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DETAILED ASSESSMENT OF OBSERVANCE—BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

This Detailed Assessment of Observance of the Basel Core Principles for Effective Banking Supervision was prepared by a staff team of the International Monetary Fund and World Bank. It is based on the information available at the time it was completed in July 2019.

Disclaimer:
This document was prepared before COVID-19 became a global pandemic and resulted in unprecedented economic strains. It, therefore, does not reflect the implications of these developments and related policy priorities. We direct you to the **IMF Covid-19 page** that includes staff recommendations with regard to the COVID-19 global outbreak.

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BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

Prepared By
Monetary and Capital Markets Department, IMF, and Finance, Competitiveness and Innovation Global Practice, World Bank

This report was prepared in the context of a joint IMF-World Bank standards assessment mission in the Philippines during June-July 2019, led by Hiroko Oura (IMF) and Ilias Skamnelos (WB), and overseen by the Monetary and Capital Markets Department, IMF, and the Finance, Competitiveness and Innovation Global Practice, World Bank. Further information on the FSAP program can be found at http://www.imf.org/external/np/fsap/fssa.aspx, and www.worldbank.org/fasp.

INTERNATIONAL MONETARY FUND

THE WORLD BANK

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Glossary

AASC	Auditing and Assurance Standards Council
AML	Anti-money laundering
AMLC	Anti-Money Laundering Council
AFS	Audited financial statement
BCM	Business Continuity Management
BCP	Basel Core Principles for Effective Banking Supervision
BIS	Bank for International Settlements
BPR	Bank Performance Report
BRes	Bank for Resolution Framework
BSP	Bangko Sentral ng Pilipinas—Central Bank of the Philippines
BSFI	BSP Supervised Financial Institution
BSOS	Banking Sector Outlook Survey
BSPI	Bangko Sentral ng Pilipinas Institute
BSRA	Banking System Risk Analysis
CAR	Capital Adequacy Ratio
CCB	Capital Conservation Buffer
CCyB	Counter-cyclical Capital Buffer
CDA	Co-operative Development Authority
CDO	Cease and Desist Order
CET1	Core Equity Tier 1
CFP	Contingency Funding Plan
CMG	Crisis Management Group
CRO	Chief Risk Officer
DOF	Department of Finance
DOSRI	Directors, officers, stockholders and their related interests
D-SIB	Domestic Systemically Important Bank
DSA	Department of Supervisory Analytics
EIC	Examiner in Charge
FCMR	Financial Crisis Management and Resolution Framework
FCSC	Financial Conglomerate Supervision Committee
FSAP	Financial Sector Assessment Program
FSCC	Financial Stability Coordination Council
FSD	Financial Supervision Department
FSF	Financial Sector Forum
FSR	Financial Stability Report
FSS	Financial Supervision Sector
FSSS	Financial Supervision Subsectors
FRP	Financial Reporting Package
FX	Foreign Exchange
GBL	General Banking Law 2000

GDP	Gross Domestic Product
IA	Internal Audit
IAS	International Accounting Standards
IC	Insurance Commission
ICAAP	Internal Capital Adequacy Assessment Process
IO	Institutional Overview
IRRBB	Interest Rate Risk in the Banking Book
LCR	Liquidity Coverage Ratio
LE	Large Exposures
LOC	Letter of Commitment
MB	Monetary Board
MIS	Management Information System
MLR	Minimum Liquidity Ratio
MOA	Memorandum of Agreement
MORB	Manual of Regulation for Banks
MORFXT	Manual of Regulations on Foreign Exchange Transactions
MOU	Memorandum of Understanding
MRM	Market Risk Model
MSB	Money Service Business
NBFI	Non-bank Financial Institution
NCBA	New Central Bank Act, as amended
NPL	Non-performing Loan
NSFR	Net Stable Funding Ratio
NSSLA	Non-Stock Savings and Loan Associations
OSRM	Office of Systemic Risk Management
PAS	Philippine Accounting Standards
PCA	Prompt Corrective Action
PCAP	Prompt Corrective Action Plan
PCDNC	Philippine Central Depository Nominee Corporation
PDIC	Philippine Deposit Insurance Corporation
PFRS	Philippine Financial Reporting Standards
PSA	Philippine Standards on Audit
PSSS	Policy and Specialized Supervision Subsector
QB	Quasi-bank
QMS	Quality Management Standards
RA	Republic Act
REST	Real Estate Stress Test
ROE	Report of Examination
ROPA	Real and Other Properties Acquired
RPT	Related Party Transaction
SAFR	Supervisory Assessment Framework
SBL	Single Borrower's Limit
SEC	Securities and Exchange Commission

SG	Supervision Guidelines
SPRD	Supervisory Policy and Research Department
SRP	Supervisory Review Process
SSM	Single Supervisory Mechanism
UBO	Ultimate Beneficial Owner

INTRODUCTION[1]

1. **The BSP's regulatory framework is broadly effective for the size and complexity of the Philippine banking system, but legislative gaps continue to hinder effective supervision of banks.** The BSP has a well-resourced, experienced and highly committed staffing complement, but there is an ongoing need to develop and maintain adequate expertise in certain complex areas (e.g., risk modelling). Since the FSAP in 2002, and the assessment update in 2010, the BSP has made significant progress in enhancing the regulatory framework in a number of areas. But significant weaknesses in the legislative framework, arising notably from the bank secrecy laws and the lack of power for the BSP to supervise the parent companies and their affiliates of banking groups, present a material hindrance to effective supervision.

2. **Several initiatives undertaken by BSP have strengthened the overall regulatory and supervisory framework.** BSP's recently updated Charter (February 2019), among other things, formalizes its financial stability mandate, extends the scope of supervised entities, and grants additional authority to force banks to hold capital beyond the minimum regulatory requirement when needed. The BSP aims to implement the full Basel framework and is in the process of doing so. A number of core Basel III elements have been introduced by the BSP since the most recent assessment (e.g., capital definition amendments; higher capital minima requirements; Liquidity Coverage Ratio (LCR); Net Stable Funding Ratio (NSFR); leverage ratio; and the framework for D-SIBs), in addition to amendments to core banking supervision legislation and numerous guidelines.

3. **A number of new initiatives are in train which, when implemented, will align the BSP regulatory framework more closely to applicable Basel standards.** Assessors noted that the BSP is in the process of updating guidelines pertaining to large exposures, interest rate risk in the banking book, market risk management, model risk management, country and transfer risk capturing the investment side, and Pillar 3 disclosure requirements[2]. BSP needs to develop guidance in the areas of bank's internal credit risk models and intra-day liquidity reporting. Liquidity monitoring tools, specifically in respect of cash flow mismatch reporting, need to be reviewed and aligned with Basel standards.

4. **Bank secrecy laws in the Philippines restrict the BSP's ability to undertake effective supervision.** The Bank Secrecy laws state that all bank deposits with banking institutions in the Philippines are considered to be of an absolutely confidential nature and may not be examined, inquired or looked into by any person, including the BSP, except in defined circumstances. BSP should be granted unimpaired access to information on all customer accounts, and the ability,

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[1] This Detailed Assessment Report has been prepared by Geraldine Low (IMF) and Alan Ball and Keith Ligon (World Bank).

[2] Since the on-site BCP assessment, the BSP has finalised the following guidelines or amendments to regulations which have not been reviewed nor taken into account as part of this assessment: 1) Guidelines on Investment Activities of BSP-Supervised Financial Institutions (Circular No. 1042–25 July 2019); 2) Guidelines on the Management of Interest Rate Risk in the Banking Book and amendment to the Guidelines on Market Risk Management (Circular No. 1044–6 August 2019); 3) Revised Risk-Based Capital Adequacy Framework for Stand-alone Thrift, Rural and Cooperative Banks (Circular No. 1079–9 March 2020); 4) Amendments to the Framework for Dealing with D-SIBs (Circular No. 1051–27 September 2019); 5) Report on Intraday Liquidity of Universal and Commercial Banks and their Subsidiary Banks/Quasi-Banks (Circular No. 1064–3 December 20190); and 6) Amendments to Regulations on Financial Audit of Banks and NBFIs (Circular Nos. 1074 and 1075–7 February 2020).

without constraints, to employ and share depositor information for any prudential purpose (e.g., funding concentrations from related parties, intra-group dependencies, cash flow analysis, related-party transactions (RPT) and off-site anti-money laundering (AML) data and analysis) in order to fulfill its supervisory mandate to address safety and soundness concerns.

5. BSP's ability to assess the impact of mixed conglomerate structures on D-SIB banking groups needs to be strengthened. The BSP has to rely to a large extent on public information for assessing risks in the wider conglomerates as it does not have the power to supervise a bank's parent or the wider group, or to review their activities to determine their impact on the safety and soundness of the bank and the bank groups within the conglomerates. The recent Charter amendment gave the BSP an additional power to obtain data and information from entities including parent and affiliate companies for "statistical and policy development purposes", but the limited scope of this new authority does not provide the BSP with sufficient powers to assess any potential negative impact the activities of those companies may have on the safety and soundness of the banking group. Limitations on BSP's enforcement powers also impair its ability to fully protect the bank from the actions of parent companies and affiliates.

6. More work is needed to strengthen BSP's oversight on the assessment of ultimate beneficial ownership (UBO) of banks operating in the Philippines. BSP is able to govern transfers of greater than 10 percent of voting shares of a bank, however current laws and regulations do not enable BSP to address transfers by or assess suitability of UBO or significant indirect controlling interests of banks.

7. BSP's ability to assess the resolvability of banks, especially D-SIBs, and support the orderly resolution of a problem bank, including the preparedness for effectively dealing with a major bank failure needs to be developed. BSP should continue ongoing improvements to its Prompt Corrective Action (PCA) framework and ensure that failed or failing banks are resolved in a prompt and timely fashion. BSP should incorporate an assessment of resolvability into its supervisory framework, especially for D-SIBs, in conjunction with the PDIC. BSP should continue its ongoing efforts to ensure that the PCA framework effectively operates to require firms to be placed into resolution at an early stage and before equity has been exhausted, and that the supporting legal and regulatory framework ensures the transition of problem banks to the PDIC is on a timely basis to avoid losses to the deposit insurance fund and mitigate moral hazard risks.

