA, PILIPINAS

OFFICE OF THE GOVERNOR

Circular No. 688
Series of 2010

**Subject: Revised Risk-Based Capital Adequacy Framework
For Stand-Alone Thrift Banks, Rural Banks and Cooperative Banks**

The Monetary Board, in its Resolution No. 660 dated 13 May 2010, approved the attached guidelines implementing the Revised Risk-Based Capital Adequacy Framework for stand-alone thrift banks, rural banks and cooperative banks.

The appropriate risk-based Capital Adequacy Ratio (CAR) Report Forms shall be covered by a separate issuance.

Pilot runs of the CAR Reports based on the revised framework shall be conducted starting with the end-December 2010 report until end-December 2011 report.

This Circular shall take effect on 1 January 2012.

FOR THE MONETARY BOARD:

AMANDO M. TETANGCO, JR.
Governor

26 May 2010

Att: A/S

PANANALAPING MATATAG, BANSANG PANATAG

**RISK-BASED CAPITAL ADEQUACY FRAMEWORK
FOR STAND-ALONE THRIFT BANKS, RURAL BANKS
AND COOPERATIVE BANKS¹**

Part I. Risk-Based Capital Adequacy Ratio

1. The risk based capital adequacy ratio (CAR) of stand-alone thrift banks (TBs), rural banks (RBs) and Cooperative Banks (Coop Banks), or collectively, "banks", expressed as a percentage of qualifying capital to risk-weighted assets, shall not be less than 10%.
2. Qualifying capital is computed in accordance with the provisions of Part II. Risk weighted assets is the sum of (1) credit risk-weighted assets (Part III), and (2) operational risk-weighted assets (Part IV): *Provided, That banks that shall engage in derivatives activities as end-user for hedging purpose and/or under a Type 3-Limited User Authority granted pursuant to the provisions of Circular No. 594 dated 8 January 2008, shall likewise include counterparty credit risk-weighted assets and/or market risk-weighted assets relative to such exposures, which shall be computed based on the relevant provisions of The Revised Risk-Based Capital Adequacy Framework for the Philippine Banking System issued under Circular No. 538 dated 4 August 2006, as amended.*
3. The CAR requirement will be applied to all stand-alone TBs, RBs and Coop Banks on both solo and consolidated bases, as applicable. The application of the requirement on a consolidated basis is the best means to preserve the integrity of capital in banks with subsidiaries by eliminating double gearing. However, as one of the principal objectives of supervision is the protection of depositors, it is essential to ensure that capital recognized in capital adequacy measures is readily available for those depositors. Accordingly, individual banks should likewise be adequately capitalized on a stand-alone basis.
4. To the greatest extent possible, all banking and other relevant financial activities (both regulated and unregulated) conducted by a bank and its subsidiaries will be captured through consolidation. Thus, majority-owned or controlled financial allied undertakings (i.e., RBs and venture capital corporations (VCCs) for TBs, and RBs for Coop Banks) should be fully consolidated on a line-by-line basis. Exemptions from consolidation shall only be made in cases where such holdings are acquired through debt previously contracted and held on a temporary basis, are subject to different regulation, or where non-consolidation for regulatory capital purposes is otherwise required by law. All cases of exemption from consolidation must be made with prior clearance from the BSP.
5. Banks shall comply with the minimum CAR at all times notwithstanding that supervisory reporting shall only be on quarterly basis. Any breach, even if only

¹ These refer to TBs, RBs, and Coop Banks that are not subsidiaries of universal banks (UBs) and commercial banks (KBs).

temporary, shall be reported to the bank's Board of Directors and to BSP-Supervision and Examination Sector (SES) within 3 banking days. For this purpose, these banks shall develop an appropriate system to properly monitor their compliance.

6. The BSP reserves the right, upon authority of the Deputy Governor-SES, to conduct on-site inspection outside of regular or special examination, for the purpose of ascertaining the accuracy of CAR calculations as well as the integrity of CAR monitoring and reporting systems.

Part II. Qualifying Capital

1. Qualifying capital consists of Tier 1 (core plus hybrid) capital and Tier 2 (supplementary) capital elements, net of required deductions from capital.

A. Tier 1 Capital

2. Tier 1 capital is the sum of core Tier 1 capital and allowable amount of hybrid Tier 1 capital, as set in paragraph 11.
3. Core Tier 1 capital consists of:

- a) Paid-up common stock;
- b) Paid-up perpetual and non-cumulative preferred stock;
- c) Additional paid-in capital;
- d) Retained earnings;
- e) Undivided profits;
- f) Net gains on fair value adjustment of hedging instruments in a cash flow hedge of available for sale equity securities;
- g) Cumulative foreign currency translation; and
- h) Minority interest in subsidiary financial allied undertakings (i.e., RBs and VCCs for TBs, and RBs for Coop Banks) which are less than wholly-owned: *Provided*, That a bank shall not use minority interests in the equity accounts of consolidated subsidiaries as an avenue for introducing into its capital structure elements that might not otherwise qualify as Tier 1 capital or that would, in effect, result in an excessive reliance on preferred stock within Tier 1:

Less:

- i. Common stock treasury shares;
- ii. Perpetual and non-cumulative preferred stock treasury shares;
- iii. Net unrealized losses on available for sale equity securities purchased;
- iv. Unbooked valuation reserves and other capital adjustments based on the latest report of examination as approved by the Monetary Board;

- v. Total outstanding unsecured credit accommodations, both direct and indirect, to directors, officers, stockholders and their related interests (DOSRI), net of allowance for credit losses;
 - vi. Total outstanding unsecured loans, other credit accommodations and guarantees granted to subsidiaries and affiliates, net of allowance for credit losses;
 - vii. Deferred tax asset, net of deferred tax liability: Provided, That the conditions to offset under PAS 12 are met: Provided, further, That any excess of deferred tax liability over deferred tax asset (i.e., net deferred tax liability) shall not be added to Tier 1 capital; and
 - viii. Goodwill, net of allowance for losses, including that relating to unconsolidated subsidiary RBs and VCCs for TBs, and RBs for Coop Banks (on solo basis) and unconsolidated non-financial allied undertakings (on solo and consolidated bases).
4. Hybrid Tier 1 capital in the form of perpetual preferred stock and perpetual unsecured subordinated debt may be issued subject to prior BSP approval and to the conditions in paragraph 11.