INSTITUTIONAL AND MARKET STRUCTURE—OVERVIEW

A. Institutional Structure

8. The BSP is responsible for the prudential regulation and supervision of banks, nonbanking entities,[3] money service businesses, credit granting entities and payment system operators. BSP is the central monetary authority responsible for providing policy directions in the

[3] Nonbanks include Investment Houses Finance Companies, Investment Companies, and other NBFIs with quasi-banking functions or are subsidiaries of banks/quasi-banks, Pawnshops, Non-Stocks Savings and Loan Associations, Trust Corporations, and Credit Card Companies.

area of money, banking and credit. It also oversees the payment and settlement systems in the Philippines, including overseeing the critical financial market infrastructure.

9. The Philippines regulatory framework includes other financial sector authorities responsible for financial regulation:

- **Securities and Exchange Commission (SEC)** is the national government regulatory agency charged with supervision over the corporate sector, capital market participants and the securities and investment instruments markets. In addition to its regulatory functions, the SEC also maintains the country's company register.
- **The Insurance Commission (IC)** is a national government regulatory agency which supervises and regulates the operations of life and non-life companies, mutual benefit associations, and trusts for charitable uses. It issues licenses to insurance agents, general agents, resident agents, underwriters, brokers, adjusters and actuaries. It has also the authority to suspend or revoke such licenses.
- **Philippine Deposit Insurance Corporation (PDIC)** is a government-run corporation providing deposit insurance coverage to member banks. PDIC serves as the principal resolution authority for insured institutions. Membership of banks is mandatory and provides protection up to PhP 500,000 to depositors.

10. The regulators, together with the Department of Finance (DOF), form the Financial Stability Co-ordination Council (FSCC), a voluntary body chaired by the Governor of the BSP, which meets quarterly to discuss industry wide perspectives in identifying financial issues and contemplating macroprudential regulation to mitigate systemic risk. FSCC members signed a Memorandum of Agreement (MOA) in January 2014 to formalize representation of the FSCC, streamline its working groups and to clarify communication initiatives. In addition, the Financial Sector Forum (FSF), made up of the BSP, SEC, IC and PDIC, meet six times per year to exchange information and to coordinate regulatory and supervisory policies where appropriate of its members.

B. Overview of the Banking Sector

11. The banking sector accounted for approximately 76 percent of the financial system's total resources,[4] or 98 percent of the nominal Gross Domestic Product (GDP), as of end-June 2019. As outlined in Table 1, BSP's supervised financial institutions consist of 554 banks, 1,214 nonbank financial institutions and 2 off-shore banking units. Banking sector assets are broken down by: 46 universal and commercial banks representing 91.3 percent of total bank assets, 3 government banks[5] (14.4 percent of total bank assets), 51 thrift banks (7.2 percent of total bank assets), and 457 rural and cooperative banks (1.5 percent of total bank assets). Although 30 foreign

[4] BSP website indicates banking sector assets accounts for approximately 83 percent of the financial systems total resources as this ratio does not include insurance and mutual fund assets.

[5] Three state-owned banks, two of which are considered significant, are operated under separate charters but supervised by the BSP as universal banks.

banks were approved and authorized to operate by the BSP in the Philippines, this represented only 7.2 percent of the total banking system assets as at end of June 2019.[6] Domestic banks have minimal overseas activities.

Table 1. Philippines: Financial Sector Structure

Type of Institution	Number of Institution[1]	Assets June 2019			Asset Dec 2009		
		Billion PHP	Percent of total	Percent of GDP	Billion PHP	Percent of total	Percent of GDP
Bank	554	17,590	76	98	6,512	74	81
Universal and Commercial Banks	46	16,019	69	89	5,779	66	72
o/w Government Banks	3						
Thrift Banks	51	1,288	6	7	555	6	7
Rural and Cooperative Banks	457	283	1	2	178	2	2
Non-Bank Financial Institutions (NBFIs)[2]		5,673	24	32	2,303	26	29
Insurance		1,716	7	10	554	6	7
Mutual Funds		258	1	1	59	1	1
Other NBFIs[3]		3,699	16	21	1,690	19	21
Total		23,263	100	130	8,815	100	110

Sources: National authorities

1/ Number of institutions is as at end-June 2019.

2/ Data on NBFIs is as of end-March 2019, except Insurance Mutual which is as of end-June 2019.

3/ Includes Investment Houses, Finance Companies, Investment Companies, Securities Dealers/Brokers, Pawnshops, Lending Investors, Non-Stock Savings and Loan Assns., Venture Capital Corps., and Credit Card Companies which are under BSP supervision; also includes Private and Government Insurance Companies (i.e., SSS and GSIS). Data as of end-March 2019.

12. Banking sector risks stem primarily from global macro-financial developments, which could be amplified by several vulnerabilities in the corporate sector and the real estate markets. The Philippine is a small open economy well-integrated with the global supply chain, and its macro-financial performance—the key drivers of bank health—is highly dependent on global conditions. Some corporate vulnerability indicators started to deteriorate in the past couple of years despite their strong levels. Risks from the corporate sector could be further amplified by the complex mixed conglomerate structures. Loans to booming real estate market is close to the regulatory cap of 20 percent of total loans.

13. BSP has identified a number of D-SIBs, an important part of which belong to larger Philippine conglomerate groups and some of which are foreign bank branches. The conglomerates are mixed activity, with a wide range of commercial activities across the various groups, including real estate, breweries, petrochemical companies etc. BSP requires D-SIBs to hold additional capital, including a capital conservation buffer (2.5 percent). The BSP has introduced a countercyclical capital buffer, but it is currently set at 0 percent.

[6] The RA provides that at least 60 percent of the banking system's total resources must be controlled by domestic banks that are majority owned by Filipinos.

14. **Overall, the banking sector has strong capital and liquidity levels.** The Basel III capital adequacy ratio (CAR), adopted effective January 2014, for universal and commercial banks stood at 15.9 percent on a consolidated basis, well above the BSP (10 percent) and BIS prescribed minimum requirements. Common equity tier 1 capital (CET1) stood at 14.5 percent on a consolidated basis. Data as of end-October 2018 indicated the liquidity coverage ratio (LCR) of the universal and commercial banks[7] recorded at 173.1 percent (on a solo basis).

15. **Gross loans contribute to 60 percent of assets and have been driving banking sector growth, with real estate lending comprising the largest share of the loan portfolio at about 17 percent.** Although the average non-performing loan (NPL) ratio was reported at 2.1 percent at end of June 2019, thrift banks reported NPLs at 5.9 percent and rural/cooperative banks at 11.4 percent respectively. NPL coverage ratio is reported at 93.3 percent, which includes the general allowance provision of 100 basis points, end of June 2019. Following the implementation of PFRS 9, the BSP has required universal and commercial banks to maintain a minimum general allowance of 100 basis points, as a floor to the expected credit loss provisioning required in the new standard.

16. **Deposits are mainly from resident individuals and private corporations.** At the end of June 2019, savings accounted for 46 percent of deposits.

17. **The system has been recording annualized returns on assets and equity of 1.2 percent and 9.8 percent respectively.** The net interest margin (NIM) is on an upward trend and stands at 3.6 percent.

PRECONDITIONS FOR EFFECTIVE BANKING SUPERVISION[8]

18. **Although the Philippine economy continues** to demonstrate strong growth of over 6.3 percent between 2010–2018, in 2018 the country faced some challenging issues including rising inflation of 5.2 percent (above target) and some volatility in the Philippine Peso. Monetary policy response has since addressed these issues. As of June 2019, year-on-year inflation eased to 3.4 percent (within target). The overall debt-to-GDP ratio stood at 43.7 percent.

19. **BSP recently amended its Charter to formalize its statutory mandate of promoting and maintaining financial stability.** The BSP continues to work in close coordination with other relevant agencies on the FSCC to promote financial stability. On matters of systemic importance, BSP has worked closely with the DOF in the past, including on the drafting or formulation of any legislation pertaining to financial institutions and financial stability measures. Further, the DOF, together with the Bureau of the Treasury, has primary responsibility for all fiscal matters.

[7] Stand-alone thrift, rural and cooperative banks are subject to a simplified minimum liquidity ratio, based on eligible liquid assets to total liabilities. The minimum ratio is set at 20 percent.

[8] Sources of information: BSP's "A Report on the Philippines Financial System, Second Semester of 2018."

20. The Philippines' public infrastructure, including its legal system, oversight of professionals, accounting standards, and governance and supervision of other financial markets appears strong, as follows:

- The legal system of business laws, including corporate, bankruptcy, contract, consumer protection and private property laws exist.
- Professionals (e.g., accountants, auditors and lawyers) are subject to transparent and ethical standards with oversight by their respective regulatory boards. National accounting and auditing standards are substantially equivalent to international principles and many elements of international good practice are in place to foster reliable and efficient corporate financial reporting. Further, the external auditors of supervised entities of the BSP, SEC and IC are all subject to a stringent accreditation standards program overseen by the SEC.
- The banking sector, financial market and insurance sector have well defined rules to govern and supervise entities by the BSP, SEC and IC respectively.
- The Credit Information System Act, enacted in 2008, provided for the creation of a central credit bureau and the establishment of the Credit Information Corporation which provides credit information to the country.
- Basic economic, financial and social statistics are made available to the public through various government websites.

21. BSP has the primary regulatory responsibility for the Philippines' payments system, including the systemically important payment systems and financial market infrastructures. The newly enacted National Payment Systems Act, effective October 2018, lays out a comprehensive legal and regulatory framework for the payment system related to BSP's oversight role of the Philippine Real Time Gross Settlement System or the "*PhilPaSS*" and the National Retail Payment System.

22. The framework for crisis management, recovery and resolution is currently under development in the Philippines. Although the FSCC recently approved the Financial Crisis Management and Resolution (FCMR) Framework, much more work is needed to develop additional legislative resolution tools as well as strengthening the jurisdiction's crisis preparedness measures for the potential failure of a major bank. Each agency, including the BSP, is currently creating FCMR handbooks to develop individual agency crisis preparedness plans.

23. The PDIC provides some degree of protection in its current role as liquidator for smaller member financial institutions. PDIC's charter provides for the authority to conduct special examinations and take prescriptive action when and if needed. PDIC, with the BSP, carries out joint examinations of member institutions that the BSP has designated as firms in the resolution phase and generally acts in conjunction with the BSP at all times. BSP's Monetary Board (MB) makes the final decision on whether a bank will be liquidated by the PDIC. The PDIC does not currently play a role in the review of D-SIB recovery plans, nor the assessment of resolvability of a major bank.