B. Tier 2 Capital

5. Tier 2 capital is the sum of upper Tier 2 capital and lower Tier 2 capital.
6. The total amount of lower Tier 2 capital before deductions enumerated in paragraph 9 that may be included in total Tier 2 capital shall be limited to a maximum of 50% of total Tier 1 capital (net of deductions enumerated in paragraph 3). The total amount of upper and lower Tier 2 capital both before deductions enumerated in paragraph 9 that may be included in total qualifying capital shall be limited to a maximum of 100% of total Tier 1 capital (net of deductions enumerated in paragraph 3).
7. Upper Tier 2 capital consists of:
- a) Paid-up perpetual and cumulative preferred stock;
 - b) Paid-up limited life redeemable preferred stock issued with the condition that redemption thereof shall be allowed only if the shares redeemed are replaced with at least an equivalent amount of newly paid-in shares so that the total paid-in capital stock is maintained at the same level prior to redemption;
 - c) Appraisal increment reserve – bank premises, as authorized by the Monetary Board;
 - d) Net unrealized gains on available for sale equity securities purchased subject to a 55% discount;
 - e) General loan loss provision, limited to a maximum of 1% of total credit risk-weighted assets, and any amount in excess thereof shall be deducted from the total credit risk-weighted assets in computing the denominator of the risk-based capital ratio;

- f) With prior BSP approval, unsecured subordinated debt with a minimum original maturity of at least ten (10) years, issued subject to the conditions in paragraph 12, in an amount equivalent to its carrying amount discounted by the following rates:

Remaining maturity	Discount factor
5 years & above	0%
4 years to <5 years	20%
3 years to <4 years	40%
2 years to <3 years	60%
1 year to <2 years	80%
< 1 year	100%

- g) Deposit for common stock subscription;
h) Deposit for perpetual and non-cumulative preferred stock subscription; and
i) Hybrid Tier 1 capital as defined in paragraph 4 in excess of the maximum allowable limit of 15% of total Tier 1 capital (net of deductions enumerated in paragraph 3):

Less:

- i. Perpetual and cumulative preferred stock treasury shares;
- ii. Limited life redeemable preferred stock treasury shares with the replacement requirement upon redemption;
- iii. Sinking fund for redemption of limited life redeemable preferred stock with the replacement requirement upon redemption; and
- iv. Net losses in fair value adjustment of hedging instruments in a cash flow hedge of available for sale equity securities.

8. Lower Tier 2 capital consists of:

- a) Paid-up limited life redeemable preferred stock without the replacement requirement upon redemption in an amount equivalent to its carrying amount discounted by the following rates:

Remaining maturity	Discount factor
5 years & above	0%
4 years to <5 years	20%
3 years to <4 years	40%
2 years to <3 years	60%
1 year to <2 years	80%
< 1 year	100%

- b) With prior BSP approval, unsecured subordinated debt with a minimum original maturity of at least five (5) years, issued subject to the conditions in paragraph 13, in an amount equivalent to its carrying amount discounted by the following rates:

Remaining maturity	Discount factor
5 years & above	0%
4 years to <5 years	20%
3 years to <4 years	40%
2 years to <3 years	60%
1 year to <2 years	80%
< 1 year	100%

- c) Deposit for perpetual and cumulative preferred stock subscription; and
- d) Deposit for limited life redeemable preferred stock subscription with the replacement requirement upon redemption;

Less:

- i. Limited life redeemable preferred stock treasury shares without the replacement requirement upon redemption; and
- ii. Sinking fund for redemption of limited life redeemable preferred stock without the replacement requirement upon redemption up to the extent of the balance of redeemable preferred stock after applying the cumulative discount factor.

C. Deductions from the total of Tier 1 and Tier 2 capital

9. The following items should be deducted 50% from Tier 1 and 50% from Tier 2 capital: *Provided*, That the amount to be deducted from Tier 2 capital shall be limited to its balance and any excess thereof shall be deducted from Tier 1 capital:
 - a) Investments in equity of unconsolidated subsidiary RBs and VCCs for TBs, and RBs for Coop Banks, after deducting related goodwill, if any (for solo basis);
 - b) Investments in other regulatory capital instruments of unconsolidated subsidiary RBs for Coop Banks (for solo basis);
 - c) Investments in equity of unconsolidated subsidiary non-financial allied undertakings, after deducting related goodwill, if any (for both solo and consolidated bases);
 - d) Significant minority investments (20%-50% of voting stock) in banks and other financial allied undertakings (for both solo and consolidated bases); and
 - e) Reciprocal investments in equity/other regulatory capital instruments of other banks/quasi-banks/enterprises.
10. Any asset deducted from qualifying capital in computing the numerator of the risk-based capital ratio shall not be included in the total risk-weighted assets in computing the denominator of the ratio. Available for sale debt securities shall be risk-weighted net of allowance for credit losses, but without considering accumulated market gains/(losses).

D. Eligible instruments under hybrid Tier 1 capital

11. Perpetual preferred stock and perpetual unsecured subordinated debt issuances of banks should comply with the following minimum conditions in order to be eligible as hybrid Tier 1 (HT1) capital:

- a) It must be issued and fully paid-up. Only the net proceeds received from the issuance shall be included as capital;
- b) The dividends/coupons must be non-cumulative. It is acceptable to pay dividends/coupons in scrip or shares of stock if a cash dividend/coupon is withheld: *Provided*, That this does not result to issuing lower quality capital: *Provided, further*, That where such dividend/coupon stock settlement feature is included, the bank should ensure that it has an appropriate buffer of authorized capital stock and appropriate stockholders and board authorization, if necessary, to fulfill their potential obligations under such issues;
- c) It must be available to absorb losses of the bank without it being obliged to cease carrying on business. The agreement governing its issuance should specifically provide for the dividend/coupon and principal to absorb losses where the bank would otherwise be insolvent, or for its holders to be treated as if they were holders of a specified class of share capital in any proceedings commenced for the winding up of the bank. Issue documentation must disclose to prospective investors the manner by which the instrument is to be treated in loss situation.

Alternatively, the agreement governing its issuance can provide for automatic conversion into common shares or perpetual and noncumulative preferred shares upon occurrence of certain trigger events, as follows:

- i. Breach of minimum capital ratio;
- ii. Commencement of proceedings for winding up of the bank; or
- iii. Upon appointment of receiver for the bank.

The rate of conversion must be fixed at the time of subscription to the instrument. The bank must also ensure that it has appropriate buffer of authorized capital stock and appropriate stockholders and board authorization for conversion/issue to take place anytime;

- d) Its holders must not have a priority claim, in respect of principal and dividend/coupon payments in the event of winding up of the bank, which is higher than or equal with that of depositors, other creditors of the bank and holders of lower Tier 2 (LT2) and upper Tier 2 (UT2) capital instruments. Its holder must waive his/its right to set-off any amount he/it owes the bank against any subordinated amount owed to him/it due to the HT1 capital instrument;

- e) It must neither be secured nor covered by a guarantee of the issuer or related party or other arrangement that legally or economically enhances the priority of the claim of any holder as against depositors, other creditors of the bank and holders of LT2 and UT2 capital instruments;
- f) It must not be redeemable at the initiative of the holder. It must not be repayable without the prior approval of the BSP: *Provided*, That repayment may be allowed only in connection with call option after a minimum of five (5) years from issue date: *Provided*, however, That a call option may be exercised within the first five (5) years from issue date when:
 - i. It was issued for the purpose of a merger with or acquisition by the bank and the merger or acquisition is aborted;
 - ii. There is a change in tax status of the HT1 capital instrument due to changes in the tax laws and/or regulations; or
 - iii. It does not qualify as HT1 capital as determined by the BSP:

Provided, further, That such repayment shall be approved by the BSP only if the preferred share/debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue, unless the bank's capital ratio remains more than adequate after redemption.