24. BSP has authority to provide emergency liquidity assistance. In periods of national and/or local financial panic and during normal periods (so long as the bank is not insolvent), the BSP provides emergency loans and advances to banks within prescribed limits and conditions as outlined in the Republic Act.[9]

25. Transparent information is provided by banks to the public. Philippine Financial Reporting Standards (PFRS), which are substantially equivalent to the International Financial Reporting Standards (IFRS), were adopted in 2005. Meanwhile, PFRS 9 was adopted effective January 1, 2018. Although not Pillar 3 compliant, major banks are required to disclose their financial statements to enable users to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed and its management of those risks. In addition, publicly-traded domestic banks are also subject to disclosure requirements imposed by the SEC of the Philippines.

MAIN FINDINGS

A. Responsibilities, Objectives, Powers, Independence (CP 1–2)

26. A significant weakness in the legislative and regulatory framework arises from bank secrecy laws, which prevent the BSP from identifying the names of a bank depositor other than in defined circumstances, thereby constraining the BSP's ability to conduct effective supervision of banks. The constraints imposed by these two Acts hinder effective supervision (e.g., identifying funding concentrations from related parties, intra-group dependencies, cash flow analysis, RPT and off-site AML data and analysis).

27. Although independence of the BSP is clearly prescribed in law, the BSP's Charter specifies the composition of the MB, which includes a member of the Cabinet. Although the Cabinet member has only one vote and there is no evidence of any past political interference in the supervisory decisions taken by the MB, the presence of a senior political appointee to the MB, by definition, gives rise to a concern that the operational independence of the BSP is compromised.

28. The BSP does not have the power to regulate and examine the parent or other affiliate companies of BSP supervised firms. Recently passed legislation provides the BSP with the authority to obtain data from a bank's parent and their related parties outside the banking group for "statistical and policy development purposes in relation to the proper discharge of its functions and responsibilities." However, the BSP has not had cause to use this authority to date, and the scope of the new authority to collect data is limited. It does not provide the BSP with full powers to review the activities of parent companies and of companies affiliated with parent companies.

B. Licensing, Changes in Control, and Acquisitions (CP 4–7)

29. BSP possesses authority to set prudential conditions upon the granting of banking licenses and major acquisitions, but regulations need to be updated in key areas and rendered

[9] S. 81(D) of the Republic Act No. 7653 as amended by Republic Act No. 11211.

consistent with prudential standards. Licensing standards should be updated to provide greater clarity regarding key elements, including especially the examination of the suitability of ultimate beneficial owners and setting objective criteria that ensures all applicants have adequate and consistent governance, internal controls and risk management systems 'in place' upon commencing operations. Internal procedures should mandate on-site examinations upon initiation and more frequent review of newly licensed banks.

30. BSP's legal and regulatory authority and standards regarding transfer of significant ownership or controlling interest and to assess the suitability of beneficial owners need to be clearly established. Current standards requiring approval of transfers of significant ownership or controlling interest are fixed by the NCBA to a 10 percent direct interest in 'voting shares in banks.' Existing regulations lack a definition of ultimate beneficial owner, do not provide clarity in the definition of 'control' or 'significant controlling interest,' and are similarly tied to ownership or control of voting shares. The application of S. 25-A of the NCBA and the lack of regulatory clarity regarding the definition of 'control' or 'significant controlling interest' to include ultimate beneficial ownership, or indirect control of voting shares, impairs BSP's ability to review and approve transfers of significant controlling interests and assess suitability of ultimate beneficial owners.

C. Supervisory Cooperation and Cross Border Supervision (CP 3, 12, 13)

31. BSP has MOAs in place to support information sharing as well as co-operation and co-ordination between both domestic and foreign regulatory authorities. The overseas activities of Philippine banks are not material to their overall operations, but the BSP has established MOAs and less formal information sharing arrangements with relevant host and home countries. Existing regulations and practical arrangements between the BSP and domestic and foreign regulators provide an effective framework for cooperation and collaboration.

32. The majority of D-SIBs are incorporated within conglomerate structures that include non-regulated parent companies and affiliates engaged in non-banking activities, but this 'wider group' is not captured within the BSP's regulatory perimeter. The BSP's on- and off-site supervisory regime assesses the adequacy of a consolidated banking groups' capital and liquidity positions effectively and ensures that RPTs are conducted on an arms-length basis, but this framework does not capture the risks posed to the banking group by companies in the wider group. The BSP has to rely to a large extent on public information for assessing wider group risks as it does not have the power to supervise a bank's parent or its affiliates.

33. As there are financial entities regulated by other domestic agencies outside the consolidated groups regulated by the BSP, the BSP should consider bringing those entities into the relevant consolidated banking groups to enable the BSP to capture the risks they pose to the banking group. In the interim, the BSP should strengthen its coordination with other domestic regulators through the establishment of formal colleges of supervisors to ensure that risks posed by other financial entities are assessed and mitigated adequately. BSP regulated banks within conglomerate structures should also specifically identify all risks arising from companies within their wider group structure in their ICAAP and describe fully the internal controls for reporting and managing such risks.

D. Supervisory Approach (CP 8–10)

34. BSP maintains an effective system of banking supervision that is evolving to enhance current abilities to develop a more forward-looking and risk-based approach to oversight of banks, bank groups and systemically important firms. BSP employs an effective range of examination techniques, tools and reporting requirements to support its supervisory processes and approach. BSP is reviewing its supervisory approach and moving to further refine its examination process to focus more directly on key risks, resiliency and systemic risks, and is working to gain better oversight of risks to safety and soundness that can be imposed upon banks that operate within a large, complex conglomerate structure.

35. BSP's supervisory approach presently does not include an assessment of resolvability of supervised financial institutions, in conjunction with PDIC, to support planning for the orderly resolution of D-SIBs. The assessment of resolvability, in particular of D-SIBs that operate within a conglomerate group, necessarily depends upon an effective framework for early intervention and resolution, as well as the supervisory authority obtaining comprehensive information regarding the bank and banking group and the interconnections and inter-dependencies with the wider conglomerate that may present obstacles to orderly resolution.

E. Corrective and Sanctioning Powers of Supervisors (CP 11)

36. While BSP has an appropriate set of enforcement powers, the timeframes within which the remediation of significant supervisory issues are concluded or resolved can be extensive. BSP issues directives to banks upon completion of the Report of Examination (ROE) and requires bank management to submit an acceptable remediation plan. The bank is required to submit quarterly updates on remediation efforts, and will be assessed for compliance with open directives at the next annual (or greater) examination. Matters can be elevated to require banks to issue written letters of commitment, and such remediation commitments can be revised or amended. Banks with continuing and significant supervisory concerns are placed into PCA and can linger in such status for prolonged periods (years), during which time the banks can remain capital deficient; and firms are not placed into resolution at an early stage and before equity has been exhausted. While BSP has worked to improve the effectiveness of its PCA framework, further work is needed to ensure that unhealthy and poorly managed banks are addressed in a prompt and timely fashion.

37. Limitations on BSP's enforcement powers impair its ability to fully protect the bank from the actions of parent companies and affiliates. Since parent companies and their affiliates fall outside of BSP's regulatory perimeter, direct action against non-regulated entities within the conglomerate group cannot be taken. Available information on conglomerate structure is updated only periodically and there is no requirement that the bank or banking group regularly provide a comprehensive and current view of group-wide interconnections and inter-dependencies; thereby impairing BSP's ability to ring-fence the bank from the actions of parent companies that would be detrimental to the safety and soundness of a bank or banking group operating within the conglomerate structure.

F. Corporate Governance and Internal Audit (CP 14, 26)

38. Corporate governance regulations have been strengthened by the BSP together with a more direct area of on-site supervisory focus, in line with the updated Basel Core Principles. Current supervisory practice of assessing governance is carried out not only during on-site examinations, but through other initiatives such as the working group conducting interviews on corporate culture and conduct. Regulations clearly articulate and hold accountable those with key responsibilities within the bank, placing primary responsibility for ensuring the establishment of an effective risk management framework and controls with boards of directors while ensuring management operates within board approved policies. BSP recognizes the need for proportionality and thereby has set appropriate minimum requirements for less complex banks.

39. BSP's regulations set expectations for banks to demonstrate a strong internal control environment and internal audit function. BSP amended its regulations to address the need for banks to have a strong compliance function and recognizes the importance to review the overall strength of the internal audit program through its on-site examination framework.

G. Capital (CP 16)

40. An appropriate capital framework is in place for the major banks in the Philippine banking sector, with minimum capital ratios and a leverage ratio set at more conservative levels than applicable Basel standards. The capital framework for stand-alone rural, thrift and cooperative banks is in the process of being revised to align more closely with Basel III. The BSP does not directly vary individual banks' capital requirements to reflect their risk profile. The BSP should consider setting individual capital ratios for banks based on their risk profile and introduce a simplified ICAAP for the rural, thrift and cooperative banks.

H. Credit Risk and Problems Assets, Provisions and Reserves (CP 17–18)

41. BSP should develop a center of technical credit risk expertise to ensure it keeps pace with bank's likely progression to more sophisticated credit products/facilities. It will be key for BSP to develop guidance to communicate its expectations on bank's management of internal credit risk models. Further, BSP should contemplate horizontal deep dive credit reviews to ensure it has a deep understanding of bank's credit risk management practices, especially across the D-SIBs.

42. BSP has released adequate guidance on its expectations with respect to banks' asset classification and provisioning requirements. In general, BSP's guidance is in line with IFRS 9 requirements (with the implementation of PFRS 9), however, it will be important for BSP to reassess the adequacy of its guidance pertaining to expected loss provisioning requirements once the SEC has released its guidance. In addition, the BSP will need to update its provisioning requirements for less sophisticated banks to ensure adequate collateral valuation write-off requirements are in line with PFRS 9.

I. Risk Management (CP 19–25)

43. Aspects of banks' risk management practices pertaining to contingency planning will need to be addressed. As BSP moves towards a view on the adequate level of minimum prudential capital and liquidity requirements on a bank-by-bank basis, it will be critical for BSP to update its ICAAP guidance and introduce an ILAAP to ensure it is aligned with current international practices. Further, BSP should separate out the D-SIB recovery plans from the ICAAP to ensure not only that adequate assessments by banks are carried out, but BSP cross D-SIB assessments are carried out. Further, BSP should share these recovery plans with the resolution authority to ensure that it is adequately prepared to effectively deal with a major bank problem or failure.