It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency. The agreement governing its issuance must not contain any provision that mandates or creates an incentive for the bank to repay the outstanding principal of the instrument, e.g., a cross-default or negative pledge or a restrictive covenant, other than a call option which may be exercised by the bank;

- g) Its main features must be publicly disclosed by annotating the same on the instrument and in a manner that is easily understood by the investor;
- h) The proceeds of the issuance must be immediately available without limitation to the bank;
- i) The bank must have full discretion over the amount and timing of dividends/coupons where the bank:
 - i. Has not paid or declared a dividend on its common shares in the preceding financial year; or
 - ii. Determines that no dividend is to be paid on such shares in the current financial year.

The bank must have full control and access to waived payments;

- j) Any dividend/coupon to be paid must be paid only to the extent that the bank has profits distributable determined in accordance with existing BSP regulations. The dividend/coupon rate, or the formulation for calculating dividend/coupon payments must be fixed at the time of issuance and must not be linked to the credit standing of the bank;

- k) It may allow only one (1) moderate step-up in the dividend/coupon rate in conjunction with a call option, only if the step-up occurs at a minimum of ten (10) years after the issue date and if it results in an increase over the initial rate that is not more than:
 - i. 100 basis points less the swap spread between the initial index basis and the stepped-up index basis; or
 - ii. 50% of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis.

The swap spread should be fixed as of the pricing date and reflect the differential in pricing on that date between the initial reference security or rate and the stepped-up reference security or rate.

- l) It must be underwritten by a third party not related to the issuer bank nor acting in reciprocity for and in behalf of the issuer bank;
- m) It must be issued in minimum denominations of at least five hundred thousand pesos (P500,000.00) or its equivalent;
- n) It must clearly state on its face that it is not a deposit and is not insured by the Philippine Deposit Insurance Corporation (PDIC); and
- o) The bank must submit a written external legal opinion that the abovementioned requirements, including the subordination and loss absorption features, have been met.

Provided, That for purposes of reserve requirement regulation, it shall not be treated as time deposit liability, deposit substitute liability or other forms of borrowings: *Provided, further*, That the total amount of HT1 capital that may be included in the Tier 1 capital shall be limited to a maximum of 15% of total Tier 1 capital (net of deductions enumerated in paragraph 3). *Provided, furthermore*, That the amount of HT1 capital in excess of the maximum limit shall be eligible for inclusion in UT2 capital, subject to the limit in total Tier 2 capital. To determine the allowable amount of HT1 capital, the amount of total core Tier 1 capital (net of deductions enumerated in paragraph 3) should be multiplied by 17.65%, the number derived from the proportion of 15% to 85% (i.e., $15\%/85\% = 17.65\%$): *Provided, finally*, That where it is denominated in foreign currency, it shall be revalued in accordance with PAS 21.

E. Eligible unsecured subordinated debt

- 12. Unsecured subordinated debt issuances by banks should comply with the following minimum conditions in order to be eligible as upper Tier 2 (UT2) capital:
 - a) It must be issued and fully paid-up. Only the net proceeds received from the issuance shall be included as capital;

- b) It must be available to absorb losses of the bank without it being obliged to cease carrying on business. The agreement governing its issuance should specifically provide for the coupon and principal to absorb losses where the bank would otherwise be insolvent, or for its holders to be treated as if they were holders of a specified class of share capital in any proceedings commenced for the winding up of the bank. Issue documentation must disclose to prospective investors the manner by which the instrument is to be treated in loss situation.

Alternatively, the agreement governing its issuance can provide for automatic conversion into common shares or perpetual and non-cumulative shares or perpetual and cumulative preferred shares upon occurrence of certain trigger events, as follows:

- i. Breach of minimum capital ratio;
- ii. Commencement of proceedings for winding up of the bank; or
- iii. Upon appointment of receiver for the bank.

The rate of conversion must be fixed at the time of subscription to the instrument. The bank must also ensure that it has appropriate buffer of authorized capital stock and appropriate stockholders and board authorization for conversion/issue to take place anytime;

- c) Its holders must not have a priority claim, in respect of principal and coupon payments of the UT2 in the event of winding up of the bank, which is higher than or equal with that of depositors, other creditors of the bank, and holders of LT2 capital instruments. Its holder must waive his/its right to set-off any amount he/it owes the bank against any subordinated amount owed to him/it due to the UT2 capital instrument;
- d) It must neither be secured nor covered by a guarantee of the issuer or related party or other arrangement that legally or economically enhances the priority of the claim of any holder as against depositors, other creditors of the bank and holders of LT2 capital instruments;
- e) It must not be redeemable at the initiative of the holder. It must not be repayable prior to maturity without the prior approval of the BSP: *Provided*, That repayment may be allowed only in connection with call option after a minimum of five (5) years from issue date: *Provided, however*, That a call option may be exercised within the first five (5) years from issue date when:
- i. It was issued for the purpose of a merger with or acquisition by the bank and the merger or acquisition is aborted;
 - ii. There is a change in tax status of the UT2 capital instrument due to changes in the tax laws and/or regulations; or
 - iii. It does not qualify as UT2 capital as determined by the BSP:

Provided, further, That such repayment prior to maturity shall be approved by the BSP only if the debt is simultaneously replaced with issues of new capital

which is neither smaller in size nor of lower quality than the original issue, unless the bank's capital ratio remains more than adequate after redemption,

It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency. The agreement governing its issuance must not contain any provision that mandates or creates an incentive for the bank to repay the outstanding principal of the instrument, e.g., a cross-default or negative pledge or a restrictive covenant, other than a call option which may be exercised by the bank;

- f) Its main features must be publicly disclosed by annotating the same on the instrument and in a manner that is easily understood by the investor;
- g) The proceeds of the issuance must be immediately available without limitation to the bank;
- h) The bank must have the option to defer any coupon payment where the bank:
 - i. Has not paid or declared a dividend on its common shares in the preceding financial year; or
 - ii. Determines that no dividend is to be paid on such shares in the current financial year;

It is acceptable for the deferred coupon to bear interest but the interest rate payable must not exceed market rates;

- i) The coupon rate, or the formulation for calculating coupon payments must be fixed at the time of issuance and must not be linked to the credit standing of the bank;
- j) It may allow only one (1) moderate step-up in the coupon rate in conjunction with a call option, only if the step-up occurs at a minimum of ten (10) years after the issue date and if it results in an increase over the initial rate that is not more than:
 - i. 100 basis points less the swap spread between the initial index basis and the stepped-up index basis; or
 - ii. 50% of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis.

The swap spread should be fixed as of the pricing date and reflect the differential in pricing on that date between the initial reference security or rate and the stepped-up reference security or rate;

- k) It must be underwritten or purchased by a third party not related to the issuer bank nor acting in reciprocity for and in behalf of the issuer bank;
- l) It must be issued in minimum denominations of at least five hundred thousand pesos (P500,000.00) or its equivalent;

m) It must clearly state on its face that it is not a deposit and is not insured by the Philippine Deposit Insurance Corporation (PDIC); and

n) The bank must submit a written external legal opinion that the abovementioned requirements, including the subordination and loss absorption features, have been met: *Provided*, That it shall be subject to a cumulative discount factor of 20% per year during the last five (5) years to maturity (i.e., 20% if the remaining life is 4 years to less than 5 years, 40% if the remaining life is 3 years to less than 4 years, etc.): *Provided, further*, That where it is denominated in a foreign currency, it shall be revalued in accordance with PAS 21: *Provided, furthermore*, That for purposes of reserve requirement regulation, it shall not be treated as time deposit liability, deposit substitute liability or other forms of borrowings;

13. Unsecured subordinated debt issuances banks should comply with the following minimum conditions in order to be eligible as lower Tier 2 (LT2) capital:

a) It must be issued and fully paid-up. Only the net proceeds received from the issuance shall be included as capital;

b) Its holders must not have a priority claim, in respect of principal and coupon payments in the event of winding up of the bank, which is higher than or equal with that of depositors and other creditors of the bank. Its holder must waive his/its right to set-off any amount he/it owes the bank against any subordinated amount owed to him/it due to the LT2 capital instrument;

c) It must neither be secured nor covered by a guarantee of the issuer or related party or other arrangement that legally or economically enhances the priority of the claim of any holder as against depositors and other creditors of the bank;

d) It must not be redeemable at the initiative of the holder. It must not be repayable prior to maturity without the prior approval of the BSP: *Provided*, That repayment may be allowed only in connection with call option after a minimum of five (5) years from issue date: *Provided, however*, That a call option may be exercised within the first five (5) years from issue date when:

- i. It was issued for the purpose of a merger with or acquisition by the bank and the merger or acquisition is aborted;
- ii. There is a change in tax status of the LT2 capital instrument due to changes in the tax laws and/or regulations; or
- iii. It does not qualify as LT2 capital as determined by the BSP:

Provided, further, That such repayment prior to maturity shall be approved by the BSP only if the debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue, unless the bank's capital ratio remains more than adequate after redemption.

It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency. The agreement governing the

issuance must not contain any provision that mandates or creates an incentive for the bank to repay the outstanding principal of the instrument, e.g., a cross-default or negative pledge or a restrictive covenant other than a call option which may be exercised by the bank;

- e) Its main features must be publicly disclosed by annotating the same on the instrument and in a manner that is easily understood by the investor;
- f) The proceeds must be immediately available without limitation to the bank;
- g) The coupon rate, or the formulation for calculating coupon payments must be fixed at the time of issuance and must not be linked to the credit standing of the bank;
- h) It may allow only one (1) moderate step-up in the coupon rate in conjunction with a call option, only if the step-up occurs at a minimum of five (5) years after the issue date and if it results in an increase over the initial rate that is not more than:
 - i. 100 basis points less the swap spread between the initial index basis and the stepped-up index basis; or
 - ii. 50% of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis;

The swap spread should be fixed as of the pricing date and reflect the differential in pricing on that date between the initial reference security or rate and the stepped-up reference security or rate.

- i) It must be underwritten or purchased by a third party not related to the issuer bank nor acting in reciprocity for and in behalf of the issuer bank;
- j) It must be issued in minimum denominations of at least five hundred thousand pesos (P500,000.00) or its equivalent;
- k) It must clearly state on its face that it is not a deposit and is not insured by the Philippine Deposit Insurance Corporation (PDIC); and
- l) The bank must submit a written external legal opinion that the abovementioned requirements, including the subordination feature have been met: *Provided*, That it shall be subject to a cumulative discount factor of 20% per year during the last five (5) years to maturity (i.e., 20% if the remaining life is 4 years to less than 5 years, 40% if the remaining life is 3 years to less than 4 years, etc.): *Provided, further*, That where it is denominated in a foreign currency, it shall be revalued in accordance with PAS 21: *Provided, furthermore*, That for purposes of reserve requirement regulation, it shall not be treated as time deposit liability, deposit substitute liability or other forms of borrowings.

Part III. Credit Risk-Weighted Assets

1. Credit risk-weighted assets shall be determined by assigning risk weights to amounts of on-balance sheet assets and to credit equivalent amounts of off-balance sheet items and for banks that shall engage in derivatives activities as end-user for hedging purpose and/or under a Type 3-Limited User Authority granted pursuant to the provisions of Circular No. 594 dated 8 January 2008, inclusive of derivative contracts: *Provided*, That the following shall be deducted from the total credit risk-weighted assets:
 - a) General loan loss provision (in excess of the amount permitted to be included in upper Tier 2 capital); and
 - b) Unbooked valuation reserves and other capital adjustments affecting asset accounts based on the latest report of examination as approved by the Monetary Board.

A. On-Balance Sheet Assets

2. The risk-weighted amount shall be the product of the net carrying amount of the asset and the risk weight associated with that asset. Net carrying amount shall refer to the outstanding balance of the account inclusive of unamortized discount/(premium) and accumulated market gains/(losses), and net of allowance for credit losses: *Provided*, That for available for sale debt securities, any accumulated market gains/(losses) shall be deducted/added back as stated in paragraph 10 of Part II.

a) 0% risk weight –

- i. Cash on hand (including foreign currency notes and coins on hand acceptable as international reserves);
- ii. Peso-denominated claims on or portions of claims guaranteed by or collateralized by peso-denominated securities issued by the Philippine National Government and the BSP;
- iii. Claims on or portions of claims guaranteed by or collateralized by securities issued by central governments and central banks of foreign countries with the highest credit quality as defined in Part VI;
- iv. Claims on or portions of claims guaranteed by or collateralized by securities issued by multilateral development banks with the highest credit quality as defined in Part VI;
- v. Loans to the extent covered by hold-out on, or assignment of deposits/deposit substitutes maintained with the lending bank;
- vi. Loans or acceptances under letters of credit to the extent covered by margin deposits;
- vii. Peso-denominated special time deposit loans to the extent guaranteed by Industrial Guarantee and Loan Fund (IGLF);