44. BSP does not impose a single borrower limit on banks at a consolidated level. Assessors note that BSP is currently working on the update of its large exposure guideline that will include the tracking of single borrower and aggregate large exposures on both a solo and consolidated basis. It will also expand the definition of interdependence**,** among other things. The large exposure limits for banks, especially banking groups with a conglomerate group structure, is essential in BSP's ability to effectively supervise and assess the level of interconnectedness risk impacting the bank.

45. An appropriate regulatory framework is in place to ensure banks comply with minimum requirements for liquidity and funding. The BSP has introduced the LCR and NSFR frameworks for the D-SIBs and other major banks and has a simplified liquidity regime for smaller banks. There are weaknesses in the monitoring tools for the LCR, which should be reviewed and aligned more closely with applicable Basel standards, and consideration should be given to introducing an ILAAP framework to enable the BSP to set individual minimum liquidity and funding requirements for the major banks. A monitoring regime for intraday liquidity has recently been introduced.

46. The regulatory framework and supervisory practice for market risk and interest rate risk in the banking book (IRRBB) are appropriate given the level of complexity of the risks being run by banks. The BSP is resourced in terms of both numbers and levels of expertise to supervise banks' market risk functions effectively. There are proposals in hand to update both the market risk and IRRBB frameworks.[10] When in place, both regimes will be better aligned to applicable Basel standards.

J. Disclosures and Transparency (CP 27–28)

47. **The BSP prescribes detailed public disclosure requirements for banks on both a consolidated and solo basis and verifies that these requirements are met.** The disclosure regime is not as comprehensive as the current BCBS Pillar 3 framework in terms of the scope and detail of coverage required across a number of risk elements (e.g., for NSFR, market risk, IRRBB and remuneration), but the current disclosure regime is in the process of being revised to align it more closely to the Basel Pillar 3 regime. Banks' financial reporting requirements are in accordance with international standards.

K. Abuse of Financial Services (CP 29)

48. **Although BSP's supervisory oversight of bank's compliance with AML/CFT requirements remains strong, certain components of the regulatory framework need to be strengthened.** BSP has made a concerted effort to effectively utilize its contingent of AML experts, however, it must ensure adequate resources are available to cover all banking institutions and other entities (e.g., MSBs) under its mandate. Further, although BSP makes use of its enforcement tools (issuing directives, letters of commitment, etc.), it needs to ensure it is effectively utilizing its monetary penalty regime for AML/CFT non-compliance issues on a consistent basis.

DETAILED ASSESSMENT

49. **This assessment is based on the current state of the implementation of the Basel Core Principles for Effective Banking Supervision (BCP) in the Philippines.** The BCP assessment mission took place from June 19 to July 9, 2019. Regulatory initiatives after the assessment date have not been taken into account.

50. **The ratings assigned during this assessment are not directly comparable to those from the previous assessment.** The methodology issued by the Basel Committee on Banking Supervision (BCBS) September 2012 was used for the current assessment and the authorities have opted to be assessed and graded on the essential criteria (EC) only. The 2002 BCP assessment, prepared in the context of the 2002 FSAP, as well as the focused follow-up report prepared in 2010 was based on the previous methodology. Since then, the methodology has been revised leading to some substantive changes.

51. **The 2012 methodology reflects lessons from the global financial crisis (GFC) and emerging supervisory best practices.** New principles have been added to the methodology along with new EC for each principle that provide more detail. Altogether, the revised Basel Core Principles

[10] See footnote 2.

(BCPs) now contain 247 separate essential and additional criteria against which a supervisory agency may be assessed. In particular, the revised BCPs strengthen the requirements for supervisors, the approaches to supervision and supervisors' expectations of banks. While the BCPs set out the powers that supervisors should have to address safety and soundness concerns, there is a heightened focus on the actual use of the powers, in a forward-looking approach through early intervention.

52. The assessment team reviewed the framework of laws, rules, and guidance and held extensive meetings with authorities and market participants. The assessment team met officials of the BSP, the DOF, Bureau of the Treasury, PDIC, auditing firms, Board of Accountancy and SEC Oversight Assurance Committee and banking sector participants. The authorities provided a comprehensive self-assessment of the BCPs, as well as detailed responses to additional questionnaires, and facilitated access to staff and to supervisory documents and files on a confidential basis.

53. The standards were evaluated in the context of the sophistication and complexity of the financial system of the Philippines. The BCPs must be capable of application to a wide range of jurisdictions whose banking sectors will inevitably include a broad spectrum of banks. To accommodate this breadth of application, a proportionate approach is adopted within the BCP, both in terms of the expectations on supervisors for the discharge of their own functions and in terms of the standards that supervisors impose on banks. An assessment of a country against the BCPs must, therefore, recognize that its supervisory practices should be commensurate with the complexity, interconnectedness, size, and risk profile and cross-border operation of the banks being supervised. In other words, the assessment must consider the context in which the supervisory practices are applied. The concept of proportionality underpins all assessment criteria. For these reasons, an assessment of one jurisdiction will not be directly comparable to that of another.

54. An assessment of compliance with the BCPs is not, and is not intended to be, an exact science. Reaching conclusions required judgments by the assessment team. Banking systems differ from one country to another, as do their domestic circumstances. Furthermore, banking activities are undergoing rapid change after the GFC, prompting the evolution of thinking on, and practices for, supervision. Nevertheless, by adhering to a common, agreed methodology, the assessment should provide the authorities with an internationally consistent measure of the quality of their banking supervision in relation to the revised BCPs, which are internationally acknowledged as minimum standards.

55. The team appreciated the very high quality of cooperation received from the authorities. The team extends its warm thanks to staff of the authorities, who provided excellent cooperation, including provision of documentation and technical support.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions	
Principle 1	**Responsibilities, objectives and powers.** An effective system of banking supervision has clear responsibilities and objectives for each authority involved in the supervision of banks and banking groups. [/1] A suitable legal framework for banking supervision is in place to provide each responsible authority with the necessary legal powers to authorize banks, conduct ongoing supervision, address compliance with laws and undertake timely corrective actions to address safety and soundness concerns.[/2]
Essential criteria	
EC1	The responsibilities and objectives of each of the authorities involved in banking supervision [/3] are clearly defined in legislation and publicly disclosed. Where more than one authority is responsible for supervising the banking system, a credible and publicly available framework is in place to avoid regulatory and supervisory gaps.
Description and findings re EC1	The Bangko Sentral ng Pilipinas (BSP) is the primary banking supervisory authority in the Philippines, but the Philippine Deposit Insurance Corporation (PDIC) also has a supervisory role in law. The Memorandum of Arrangement (MOA) which sets out their respective responsibilities of the two authorities has not been disclosed in public. The BSP was established under Article XII, S. 20 of the 1987 Constitution of the Republic of the Philippines. This specified that the BSP should "provide policy direction in the areas of money, banking, and credit and shall have supervision over the operations of banks and exercise such regulatory powers as may be provided by law over the operations of finance companies and other institutions performing similar functions". S. 3 of Republic Act (RA) No. 7653 or the "New Central Bank Act" (NCBA), as amended by RA No. 11211, gives force to this constitutional mandate, and provides the BSP with the power to supervise the operations of banks and to exercise such regulatory and examination powers over the quasi-banking operations of non-bank financial institutions as mandated by the Monetary Board (MB) of the BSP. Quasi-banks are defined as entities engaged in the borrowing of funds through the issuance, endorsement or assignment with recourse or acceptance of deposit substitutes for purposes of relending and purchasing of receivables and other obligations. S. 3 of the NCBA, as amended, also requires the BSP to promote financial stability. The mandate of the PDIC is set out in the RA No. 3591, as amended. It has the power to conduct joint examinations with the prior agreement of the BSP, and to appoint its own independent experts (RA No. 9302) to investigate frauds or other irregularities arising from BSP or PDIC examinations. The PDIC also has enforcement powers against banks. When an examination by the PDIC identifies unsafe or unsound practices by a bank or its directors, the examination report is submitted to the MB to secure corrective action. ____- [1/] In this document, "banking group" includes the holding company, the bank and its offices, subsidiaries, affiliates and joint ventures, both domestic and foreign. Risks from other entities in the wider group, for example non-bank (including non-financial) entities, may also be relevant. This group-wide approach to supervision goes beyond accounting consolidation. [2/] The activities of authorising banks, ongoing supervision and corrective actions are elaborated in the subsequent Principles. [3/] Such authority is called "the supervisor" throughout this paper, except where the longer form "the banking supervisor" has been necessary for clarification.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	If no such corrective action is taken by the MB within forty-five days from its submission, the PDIC may itself institute whatever corrective action it deems necessary. This may involve a cease and desist order or require the bank or its directors to correct the practices or violations identified within forty-five days. If the practice is likely to cause insolvency or substantial dissipation of assets or earnings of the bank, the period to take corrective action is reduced to fifteen days. The PDIC is required to inform the MB of any action it has taken. In practice, the PDIC does not have the resources to undertake examinations of banks unless jointly with the BSP and is unlikely, therefore, to undertake its own enforcement action. The MOA signed between the BSP and PDIC sets out the co-ordination, co-operation and data sharing arrangements between the two agencies; provides for the two parties to notify each other of the examinations planned in the year ahead; allows for joint examinations to be conducted; and for the two bodies to harmonize their examination procedures and reports. The MOA has not been made public, but its contents are not of a confidential nature. The MOA between the BSP and PDIC should be made public to provide greater transparency around the responsibilities of the two authorities. Co-operative enterprises are licensed by the Cooperative Development Agency (CDA), but the enterprises require prior BSP approval should they wish subsequently to become banks. The BSP is responsible for the supervision of all co-operative banks, but there are no formal co-ordination or data sharing arrangements in place between the two agencies. See BCP 3 for details of cooperation with domestic and overseas regulators.
EC 2	The primary objective of banking supervision is to promote the safety and soundness of banks and the banking system. If the banking supervisor is assigned broader responsibilities, these are subordinate to the primary objective and do not conflict with it.
Description and findings re EC2	Although prevailing legislation does not specify the promotion of safety and soundness of banks and the banking system as a primary objective of the BSP, S. 4 of the General Banking Law of 2000 (GBL) sets out the following banking supervisory functions of the BSP. These have the intent of promoting the safety and soundness of banks: • issuance of rules of conduct or the establishment of standards of operation for uniform application to all institutions or functions covered; • conduct of examinations to determine compliance with laws and regulations if the circumstances so warrant as determined by the MB; • overseeing to ascertain that laws and regulations are complied with; • regular investigation which shall not be more often than once a year from the last date of examination to determine whether an institution is conducting its business on a safe or sound basis; • inquire into the solvency and liquidity of the institution; and • enforcing prompt corrective action. The BSP has separate objectives to promote financial and price stability, but these do not conflict with its primary banking supervisory role.
EC3	Laws and regulations provide a framework for the supervisor to set and enforce minimum prudential standards for banks and banking groups. The supervisor has the power to