- viii. Peso-denominated real estate mortgage loans to the extent guaranteed by the Home Guaranty Corporation (HGC); and
- ix. Peso-denominated loans to the extent guaranteed by the Trade and Investment Development Corporation of the Philippines (TIDCORP).

b) 20% risk weight –

- i. Checks and other cash items (including foreign currency checks and other cash items denominated in currencies acceptable as international reserves);
- ii. Claims on or portions of claims guaranteed by or collateralized by securities issued by local government units (LGUs) with the highest credit quality as defined in Part VI;
- iii. Claims on or portions of claims guaranteed by or collateralized by securities issued by non-central government public sector entities of foreign countries with the highest credit quality as defined in Part VI;
- iv. Claims on or portions of claims guaranteed by Philippine incorporated banks/quasi-banks with the highest credit quality as defined in Part VI;
- v. Claims on or portions of claims guaranteed by foreign incorporated banks with the highest credit quality as defined in Part VI;
- vi. Interbank call loans;
- vii. Claims on Philippine incorporated private enterprises (including claims on government corporations and on MSME not qualifying under highly diversified loan portfolio as defined in Item "d" below) with the highest credit quality as defined in Part VI; and
- viii. Claims on foreign incorporated private enterprises with the highest credit quality as defined in Part VI.

c) 50% risk weight –

- i. Loans to individuals for housing purpose, fully secured by first mortgage on residential property that is or will be occupied by the borrower which are not classified as non-performing; and
- ii. Local government unit (LGU) bonds which are covered by Deed of Assignment of Internal Revenue Allotment of the LGU and guaranteed by the LGU Guarantee Corporation.

d) 75% risk weight –

Qualified micro, small and medium enterprise (MSME) loan portfolio that meets the following criteria:

For individual claims that may form part of the MSME loan portfolio –

(1) Claim must be on a micro, small or medium business enterprise as defined under existing BSP regulations; and

(2) Claim must be in the form of:

- Direct loan; or
- Unused letters of credit: *Provided*, That the credit equivalent amounts thereof shall be determined in accordance with paragraph 3.

For the MSME loan portfolio –

(1) It must be a highly diversified portfolio, i.e., it has at least 500 borrowers that are distributed over a number of industries; and

(2) All claims in the qualified loan portfolio must be current.

e) 100% risk weight –

- i. Foreign currency denominated claims on or portion of claims guaranteed by or collateralized by foreign currency denominated securities issued by the Philippine National Government and the BSP; *Provided*, That one-third (1/3) of the applicable risk weight shall be applied by 1 January 2012, two-thirds (2/3) by 1 January 2013, and the full risk weight by 1 January 2014; and
- ii. Non-performing loans to individuals for housing purpose, fully secured by first mortgage on residential property that is or will be occupied by the borrower.

f) 150% risk weight –

- i. All non-performing loans (except non-performing loans to individuals for housing purpose, fully secured by first mortgage on residential property that is or will be occupied by the borrower) and all non-performing debt securities.
- ii. Real and other properties acquired (ROPA) – net of allowance for losses; *Provided*, That the 150% risk weight shall be applied on a staggered basis for three years, i.e., 115% starting 1 January 2012, 130% from 1 January 2013, and 150% from 1 January 2014.

g) 100% risk weight –

All other assets including, among others, the following:

- i. Claims on central governments and central banks of foreign countries other than those with the highest credit quality;

- ii. Claims on Philippine local government units other than those with the highest credit quality;
- iii. Claims on non-central government public sector entities of foreign countries other than those with the highest credit quality;
- iv. Claims on Philippine incorporated banks/quasi-banks other than those with the highest credit quality;
- v. Claims on foreign incorporated banks other than those with the highest credit quality;
- vi. Claims on the Philippine incorporated private enterprises (including claims on government corporations and on MSME not qualifying under highly diversified loan portfolio as defined in Item "d" above) other than those with the highest credit quality;
- vii. Claims on foreign incorporated private enterprises other than those with the highest credit quality;
- viii. Loans to companies engaged in speculative residential building or property development;
- ix. Equity investments (except those deducted from capital);
- x. Bank premises, furniture, fixture and equipment, inclusive of revaluation increment – net of allowance for losses;
- xi. Foreign currency notes and coins on hand not acceptable as international reserves; and
- xii. Foreign currency checks and other cash items not acceptable as international reserves,

except those which are deducted from capital, as follows:

- i. Total outstanding unsecured credit accommodations, both direct and indirect, to directors, officers, stockholders and their related interests (DOSRI) - net of allowance for credit losses;
- ii. Total outstanding unsecured loans, other credit accommodations and guarantees granted to subsidiaries and affiliates - net of allowance for credit losses;
- iii. Deferred tax asset, net of deferred tax liability: Provided, That the conditions to offset under PAS 12 are met: Provided, further, That any excess of deferred tax liability over deferred tax asset (i.e., net deferred tax liability) shall not be added to Tier 1 capital;
- iv. Goodwill, net of allowance for losses, including that relating to unconsolidated subsidiary RBs and VCCs for TBs, and RBs for Coop Banks (on solo basis) and unconsolidated non-financial allied undertakings (on solo and consolidated bases);
- v. Sinking fund for redemption of limited life redeemable preferred stock with the replacement requirement upon redemption;

- vi. Sinking fund for redemption of limited life redeemable preferred stock without the replacement requirement upon redemption (limited to the balance of redeemable preferred stock after applying the cumulative discount factor);
- vii. Investment in equity of unconsolidated subsidiary RBs and VCCs for TBs, and RBs for Coop Banks after deducting related goodwill, if any (for solo basis);
- viii. Investments in other regulatory capital instruments of unconsolidated subsidiary RBs for Coop Banks (for solo basis);
- ix. Investment in equity of subsidiary non-financial allied undertakings, after deducting related goodwill, if any (for both solo and consolidated bases);
- x. Significant minority investments (20%-50% of voting stock) in banks and other financial allied undertakings (for both solo and consolidated bases); and
- xi. Reciprocal investments in equity/other regulatory capital instruments of other banks/quasi-banks/enterprises.

B. Off-Balance Sheet Assets

3. The risk-weighted amount shall be calculated using a two-step process. First, the credit equivalent amount of an off-balance sheet item shall be determined by multiplying its notional principal amount by the appropriate credit conversion factor, as follows:

a) 100% credit conversion factor

This shall apply to direct credit substitutes, e.g., general guarantees of indebtedness (including standby letters of credit serving as financial guarantees for loans and securities) and acceptances (including endorsements with the character of acceptances), and shall include:

- i. Guarantees issued other than shipside bonds/airway bills; and
- ii. Financial standby letters of credit (net of margin deposit).

b) 50% credit conversion factor

This shall apply to certain transaction-related contingent items, e.g., performance bonds, bid bonds, warranties and standby letters of credit related to particular transactions, and shall include:

- i. Performance standby letters of credit (net of margin deposit), established as a guarantee that a business transaction will be performed.

This shall also apply to --

- i. Other commitments e.g., formal standby facilities and credit lines with an original maturity of more than one (1) year.

c) 20% credit conversion factor

This shall apply to short-term, self-liquidating trade-related contingencies arising from movement of goods, e.g., documentary credits collateralized by the underlying shipments, and shall include:

- i. Trade-related guarantees:
 - (1) Shipperside bonds/airway bills
 - (2) Letters of credit - confirmed
- ii. Sight letters of credit outstanding (net of margin deposit);
- iii. Usance letters of credit outstanding (net of margin deposit);
- iv. Deferred letters of credit (net of margin deposit);
- v. Revolving letters of credit (net of margin deposit) arising from movement of goods and/or services; and

This shall also apply to commitments with an original maturity of up to one (1) year.

d) 0% credit conversion factor

This shall apply to commitments, which can be unconditionally cancelled at any time by the bank without prior notice, and shall include –

- i. Credit card lines.

This shall also apply to those not involving credit risk, and shall include:

- i. Late deposits/payments received;
- ii. Inward bills for collection;
- iii. Outward bills for collection;
- iv. Travelers' checks unsold;
- v. Trust department accounts;
- vi. Items held for safekeeping/custodianship;
- vii. Items held as collaterals;
- viii. Deficiency claims receivable; and
- ix. Others.

Second, the credit equivalent amount shall be treated like any on-balance sheet asset and shall be assigned the appropriate risk weight, i.e., according to the obligor, or if relevant, the qualified guarantor or the nature of collateral.

C. Claims with Eligible Collateral/Guarantees

4. In order to obtain capital relief, all documentation used in collateralized transactions and for documenting guarantees must be binding on all parties and legally enforceable in all relevant jurisdictions. The disclosure requirements under Part V of this document must also be observed for banks to obtain capital relief.
5. In addition to the general requirement for legal certainty set out in paragraph 4, the legal mechanism by which collateral is pledged or transferred must ensure that the bank has the right to liquidate or take legal possession of it in a timely manner, in the event of default, insolvency or bankruptcy.
6. The following are the eligible collateral instruments:
 - a) Cash (as well as certificates of deposits or comparable instruments issued by the lending bank) on deposit with the bank which is incurring the counterparty exposure;
 - b) Peso-denominated securities issued by the Philippine National Government and the BSP;
 - c) Multilateral development banks;
 - d) Securities with the highest credit quality as defined in Part VI issued by:
 - i. Central government and central banks of foreign countries;
 - ii. Philippine local government units; and
 - iii. Non-central government public sector entities of foreign countries; and
 - e) First mortgage on residential property, only in the case of loans to individuals for housing purpose.
7. A guarantee must represent a direct claim on the protection provider and must be explicitly referenced to specific exposures or a pool of exposures, so that the extent of the cover is clearly defined and incontrovertible. Other than the non-payment by a protection purchaser of money due in respect of the credit protection contract, the guarantee must be irrevocable; there must be no clause in the contract that would allow the protection provider unilaterally to cancel the credit cover or that would increase the effective cost of cover as a result of deteriorating credit quality in the hedged exposure. It must also be unconditional; there should be no clause in the protection contract outside the direct control of the bank that could prevent the protection provider from being obliged to pay out in a timely manner in the event that the original counterparty fails to make the payment(s) due.
8. The following are the eligible guarantors:
 - a) Philippine National Government and the BSP;
 - b) Multilateral development banks;
 - c) Guarantors with the highest credit quality as defined in Part VI:
 - i. Central government and central banks of foreign countries;

- ii. Philippine local government units;
 - iii. Non-central government public sector entities of foreign countries;
 - iv. Philippine incorporated banks/quasi-banks; and
 - v. Foreign incorporated banks; and
- d) LGU Guarantee Corporation, in the case of LGU bonds which are covered by Deed of Assignment of Internal Revenue Allotment.
9. The extent to which a claim is guaranteed/collateralized shall be determined by the amount of current market value of securities pledged/guarantee coverage, in comparison with the carrying amount of the on-balance sheet claim or the notional principal amount of the off-balance sheet exposure.

Part IV. Operational Risk-Weighted Assets

A. Definition of operational risk

1. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk, but excludes strategic and reputational risk.
2. Banks should be guided by the Basel Committee on Banking Supervision's recommendations on *Sound Practices for the Management and Supervision of Operational Risk* (February 2003). The same may be downloaded from the BIS website (www.bis.org).

B. Measurement of capital charge

3. In computing for the operational risk capital charge, banks shall use the basic indicator approach, with modification.
4. Under this approach, banks must hold capital for operational risk equivalent to 12% of the average gross income over the previous three years of positive annual gross income; *Provided*, That this shall be applied over a 3-year period, i.e., 4% capital charge shall be applied by 1 January 2012, 8% by 1 January 2013, and 12% by 1 January 2014. Figures for any year in which annual gross income is negative or zero should be excluded from both the numerator and denominator when calculating the average.
5. Gross income must be calculated using the year-end balances from the Financial Reporting Package (FRP).
6. Gross income, for the purpose of computing for operational risk capital charge, is defined as net interest income plus non-interest income. This measure should:
 - a) be gross of any provisions for losses on accrued interest income from financial assets;
 - b) be gross of operating expenses, including fees paid to outsourcing service providers;

- c) include fees and commissions;
 - d) exclude gains/(losses) from the sale/redemption/ derecognition of non-trading financial assets and liabilities;
 - e) exclude gains/(losses) from sale/derecognition of non-financial assets; and
 - f) include other income (i.e., rental income, miscellaneous income, etc.).
7. Banks that have concerns on the insufficiency of their income data should consult their respective Central Point of Contact Department (CPCD) of the Supervision and Examination Sector (SES) for the appropriate computation of the operational risk capital charge.²

C. Measurement of operational risk-weighted assets

8. The resultant operational risk capital charge is to be multiplied by 125% before multiplying by 10 (i.e., the reciprocal of the minimum capital ratio of 10%) to arrive at the total operational risk-weighted assets.

Part V. Disclosures in the Annual Reports and Published Balance Sheet

1. In addition to the disclosure requirements under Subsections X190.5 and X192.9.c of the MORB, banks shall disclose in their Annual Reports, where applicable, the information below. Item h should also be disclosed in the quarterly Published Balance Sheet (PBS):
- a) Tier 1 capital and a breakdown of its components (including deductions solely from Tier 1);
 - b) Tier 2 capital and a breakdown of its components;
 - c) Deductions from Tier 1 (50%) and Tier 2 (50%) capital;
 - d) Total qualifying capital;
 - e) Capital requirements for credit risk;
 - f) Capital requirements for market risk;
 - g) Capital requirements for operational risk; and
 - h) Total and Tier 1 capital adequacy ratio on both solo and consolidated bases.
2. The required disclosures shall commence with Annual Reports for financial year 2012 and quarterly PBS from end-March 2012.