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	increase the prudential requirements for individual banks and banking groups based on their risk profile /4 and systemic importance./5
Description and findings re EC3	S. 108 of the NCBA, as amended, provides the BSP with the power to prescribe minimum capital ratios for banks. It also provides the BSP with the power to vary individual banks' capital ratios commensurate to their risk profile, although the BSP has not done so to date. It has, however, raised the risk weighting of certain higher risk assets above international standards, which has had the effect of raising the minimum capital ratios of banks holding those assets (e.g., Circulars Nos. 468 and 469 imposed capital charges on banks' investments in securitization and structured products, respectively to serve as a disincentive for banks to hold too much of such instruments), and it has applied higher minimum capital ratios for D-SIBs. See BCP 16.
EC4	Banking laws, regulations and prudential standards are updated as necessary to ensure that they remain effective and relevant to changing industry and regulatory practices. These are subject to public consultation, as appropriate.
Description and findings re EC4	There is considerable evidence to suggest that the BSP updates its banking supervisory legislation and regulations on a regular and structured basis. A number of core Basel III elements have been introduced in the past three years (e.g., capital definition amendments; higher capital minima requirements; Liquidity Coverage Ratio (LCR); leverage ratio; and the framework for D-SIBs), in addition to amendments to core banking supervision legislation (e.g., RA No. 11211) and numerous guidelines (e.g., operational risk management and outsourcing; related party transactions; internal control and internal audit; BSP supervisory enforcement policy; sound credit risk management and IT risk management; and definition of past due and nonperforming loans; among others). All changes to laws and regulations are subject to public consultation with industry. Although the requirement of 10 working days for the consultation period on new regulations appears short, in practice the BSP conducts extensive and effective consultation with all relevant stakeholders during the development process of new regulations. Requests for additional time to respond during the formal consultation period are common and invariably agreed. This was endorsed in discussions with banks.
EC5	The supervisor has the power to: (a) have full access to banks' and banking groups' Boards, management, staff and records in order to review compliance with internal rules and limits as well as external laws and regulations; (b) review the overall activities of a banking group, both domestic and cross-border; and, (c) Supervise the activities of foreign banks incorporated in its jurisdiction.
Description and findings re EC5	In relation to EC element (a), S. 3 and S. 4 of the GBL provide the BSP with the power to conduct examinations of banks, and S. 25 of the NCBA specifically provides the BSP with the authority to compel the presentation of all books, documents, paper or records necessary to ascertain the true condition of any bank.

/4 In this document, "risk profile" refers to the nature and scale of the risk exposures undertaken by a bank.

/5 In this document, "systemic importance" is determined by the size, interconnectedness, substitutability, global or cross-jurisdictional activity (if any), and complexity of the bank, as set out in the BCBS paper on *Global systemically important banks: assessment methodology and the additional loss absorbency requirement*, November 2011.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	However, S. 2 of RA No. 1405, otherwise known as the Law on Secrecy of Bank Deposits, states that all bank deposits with banking institutions in the Philippines are considered to be of an absolutely confidential nature and may not be examined, inquired or looked into by any person, including the BSP, except in the following circumstances: (1) Written permission or consent in writing by the depositor; (2) The BSP can examine bank accounts in the course of its periodic or special examination regarding compliance with Anti-Money Laundering Law; (3) The Anti-Money Laundering Council ("AMLC") can examine bank accounts pursuant to a court order, where there is probable cause that the deposits are related to an unlawful activity or money laundering offense; and, (4) The AMLC can examine bank accounts, without a court order, where there is probable cause that the deposits are related to certain crimes such as kidnapping for ransom, violation of the Dangerous Drugs Act, hijacking, destructive arson, murder and violations inimical to civil aviation. Similarly, S. 8 of RA No. 6426, as amended, ("the Foreign Currency Deposit Act of the Philippines") considers all foreign currency deposits of a confidential nature. Except with the written permission of the depositor, foreign currency deposits may not be examined, inquired or looked into by any person, government official, bureau or office whether judicial or administrative or legislative, or any other entity whether public or private. Notwithstanding that Section 8 of RA No 3591 (The Philippine Deposit Insurance Corporation Charter) provides that the BSP may inquire into or examine deposit accounts and all information related thereto in case there is a finding of unsafe or unsound banking practice, the constraints imposed by these two Acts hinder effective supervision (e.g., identifying funding concentrations from related parties, intra-group dependencies, cash flow analysis, relationship to RPT and off-site AML data and analysis). BSP should be granted unimpaired access to information on all customer accounts at all times and the ability, without constraints, to employ and share depositor information for any prudential purpose in order to fulfill its supervisory mandate to address safety and soundness concerns. There are a number of bills filed in the Houses of Representatives and the Senate of the Philippines proposing various amendments to/repeal of the Law on Secrecy of Bank Deposits and the Foreign Currency Deposit Act. If passed, these would remove the hindrances to effective supervision. Regarding EC elements (b) and (c), S. 3, 4 and 6 of the GBL provide the BSP with the power to supervise all entities which undertake banking or quasi-banking operations in the Philippines, including foreign branches.
EC6	When, in a supervisor's judgment, a bank is not complying with laws or regulations, or it is or is likely to be engaging in unsafe or unsound practices or actions that have the potential to jeopardize the bank or the banking system, the supervisor has the power to: (a) take (and/or require a bank to take) timely corrective action; (b) impose a range of sanctions; (c) revoke the bank's license; and (d) cooperate and collaborate with relevant authorities to achieve an orderly resolution of the bank, including triggering resolution where appropriate.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	Circular No. 875 sets out the BSP's Supervisory Enforcement Policy, S. IV of which sets out the following three categories of supervisory action available to the BSP: i) Corrective Actions Corrective actions are enforcement actions intended to require a bank to address any underlying cause of supervisory issues, concerns and problems. These include the following: - BSP Directives Directives are orders and instructions requiring a bank to undertake a specific positive action or refrain from performing a particular activity within a prescribed timeline. - Letter of Commitment (LOC) The LOC is an enforcement action where a bank's Board is required to make a written commitment to undertake a specific positive action or refrain from performing a particular activity within a given time period. The LOC is generally used to arrest emerging supervisory concerns before these develop into serious weaknesses or problems, or to address remaining supervisory issues and concerns. ii) Sanctions Sanctions that may be imposed on a bank and/or its directors and officers are subject to the prior approval and/or confirmation by the MB. Such sanctions include the following: On a bank: • Restrictions on activities and privileges; • Suspension of authorities and other activities; • Divestment and/or unwinding; • Fines. On Directors and officers: • Reprimand; • Restriction on Compensation and Benefits; • Divestment; • Suspension; • Disqualification; • Removal; • Monetary Penalties/Fines. iii) Other Supervisory Actions Subject to prior MB approval, the BSP may deploy other supervisory actions such as (i) Initiation into the PCA Framework; (ii) Issuance of a cease and desist order (CDO) against both the bank and its directors and officers; (iii) Conservatorship; and (iv) Placement under Receivership. See BCP 11 for details.
EC7	The supervisor has the power to review the activities of parent companies and of companies affiliated with parent companies to determine their impact on the safety and soundness of the bank and the banking group.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC7	The BSP does not have the power to regulate the parent company or other affiliate companies of BSP supervised institutions. The recently approved RA No. 1121 provides the BSP with a new authority to obtain data and information from any person or entity for 'statistical and policy development purposes in relation to the proper discharge of its functions and responsibilities'. This authority permits the BSP to obtain data from a bank's parent company and its affiliates, but the BSP has not had cause to use this authority to date, and the stated scope of the new authority for 'statistical and policy development purposes' is limited. It does not provide the BSP with full powers to review the activities of parent companies and of companies affiliated with parent companies. The BSP should have the legal authority to undertake such activities to determine their impact on the safety and soundness of the bank and the banking group. Since the majority of BSP designated D-SIBs are incorporated within a conglomerate structure that includes non-regulated parent companies and affiliates engaged in non-banking activities, an important feature of the BSP's supervisory practice is its ability to fully determine the impact of such non-regulated entities upon the safety and soundness of the banking group, or to provide supervisory oversight and control over significant inter-dependencies. This issue is covered in BCP 12 (EC1).
Assessment of Principle 1	Materially Non-Compliant
Comments	A significant weakness in the legislative and regulatory framework arises from the bank secrecy laws, which constrain the ability of the BSP to conduct effective ongoing supervision of banks. The laws state that all bank deposits with banking institutions in the Philippines are considered to be of an absolutely confidential nature and may not be examined, inquired or looked into by any person, including the BSP, except in defined circumstances. BSP should be granted unimpaired access to information on depositors and given the ability, without constraints, to employ and share depositor information for any prudential purpose (e.g., funding concentrations from related parties, intra-group dependencies, cash flow analysis, RPT and off-site AML data and analysis) in order to fulfill its supervisory mandate to address safety and soundness concerns. The BSP does not have the power to review and examine the parent or other affiliate companies of BSP supervised firms, although recently passed legislation provides it with authority to obtain data from such entities for 'statistical and policy development purposes in relation to the proper discharge of its functions and responsibilities. However, the BSP has not had cause to use this authority to date, and the stated scope of the new authority for 'statistical and policy development purposes' is limited. It does not provide the BSP with full powers to review the activities of parent companies and of companies affiliated with parent companies. Current legislation does not delineate clearly the respective responsibilities and objectives of the BSP, as primary supervisor of banks, and the PDIC, which also has supervisory and enforcement roles over banks in certain situations. The two authorities have signed a MOA which sets out their respective responsibilities and information sharing arrangements, but it is not a public document. The BSP and CDA do not have a formalized coordination and data-sharing agreement.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	Recommendations: • Amend the bank secrecy laws to grant BSP full access to banks' deposit and other data; • Provide BSP with the legal authority to review the activities of a bank's parent companies and of companies affiliated with parent companies' activities to determine their impact on the safety and soundness of the bank and the banking group; • Make the MOA between the BSP and PDIC public to provide greater transparency around the responsibilities of the two authorities; and • Establish a bilateral agreement between the BSP and CDA to formalize co-ordination and data-sharing arrangements between the two authorities.
Principle 2	**Independence, accountability, resourcing and legal protection for supervisors**. The supervisor possesses operational independence, transparent processes, sound governance, budgetary processes that do not undermine autonomy and adequate resources, and is accountable for the discharge of its duties and use of its resources. The legal framework for banking supervision includes legal protection for the supervisor.
Essential criteria	
EC1	The operational independence, accountability and governance of the supervisor are prescribed in legislation and publicly disclosed. There is no government or industry interference that compromises the operational independence of the supervisor. The supervisor has full discretion to take any supervisory actions or decisions on banks and banking groups under its supervision.
Description and findings re EC1	The legislative framework clearly prescribes the operational independence of the BSP S.20, Article XII, of the 1987 Constitution specifies that the BSP should be independent and that it should be free from all undue control and influence, including from the State or the government and particularly from the executive. It should not be under the executive branch of the government, nor should it be interfered with by other government agencies. S.1 of RA No. 7653 also provides that the State shall maintain a central monetary authority that shall function and operate as an independent and accountable body corporate in the discharge of its mandated responsibilities concerning money, banking and credit. Although independence of the BSP is clearly prescribed in law, S. 6 of the NCBA, as amended, specifies the composition of the MB, which includes a member of the Cabinet. Although the Cabinet member has only one vote and there is no evidence of any past political interference in the supervisory decisions taken by the MB, the presence of a senior political appointee to the MB, by definition, gives rise to a concern that the operational independence of the BSP is compromised. The NCBA, as amended, does not specify the role or responsibility of the Cabinet member. In terms of accountability, the Governor and executive members of the BSP are required to report to Congress, as and when requested, to account for any supervisory actions taken, and S. 39 and 40 of the NCBA, as amended, specify the publication timelines and scope of formal reports to the President and Congress on the actions of the BSP. The governance arrangements of the BSP are set out in S. 3 of the NCBA, as amended, and S. 4 of the GBL. These provide the BSP with full discretion and authority to supervise the operations of banks and to take actions as necessary.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Supervisory actions taken by the BSP may only be challenged in court through judicial review on the basis that any such actions were taken unlawfully.
EC2	The process for the appointment and removal of the head(s) of the supervisory authority and members of its governing body is transparent. The head(s) of the supervisory authority is (are) appointed for a minimum term and is removed from office during his/her term only for reasons specified in law or if (s)he is not physically or mentally capable of carrying out the role or has been found guilty of misconduct. The reason(s) for removal is publicly disclosed.
Description and findings re EC2	S. 6 of the NCBA specifies the membership of the MB and the terms of their appointment. It states that the MB will be composed of seven members that are appointed by the President of the Philippines for a term of six years. No member may be reappointed more than once. The members of the MB are composed of the following: (a) the Governor of the BSP, who shall be the Chairman (full time member); (b) a Cabinet member; and, (c) five members of the private sector (full time members). The Secretary of the Department of Finance (DOF) is currently the Cabinet member designated to represent the Government in the MB. S. 8, 9 and 10 of the NCBA, as amended, set out the qualifications, disqualifications and grounds for removal of members of the MB, respectively. S. 10 specifies that the President may remove any member of the MB if he is physically or mentally incapacitated that he cannot properly discharge his duties and responsibilities and such incapacity has lasted for more than six months. No member of the MB has been dismissed by a President to date. Although it is expected that any such dismissal would be made public, an obligation to disclose publicly the reason(s) for the dismissal of the Head of the MB should be incorporated in law.
EC3	The supervisor publishes its objectives and is accountable through a transparent framework for the discharge of its duties in relation to those objectives./6
Description and findings re EC3	The BSP issues an annual report which sets out, *inter alia*, key regulatory and supervisory developments over the year and commentary on the Philippine banking sector. In addition, the BSP issues an annual Financial Stability Report which highlights the macroprudential risks facing the sector and a range of other reports on the activities of the BSP, including on financial stability and banking supervision, throughout the year. S. 39 and 40 of the NCBA, as amended, specify the scope and publication timelines of these reports.
EC4	The supervisor has effective internal governance and communication processes that enable supervisory decisions to be taken at a level appropriate to the significance of the issue and timely decisions to be taken in the case of an emergency. The governing body is structured to avoid any real or perceived conflicts of interest.
Description and findings re EC4	S. 17 of the NCBA, as amended, specifies the powers and duties of the Governor of the BSP, which include the power to delegate authority throughout the BSP. Specifically, the Governor is given power to direct and supervise the operations and internal administration of the BSP, including delegating certain of his administrative responsibilities to other officers. Office Order No. 57, as amended, gives effect to this power. 6/ Please refer to Principle 1, Essential Criterion 1.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	It sets out the delegated approval and signing authorities of banking supervisory officials with the aim of ensuring that supervisory decisions are taken at the appropriate level of seniority. The MB is appropriately structured to avoid conflicts of interest. As noted in EC2, the MB comprises five individuals from the private sector in addition to the Governor and the Cabinet minister. Members are disqualified from being a director, officer, employee, consultant, lawyer, agent or stockholder of any bank, quasi-bank or any other institution which is subject to supervision or examination by the BSP. A member is required to resign from and divest himself of any and all interests in such institution before assumption of office as member of the MB. The members of the MB coming from the private sector shall not hold any other public office or public employment during their tenure. No person shall be a member of the MB if he has been connected directly with any multilateral banking or financial institution or has a substantial interest in any private bank in the Philippines, within one-year prior of his appointment. Similarly, no member of the MB shall be employed in any such institution within two years after the expiration of his term except when he serves as an official representative of the Philippine Government to such an institution.
EC5	The supervisor and its staff have credibility based on their professionalism and integrity. There are rules on how to avoid conflicts of interest and on the appropriate use of information obtained through work, with sanctions in place if these are not followed.
Description and findings re EC5	The BSP has an extensive training program in place for all supervisory staff—see EC7. It aims to equip every supervisor with the necessary knowledge and skills for the effective and efficient conduct of the BSP's banking supervision mandate. Courses have been developed in-house by subject matter experts, with guidance from experienced international banking supervision experts provided under an IMF Technical Assistance Program. The training program is tailored to the needs of supervisors based on their level of expertise, of which there are four categories: Entry, Intermediate, Advanced and Expert level courses. Courses are linked to the BIS Financial Stability Institute Connect learning program. Discussions with contacts in the banking industry confirm that BSP staff are suitably qualified and provide effective challenge during examinations and ongoing supervisory contact. The integrity of BSP staff is undoubted. BSP officials and employees conform to the provisions of RA No. 6713, which sets out the Code of Conduct and Ethical Standards for public officials and employees. The Act requires all BSP staff to: (a) Discharge their duties with utmost responsibility; (b) Act with patriotism and justice; (c) Lead modest lives; and, (d) Uphold the public interest over personal interest. In addition, a Code of Ethics issued under Office Order Nos. 2014-484 to 486 requires all BSP staff to observe the highest standards of professional ethics and to avoid any situation that may result in an actual conflict of interest or even the appearance of conflict of interest in performing official duties. BSP staff are not allowed to disclose or misuse confidential or classified information, officially known to them by reason of their office and not made