Part VI. Definitions

1. *Bank premises, furniture, fixture and equipment (inclusive of revaluation increment) – net.* This refers to the real and other properties used/to be used for banking purposes inclusive of revaluation increment as approved by the Monetary Board.

² Applies to banks operating for less than three years, or those that have been recently merged, among others.

2. *Cash on hand.* This refers to total amount of cash in the bank's vault in the form of notes and coins in Philippine currency and in foreign currencies acceptable to form part of the international reserves.
3. *Central government of a foreign country.* This refers to the central government which is regarded as such by a recognized banking supervisory authority in that country.
4. *Checks and other cash items (COCIs).* This refers to the total amount of checks and other cash items received after the selected clearing cut-off time until the close of the regular banking hours denominated in Philippine currency and in foreign currencies acceptable to form part of the international reserves.
5. *Claims.* This refer to exposures to the entity on whom the claim is held, and shall include, but shall not be limited to the following accounts, inclusive of unamortized discount/(premium) and accumulated market gains/(losses) and net of allowance for credit losses: *Provided, That for available for sale debt securities, any accumulated market gains/(losses) shall be deducted/added back as stated in paragraph 10 of Part II:*
 - a) Due from BSP;
 - b) Due from other banks;
 - c) Financial assets designated at fair value through profit or loss;
 - d) Available for sale financial assets;
 - e) Held to maturity financial assets;
 - f) Unquoted debt securities classified as loans;
 - g) Loans and receivables;
 - h) Loans and receivable arising from repurchase agreements, certificates of assignment/participation with recourse, and securities lending and borrowing transactions;
 - i) Sales contract receivables;
 - j) Accrued interest income from financial assets; and
 - k) Others, e.g., accounts receivable and dividends receivable.

Accruals on a claim shall be classified and risk weighted in the same way as the claim. Bills purchased on a without recourse basis shall be classified as claims on the drawee banks.

6. *Claims on (a) central government and central bank and non-central government public sector entities of foreign country and foreign incorporated bank/private enterprise; and (b) on Philippine National Government and central bank and local government units and Philippine incorporated bank/quasi-bank/private enterprise.* This refers to claims on governments, banks/ quasi-banks, private enterprises given the highest credit rating by any of the following BSP-recognized credit rating agencies:

International rating agencies:

Rating agency	Highest rating
Moody's	"Aa3" and above
Standard & Poor's	"AA-" and above
Fitch Ratings	"AA-" and above
And such other rating agencies as may be approved by the Monetary Board	

International rating agencies (with National Ratings):

Rating agency	Highest rating
Fitch Ratings Singapore	"AA-" and above
And such other rating agencies as may be approved by the Monetary Board	

Domestic rating agencies:

Rating agency	Highest rating
PhilRatings	"PRS Aa" and above
And such other rating agencies as may be approved by the Monetary Board	

Provided, That for purposes of this Circular,

- With prior BSP approval, international credit rating agencies may have national rating systems developed exclusively for use in the Philippines using the Philippine sovereign as reference highest credit quality anchor;
- If a claim has only one rating by any of the BSP recognized credit assessment agencies, that rating shall be used to determine the risk weight of the claim; in cases where there are two or more ratings which map into different risk weights, the higher of the two lowest risk weights should be used;
- Any reference to credit rating shall refer to issue-specific rating; the issuer rating may be used only if the claim being risk-weighted is an unsecured senior obligation of the issuer and is of the same denomination applicable to the issuer rating (e.g., local currency issuer rating may be used for risk weighting local currency denominated senior claims); or short-term or in cases of guarantees;
- For loans, risk weighting shall depend on either the rating of the borrower or the rating of the unsecured senior obligation of the borrower: *Provided*, That in the case of the latter, the loan is of the same currency denomination as the unsecured senior obligation; and

- Domestic debt issuances may be rated by BSP-recognized domestic or international credit rating agencies, which have developed a national rating scale acceptable to the BSP, while internationally issued debt obligations shall be rated by BSP-recognized international credit assessment agencies only.
7. *Consolidated basis.* This refers to combined financial statements of parent bank and subsidiary financial allied undertakings (i.e., RBs and VCCs for TBs, and RBs for Coop Banks) on a line by line basis.
 8. *Deposit for stock subscription.* This refers to the payments made by stockholders of the bank on subscription to the increase in the authorized capital which cannot be directly credited to capital stock issued pending approval by the BSP and registration with the Securities and Exchange Commission of the amendment to the Articles of Incorporation increasing capital stock. This account shall be used only when existing authorized capital is already fully subscribed.
 9. *Financial allied undertakings.* This refers to enterprises or firms with homogenous or similar activities/business/functions with the financial intermediary and may include but not limited to leasing companies, banks, investment houses, financing companies, credit card companies, financial institutions catering to small and medium scale industries (including venture capital corporations), companies engaged in foreign exchange dealership/brokerage, and such other similar activities as the Monetary Board may declare as appropriate from time to time.
 10. *Goodwill.* This refers to the future economic benefit arising from assets that are not capable of being individually identified and separately recognized.
 11. *Government corporations.* This refers to commercial undertakings owned by central governments or non-central public sector entities. Claims on Philippine government owned or controlled corporations (GOCCs) that are not explicitly guaranteed by the Philippine National Government are also included in this category.
 12. *Interbank call loans.* This refers to the cost of call/demand loans granted to other resident banks and non-bank financial intermediaries with quasi-banking authority covered under Section X343 of the MORB.
 13. *Investment in subsidiaries.* This refers to the amount of the bank's investments in the equity instruments of unconsolidated subsidiaries which shall be accounted for using the equity method. As provided under PAS 27, a subsidiary is an entity that is controlled by another entity (known as the parent). Control is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than half of the voting power of an entity, unless in exceptional circumstances, it can be directly demonstrated that such ownership does not constitute control.

14. *Loans to individuals for housing purpose, fully secured by first mortgage on residential property that is or will be occupied by the borrower.* This shall not include loans to companies engaged in speculative residential building or property development.
15. *Loans or acceptances under letters of credit to the extent covered by margin deposits.* This shall not include the unnegotiated letters of credit or the unutilized portion thereof, or other items booked under contingent accounts. This shall also not include margin deposits against loans or acceptance accounts which are fully liquidated.
16. *Loans to the extent covered by hold-out on, or assignment of, deposits or deposit substitutes maintained in the lending bank.* A loan shall be considered as secured by a hold-out on, or assignment of deposit or deposit substitute only if such deposit or deposit substitute account is covered by a hold-out agreement or deed of assignment signed by the depositor or investor/placer in favor of the bank. This shall not include loans transferred to/carried by the bank's trust department secured by deposit hold-out/assignment.
17. *Multilateral development banks.* This includes all exposures to multilateral development banks. Claims on World Bank Group, which comprised of the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC), the Asian Development Bank (ADB), the African Development Bank (AfDB), the European Bank for Reconstruction and Development (EBRD), the Inter-American Development Bank (IADB), the European Investment Bank (EIB), the European Investment Fund (EIF), the Nordic Investment Bank (NIB), the Caribbean Development Bank (CDB), the Islamic Development Bank (IDB), and the Council of Europe Development Bank (CEDB) currently receive 0% risk weight.
18. *Non-central government public sector entities of a foreign country.* This refers to entities which are regarded as such by a recognized banking supervisory authority in the country in which they are incorporated.
19. *Non-performing debt securities.* This refers to debt securities as described below:
 - a) For zero-coupon debt securities, and debt securities with quarterly, semi-annual, or annual coupon payments, they shall be considered non-performing when principal and or coupon payment is unpaid for thirty (30) days or more after due date; and
 - b) For debt securities with monthly coupon payments, they shall be considered non-performing when three (3) or more coupon payments are in arrears: Provided, however, That when the total amount of arrearages reaches twenty percent (20%) of the total outstanding balance of the debt security, the total outstanding balance of the debt security shall be considered as non-performing.

20. *Other commitments.* This includes undrawn portion of any binding arrangements which obligate the bank to provide funds at some future date.
21. *Other commitments with an original maturity of up to one (1) year.* This includes any revolving or undated open-ended commitments, e.g., overdrafts or unused credit lines, providing that they can be unconditionally cancelled at any time and subject to credit revision at least annually.
22. *Other regulatory capital instruments.* This refers to unsecured subordinated term debt instruments qualifying as capital of banks.
23. *Perpetual preferred stock.* This refers to preferred stock that does not have a maturity date, that cannot be redeemed at the option of the holder of the instrument, and that has no provision that will require future redemption of the issue. Consistent with these provisions, any perpetual preferred stock with a feature permitting redemption at the option of the issuer may qualify as capital only if the redemption is subject to prior approval of the BSP.
24. *Philippine local government units (LGUs).* This refers to Philippine government units below the level of national government, such as city, provincial, and municipal governments.
25. *Philippine National Government.* This shall refer to the Philippine National Government and its agencies such as departments, bureaus, offices, and instrumentalities, but excluding government owned or controlled corporations.
26. *Private enterprises.* This refers to all commercial companies whether organized in the form of a corporation, partnership, or sole proprietorship. This shall include government corporations.
27. *Redeemable preferred stock.* This refers to preferred stock which under existing regulation may be redeemed at the specific dates or periods fixed for redemption, only upon prior approval of the BSP and, where the conditions of the issuance specifically state, only if the shares redeemed are replaced with at least an equivalent amount of newly paid-in shares so that the total paid-in capital stock is maintained at the same level immediately prior to redemption: *Provided, That* redemption shall not be earlier than five (5) years after the date of issuance: *Provided, further, That* such redemption may not be made where the bank is insolvent or if such redemption will cause insolvency, impairment of capital or inability of the bank to meet its debts as they mature.
28. *Solo basis.* This refers to combined financial statements of head office and branches.
29. *Treasury shares.* This refers to shares of the parent bank held by a subsidiary financial allied undertaking (i.e., RBs and VCCs for TBs, and RBs for Coop Banks) in consolidated financial statements.

Part VII. Required Reports

1. Banks shall submit a report of their risk-based capital ratio on a solo basis (head office plus branches) and on a consolidated basis (parent bank plus subsidiary financial allied undertakings (i.e., RBs and VCCs for TBs, and RBs for Coop Banks) quarterly in the prescribed forms within the deadlines, i.e., 15 banking days and 30 banking days after the end of the reference quarter, respectively. Only banks with subsidiary financial allied undertakings (i.e., RBs and VCCs for TBs, and RBs for Coop Banks) which under the existing regulations are required to prepare consolidated financial statements on a line-by-line basis shall be required to submit report on consolidated basis. The abovementioned reports shall be classified as Category A-2 reports.

Part VII. Sanctions

A. For non-reporting of CAR breaches

1. It is the responsibility of the President or any officer of the bank holding equivalent position to cause the immediate reporting of CAR breaches both to its Board of Directors (BOD) and to the BSP. It is likewise the responsibility of the President/or any officer holding equivalent position to ensure the accuracy of CAR calculations and the integrity of the associated monitoring and reporting system. Any willful violation of the above will be considered as a serious offense for purposes of determining the appropriate monetary penalty that will be imposed on the President/or any officer holding equivalent position. In addition, the President/or any officer holding equivalent position shall be subject to the non-monetary sanctions:
 - a) First offense – warning
 - b) Second offense – reprimand
 - c) Third offense – 1 month suspension without pay
 - d) Further offense – disqualification

B. For non-compliance with required disclosures

2. Willful non-disclosure or erroneous disclosure of any item required to the disclosed under this framework in either the Annual Report or the Published Balance Sheet shall be considered as a serious offense for purposes of determining the appropriate monetary penalty that will be imposed on the bank. In addition, the President/or any officer holding equivalent position and the BOD shall be subject to the following non-monetary sanctions:
 - a) First offense – warning on President/or any officer holding equivalent position and the BOD
 - b) Second offense – reprimand on President/or any officer holding equivalent position and the BOD

- c) Third offense – 1 month suspension of President/or any officer holding equivalent position without pay
- d) Further offense – possible disqualification of the President/or any officer holding equivalent position and/or the BOD

C. For non-compliance with the minimum CAR

- 3. In case a bank does not comply with the prescribed minimum CAR, the Monetary Board may limit or prohibit the distribution of net profits by such bank and may require that part or all of net profits be used to increase the capital accounts of the bank until the minimum requirements has been met. The Monetary Board may, furthermore, restrict or prohibit the acquisition of major assets and the making of new investments by the bank, with the exception of purchases of readily marketable evidences of indebtedness of the Republic of the Philippines and of the BSP included in paragraph 2, Item a.ii of Part III, and any other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines, until the minimum requirement capital ratio has been restored.
- 4. In case of a bank merger, or consolidation, or when a bank is under rehabilitation program approved by the BSP, the Monetary Board may temporarily relieve the surviving bank, consolidated bank, or constituent bank or corporations under rehabilitation from full compliance with the required capital ratio under such conditions as it may prescribe.
- 5. A bank may also be subject to Prompt Corrective Action (PCA) framework when either the total CAR, Tier 1 ratio or leverage ratio falls below 10%, 6%, and 5%, respectively, or such other minimum levels that may be prescribed for the said ratios under relevant regulations, and/or the combined capital accounts falls below the minimum capital requirement prescribed under Subsection X111.1 of the MORB, pursuant to the provisions of Circular No. 523 dated 23 March 2006, as amended.