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	available to the public, to further their private interests or give undue advantage to anyone, or to prejudice public interest. S. 27 of the NCBA, as amended, prohibits BSP staff from being an officer, director, lawyer or agent, employee, consultant or stockholder, directly or indirectly, of any institution subject to supervision or examination by the BSP. They are also prohibited from requesting or receiving any gift, present or pecuniary or material benefit from any BSP supervised institution. Moreover, BSP personnel are not allowed to reveal in any manner, except under orders of the court, the Congress or any government office or agency authorized by law, or under such conditions as may be prescribed by the MB, information relating to the condition or business of any such institution. Under S. 27 of the NBCA, as amended, BSP staff are prohibited from borrowing from any institution subject to supervision or examination by the BSP unless the borrowing is transacted on an arm's length basis, fully disclosed to the MB, and subject to any rules and regulations as the MB may prescribe.
EC6	The supervisor has adequate resources for the conduct of effective supervision and oversight. It is financed in a manner that does not undermine its autonomy or operational independence. This includes: (a) a budget that provides for staff in sufficient numbers and with skills commensurate with the risk profile and systemic importance of the banks and banking groups supervised; (b) salary scales that allow it to attract and retain qualified staff; (c) the ability to commission external experts with the necessary professional skills and independence, and subject to necessary confidentiality restrictions to conduct supervisory tasks; (d) a budget and program for the regular training of staff; (e) a technology budget sufficient to equip its staff with the tools needed to supervise the banking industry and assess individual banks and banking groups; and (f) a travel budget that allows appropriate on-site work, effective cross-border cooperation and participation in domestic and international meetings of significant relevance (e.g., supervisory colleges).
Description and findings re EC6	The BSP is adequately resourced to conduct effect banking supervision. Line-side supervision is conducted by Financial Supervision Sub-sectors I, II and III (FSSS). There are nine (9) supervisory Departments in the three sub-sectors. Following a restructuring that took effect from January 2019, eight (8) departments are responsible for the supervision of a mix of universal, commercial and smaller banks. On-site and off-site supervision of each bank is conducted in each team. A separate team of experts in treasury, capital markets, fund management investment management activities forms part of a Policy and Specialized Supervision Sub-sector. It assesses market, IRRBB, liquidity, operational and counterparty credit risks run by banks. The current staffing complement of front-line supervisors in FSSS is 682, which is considered by assessors to be well resourced. The BSP is financed solely from income generated from its own operations and, as such, is not dependent on Congress for financial support. This fiscal autonomy provides

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	operational independence and full flexibility to allocate resources and to determine recruitment and remuneration policies as required. Specifically: (a) The annual budget process is well structured. It considers the adequacy of staffing resources, in terms of both quality and quantity, for the subsequent financial year; (b) Recruitment salaries and the overall package offered by the BSP are very competitive. This was confirmed in discussions with the commercial banks. Turnover levels are low; (c) S. 58 of the GBL provides the BSP with the power to commission external experts to conduct specific tasks. Budgetary resources are available for such commissions which have been used in the past (e.g., the Bangladesh Bank case); (d) See EC7; (e) The BSP has an ambitious program for IT development to improve the efficiency of the supervisory process (e.g., R2A and a new Financial Institution portal). Discussions suggest that there are adequate funds for IT development; (f) Annual travel budgets are set to accommodate international commitments to supervise the overseas operations of Philippine banks and for overseas training commitments.
EC7	As part of their annual resource planning exercise, supervisors regularly take stock of existing skills and projected requirements over the short- and medium-term, taking into account relevant emerging supervisory practices. Supervisors review and implement measures to bridge any gaps in numbers and/or skill sets identified.
Description and findings re EC7	See EC6(A) above. The BSP undertakes a comprehensive annual budget process, which includes a review of the adequacy of staffing, both in terms of quantity and quality. It has a comprehensive training program for all supervisory staff, directed by its training arm, the BSP Institute (BSPI). The BSPI's training framework has four categories: 1. Entry—Courses A to C designed for new employees, including those with professional designations such as certified public accountants. The course covers (i) basic economic concepts, (ii) the business of banking, (iii) purposes and functions of the central bank, and (iv) organization and function of the sector; 2. Intermediate—Courses D to H are designed for examination professional employees with previous experience in the financial services sector; 3. Advanced—Courses I to L signal the completion of the standard training program for most examination professionals; and, 4. Expert—Courses M to P are designed for employees whose technical and behavioral skill sets have been recognized by management to be complete in all material respects. Courses at this level are designed to advance unique skill sets beyond those of the rank-and-file examiner, analyst or manager. See BCP17 and BCP22 EC1 respectively for commentaries on credit and market risk expertise in the BSP.
EC8	In determining supervisory programmes and allocating resources, supervisors take into account the risk profile and systemic importance of individual banks and banking groups, and the different mitigation approaches available.
Description and findings re EC8	The BSP aims to adopt a risk-based approach to supervision, applying greater resources to those banks which pose the greatest risk, but all banks, including the smallest, are currently subject to annual examination. This model is in the process of being amended. See BCP 8,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC8	The BSP is introducing a supervisory model which will vary the timing of bank examinations according to the risk profile and systemic importance of the bank. The supervisory division was restructured in early 2019 to combine on-site and off-site teams to facilitate the move to a more risk-based approach to bank examinations and to enhance its approach to consolidated supervision.
EC9	Laws provide protection to the supervisor and its staff against lawsuits for actions taken and/or omissions made while discharging their duties in good faith. The supervisor and its staff are adequately protected against the costs of defending their actions and/or omissions made while discharging their duties in good faith.
Description and findings re EC9	S. 15 (e) of the NCBA, as amended, indemnifies all BSP staff against all costs and expenses reasonably incurred in connection with any civil or criminal action, suit or proceedings to which (s)he may be, or is, made a party by reason of the performance of his/her functions or duties, unless (s)he is finally adjudged in such action or proceeding to be liable for negligence or misconduct. The legal protection under Section 15 (e) of the NCBA, as amended, continues even after the officer/employee has already left the BSP, provided that the suit was filed in connection with the performance of official functions. This is governed by BSP Office Order No. 212, Series of 1997, which provides that the right to indemnification shall apply even if the BSP official or personnel has retired or resigned from the BSP. Under the guidelines, the right to indemnity is also applicable even if the case was filed after the retirement or resignation of the BSP official or personnel.
Assessment of Principle 2	Largely Compliant
Comments	The BSP has full discretion to take any supervisory actions or decisions on banks and banking groups under its supervision and is adequately resourced to carry out those duties. Although there is no evidence of any past political interference in supervisory decisions taken by the MB, the operational independence of the BSP is compromised by the attendance of a member of the Cabinet on the MB. Recommendations: • Amend the Charter of the BSP to revisit the position of the Cabinet Member as a voting member of the MB; • Amend the NCBA to require public disclosure of the reason(s) for dismissal of the Head of the MB.
Principle 3	**Cooperation and collaboration.** Laws, regulations or other arrangements provide a framework for cooperation and collaboration with relevant domestic authorities and foreign supervisors. These arrangements reflect the need to protect confidential information.[7]
Essential criteria	
EC1	Arrangements, formal or informal, are in place for cooperation, including analysis and sharing of information, and undertaking collaborative work, with all domestic authorities with responsibility for the safety and soundness of banks, other financial institutions and/or the stability of the financial system. There is evidence that these arrangements work in practice, where necessary.

[7] Principle 3 is developed further in the Principles dealing with "Consolidated supervision" (12), "Home-host relationships" (13) and "Abuse of financial services" (29).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	The legal framework is in place for co-operation and information sharing between domestic regulatory agencies. S. 3 of RA No. 7653, as amended by RA No. 11211, mandates the BSP to promote and maintain financial stability by working closely with authorities including the DOF, the Securities and Exchange Commission (SEC), the Insurance Commission (IC) and the Philippine Deposit Insurance Corporation (PDIC). Two bodies have been established to promote coordination and information sharing between these domestic regulatory bodies. The Financial Stability Coordination Council (FSCC) was established in January 2014 to identify, manage, prevent or address external and internal shocks and pressures on the Philippine financial system. It comprises representatives of the BSP, SEC, the IC, the PDIC, and the DOF. The Financial Sector Forum (FSF) was established in July 2004, by the heads of the BSP, SEC, IC and the PDIC to provide an institutional framework for coordinating the supervision and regulation of the financial system. It has a specific mandate to exchange information and to coordinate the regulatory and supervisory policies of its members. The FSF meets formally every two months but ad hoc meetings may be convened as and when required. Multilateral MOAs have been signed by FSF Member Agencies to provide for the exchange and sharing of relevant reports, information and data.[/8] The BSP has also signed bilateral MOAs with the SEC, PDIC and IC. The SEC MOA outlines arrangements to share information on entities that fall under the jurisdiction of both agencies and to consult each other on their respective findings. It also provides for the SEC and the BSP to conduct joint examinations of non-bank financial institutions (NBFIs) to ensure that regulatory gaps do not occur, although no such joint examinations have been undertaken to date. The MOA with the PDIC provides a framework for the two bodies to conduct on-site examinations jointly, or independently, and to share and exchange relevant reports, significant information and preliminary findings on individual banks—see EC5. The MOA with the IC provides the BSP with the authority to examine an insurance company which is a subsidiary or affiliate of a regulated bank. It also provides for both parties to share reports and information which are necessary for the effective implementation of their respective functions. Reviews of minutes of FSF minutes revealed wide and comprehensive discussion of systemic issues and clear exchange and challenge of views between regulatory agencies. Although there is no MOA between the BSP and the CDA, there is a working group composed of members from the BSP and the CDA that periodically meet to discuss issues and concerns on cooperative banks. A formal MOA should be agreed between the two bodies. A number of banking groups in the Philippines are subject to regulation by more than two domestic supervisory bodies. There is evidence to suggest that there is effective coordination by the BSP with other domestic bodies on a bilateral basis, but there is no framework for the BSP to convene colleges of supervisors with domestic supervisors when two or more regulators are involved. In due course, the BSP should consider establishing formal colleges of supervisors with the SEC, PDIC and IC as and when the supervisory regimes in the SEC and IC are applicable.[/9]

[8/] An amendment to the FSF multilateral MOA on Information Exchange was signed in February 2020.

[9/] A MOA establishing college arrangements to share information between domestic regulators was signed in February 2020.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC2	Arrangements, formal or informal, are in place for cooperation, including analysis and sharing of information, and undertaking collaborative work, with relevant foreign supervisors of banks and banking groups. There is evidence that these arrangements work in practice, where necessary.
Description and findings re EC2	Guidelines for the exchange of information between the BSP and relevant foreign supervisory bodies were agreed by the MB in July 2004. These provide for home supervisory counterparts to access BSP examination reports and other information of foreign-based banks in the Philippines without the prior approval of the MB. In addition, the BSP has formal MOU and informal information sharing arrangements with most of the overseas jurisdictions in which Philippine banks are active. These include the United Kingdom, Taiwan Province of China, China, Hong Kong, SAR, and Thailand. The BSP is also a signatory to the Multilateral MOU between Members of the Australia and New Zealand Banking Group Supervisory College. The BSP is in technical discussions with US counterparts for a possible MOU on home-host supervisory coordination. The MOU with the German regulator (BaFin) is redundant as supervisory responsibility for the relevant foreign branch has passed to the European Union's Single Supervisory Mechanism (SSM). The MOU needs to be reviewed. Evidence was sighted from correspondence of effective communication between the BSP and foreign regulators on a bilateral basis.
EC3	The supervisor may provide confidential information to another domestic authority or foreign supervisor but must take reasonable steps to determine that any confidential information so released will be used only for bank-specific or system-wide supervisory purposes and will be treated as confidential by the receiving party.
Description and findings re EC3	The MOUs agreed with both domestic and foreign regulators provide for confidential information passed by the BSP to be treated as confidential by the receiving party.
EC4	The supervisor receiving confidential information from other supervisors uses the confidential information for bank-specific or system-wide supervisory purposes only. The supervisor does not disclose confidential information received to third parties without the permission of the supervisor providing the information and is able to deny any demand (other than a court order or mandate from a legislative body) for confidential information in its possession. In the event that the supervisor is legally compelled to disclose confidential information it has received from another supervisor, the supervisor promptly notifies the originating supervisor, indicating what information it is compelled to release and the circumstances surrounding the release. Where consent to passing on confidential information is not given, the supervisor uses all reasonable means to resist such a demand or protect the confidentiality of the information.
Description and findings re EC4	The MOUs agreed with both domestic and foreign regulators provide for confidential information passed to the BSP to be used only for supervisory purposes and not to be disclosed to third parties without consent. The BSP has not been asked to disclose confidential information provided to it by another regulatory body.
EC5	Processes are in place for the supervisor to support resolution authorities (e.g. central banks and finance ministries as appropriate) to undertake recovery and resolution planning and actions.
Description and findings re EC5	The BSP has a MOA in place with the PDIC which sets out the coordination and cooperation arrangements between the two bodies. There is no formal process in place to effect an orderly resolution of a bank in the Philippines, although there is evidence of

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	effective bilateral coordination on a troubled bank with the PDIC, which is the principal Resolution Authority in the Philippines. The BSP is not party to the Crisis Management Groups (CMG) established by foreign banks with significant branches in the Philippines, three of which are D-SIBs, on the grounds that the Philippine operations are not material in terms of the overall size of those foreign banking groups. The BSP is not, therefore, party to any discussions on the recovery and resolution plans for those banking groups. The financial stability risk to the Philippine banking sector arising from the failure of one of the foreign D-SIBs is mitigated, in part, by the BSP's requirement for the branches to hold local capital and for the branches to comply with all local prudential regulatory requirements.
Assessment of Principle 3	Compliant
Comments	Existing regulations and practical arrangements between the BSP and domestic and foreign regulators provide an effective framework for cooperation and collaboration. The MOAs signed between the respective regulators adequately reflect the need to protect confidential information. Recommendations: • Negotiate a MOA with the SSM to replace the existing MOA with BaFin. • Negotiate a formal MOA between the BSP and CDA. • Establish formal college of supervisor arrangements for sharing information between domestic supervisory bodies.
Principle 4	**Permissible activities**. The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined and the use of the word "bank" in names is controlled**.**
Essential criteria	
EC1	The term "bank" is clearly defined in laws or regulations.
Description and findings re EC1	The term "bank" is defined in S.3.1 of the GBL or the RA No. 8791 as "entities engaged in the lending of funds obtained in the form of deposits." S. 3.2 of the GBL classifies banks into: "(a) Universal banks; (b) Commercial banks; (c) Thrift banks, composed of: (i) Savings and mortgage banks, (ii) Stock savings and loan associations, and (iii) Private development banks, as defined in RA No. 7906 (hereafter the "Thrift Banks Act"); (d) Rural banks, as defined in RA No. 7353 (hereafter the "Rural Banks Act"); (e) Cooperative banks, as defined in RA No. 6938 (hereafter the "Cooperative Code"); (f) Islamic banks as defined in RA No. 6848, otherwise known as the "Charter of Al Amanah Islamic Investment Bank of the Philippines"; and, (g) Other classifications of banks as determined by the MB of the BSP." The definition of the term "quasi-bank" (QB) is set forth in the GBL as "… entities engaged in the borrowing of funds through the issuance, endorsement or assignment with recourse or acceptance of deposit substitutes for purposes of relending or purchasing of receivables and other obligations. ("deposit substitutes" are defined in S. 95 of the NCBA as non-deposit instruments such as bankers' acceptances, promissory notes and repurchase

<table>
<tr><th colspan="2">Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)</th></tr>
<tr><td></td><td>agreements). The BSP does not charter QBs as independent entities; rather banks are permitted to engage in quasi-banking activities.</td></tr>
<tr><td>EC2</td><td>The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined either by supervisors, or in laws or regulations.</td></tr>
<tr><td>Description and findings re EC2</td><td>GBL Annotated (Book II) provides that the two basic functions of banks are: (i) acceptance of deposits from the public; and (ii) lending of funds obtained from deposits. The permissible activities of each category of banks are set out in various sections of the GBL (Articles I and II of Chapter IV and S. 53) and other special banking laws, such as the Thrift Banks Act, Rural Banks Act, Cooperative Code and Charter of Al-Amanah Islamic Investment Bank of the Philippines.

The permissible activities and powers of universal banks, commercial banks, thrift banks, rural banks and cooperative banks are further elaborated in S. 101 of the Manual of Regulation for Banks (MORB) (Classifications, Powers and Scope of Authorities of Banks).

The scope of quasi-banking activities is defined in the MORB (at S. 241-246).

Regarding the authority to engage in securities, insurance, real estate and non-financial activities:
Only universal banks are allowed to directly (or indirectly through its subsidiary) engage in securities underwriting, brokering and dealing (S. 101 of the MORB);
With prior BSP approval, banks may invest in equities of financial allied undertakings, which include companies engaged in stock brokerage/securities dealership (S. 372 of the MORB), subject to the limits prescribed under S. 373 of the MORB;
Only universal banks are allowed to cross-sell its group financial products, which include insurance products (S. 113 of the MORB); but are not permitted to directly underwrite insurance;
Only universal banks may indirectly engage in insurance underwriting and selling through its subsidiary (S. 372 of the MORB);
If the real estate is a non-financial allied undertaking (i.e., companies engaged in home building and home development): a bank (directly or through a subsidiary) may acquire up to 100% of the equity of a non-financial allied undertaking, except for thrift/rural bank which shall be limited to less than 50% of the voting shares in that enterprise. Prior MB approval is required if the investment is in excess of 40% of the total voting stock of such allied undertaking (S. 375 of the MORB);
If the real estate is a non-allied undertaking (i.e., industrial park projects/industrial estate developments, financial and commercial complex projects arising from or in connection with the government's privatization program): only universal banks (directly or through a subsidiary) may invest in the equity of an enterprise engaged in non-allied or non-related activities, subject to limits (S. 376-A of the MORB); and,
A bank (directly or through a subsidiary) may acquire up to 100% of the equity of a non-financial allied undertaking, except for thrift/rural bank which shall be limited to less than 50% of the voting shares in that enterprise. Prior MB approval is required if the investment is in excess of 40% of the total voting stock of such allied undertaking (S. 375 of the MORB).</td></tr>
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Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	It should be noted that the BSP does not supervise non-bank parent companies of banks nor of allied affiliates; and does not, therefore, define or restrict the permissible activities of a wider group or conglomerate that owns or incorporates a licensed bank.
EC3	The use of the word "bank" and any derivations such as "banking" in a name, including domain names, is limited to licensed and supervised institutions in all circumstances where the general public might otherwise be misled.
Description and findings re EC3	S. 6 of the GBL provides that no person or entity shall engage in banking operations or quasi-banking functions without authority from the BSP. S. 64 of the GBL provides: "No person, association, or corporation unless duly authorized to engage in the business of a bank, quasi-bank, trust entity, or savings and loan association as defined in this Act, or other banking laws, shall advertise or hold itself out as being engaged in the business of such bank, quasi-bank, trust entity, or association, or use in connection with its business title, the word or words "bank", "banking", "banker", "quasi-bank", "quasi-banking", "quasi-banker", "savings and loan association", "trust corporation", "trust company" or words of similar import or transact in any manner the business of any such bank, corporation or association." S. 102 of the MORB provides guidelines on business name as follows: a) Universal banks/commercial banks: Only a bank that is granted universal/commercial banking authority may represent itself to the public as such in connection with its business name; b) Thrift banks: Allowed to adopt and use any name: Provided, that the words A Thrift Bank, A Savings Bank, A Private Development Bank or A Stock Savings and Loan Association, as the case may be, are affixed after its business name; c) Rural banks/cooperative banks: May adopt a corporate name or use a business name/style with the word Rural or Coop, as the case may be. Said banks may also adopt a name without such words: Provided, that the identifying phrase, A Cooperative Bank or A Rural Bank, as the case may be, is affixed after its business name: Provided, further, that where the name of the bank is shown on letterheads, billboards and other advertising materials, the size of the letters of such phrase shall be at least one-half (½) the size of the business name; A thrift bank, rural bank, or cooperative bank may apply to be exempted from the general requirements, subject to prior approval of the BSP and that the applicant shows compliance with the following conditions: • The new business name of the bank must reasonably describe the business activities that the bank is engaged in. • The business name should not mislead, misrepresent or give a false impression to the public with respect to the banking category of a bank, the location/s and clientele it serves, as well as the products and services that the applicant bank is authorized to offer to the public;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	• The applicant bank shall not use a business name that is identical, deceptive or confusingly similar with existing corporate names, in accordance with existing applicable laws, rules and regulations governing the use of corporate names pursuant to the provisions of the Corporation Code of the Philippines.; • The applicant bank must meet the minimum capitalization requirements applicable at the time of filing of its application to change its business name; • The applicant bank must not have any major supervisory concern/s that threaten its solvency or liquidity, as determined by the appropriate department/s of the FSS; and, • Other conditions which the BSP may deem necessary or as may be warranted by the attendant circumstances in order to protect the public interest. S. 102 of the MORB further provides the rules and regulations governing bank advertisements as follows: • No bank shall publish, issue or distribute in any form, any advertisement that shall degrade, deprecate or otherwise prejudice other banking and financial institutions; • No bank shall publish, issue or distribute in any form of advertisement (in newspapers, magazines, television, radio, billboards, brochures, prospectuses, or any other medium) or allow itself to be used/mentioned in any form of advertisement unless such advertisement is in pursuance of its business or investment; • No bank shall place or cause to be placed any advertisement tending to mislead a depositor into believing that he will get more in benefits than what the bank is legally authorized to give. No bank advertisement shall contain any false claim or exaggerated representation as to its liquidity, solvency, resources, deposits and banking services; • No bank advertisement shall give the impression that the bank is engaged in a business other than banking; • Banks shall inform their depositors and other clients by advertisement or publication of the termination of benefits previously advertised or publicized; • Banks shall discontinue any advertisement whenever the same is deemed unethical/unwarranted or violative of the provisions of these regulations. The client banks and/or their advertising agencies shall incorporate in their contract/agreement for time and space with media the condition that such contract/agreement for time and space can be cancelled/terminated immediately whenever the client bank is directed by the BSP to desist or discontinue the particular advertisement in question and, • Responsibility for compliance with the above rules and regulations rests with the bank officers or directors who caused the approval or placement of such advertisement.
EC4	The taking of deposits from the public is reserved for institutions that are licensed and subject to supervision as banks.[/10]

[/10] The Committee recognizes the presence in some countries of non-banking financial institutions that take deposits but may be regulated differently from banks. These institutions should be subject to a form of regulation commensurate to the type and size of their business and, collectively, should not hold a significant proportion of deposits in the financial system.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	The term "bank" is defined in S. 3.1 of the GBL as "entities engaged in the lending of funds obtained in the form of deposits." GBL Annotated (Book II) sets forth two basic functions of banks as: (i) acceptance of deposits from the public; and (ii) lending of funds obtained from deposits. GBL Annotated Book II defines deposit as funds placed with a bank in a savings account, or in demand account subject to withdrawal by check. It signifies the act of placing cash, checks, or drafts in the custody of a bank, to be withdrawn at the will of the depositor. S. 29 of the GBL provides the powers of a commercial bank, which include the acceptance or creation of demand deposits, as well as the receipt of other types of deposits and deposit substitutes. Further, S. 33 of the GBL provides that a bank other than a universal bank or commercial bank cannot accept or create demand deposits except upon prior approval of, and subject to such conditions and rules as may be prescribed by the MB. S. 201 (Authority to Accept or Create Demand Deposits) of the MORB provides that banks may accept or create demand deposits subject to withdrawal by check. A universal bank or commercial bank may accept or create demand deposits subject to withdrawal by check, without prior authority from the BSP. A thrift bank, rural bank or cooperative bank may accept or create demand deposits upon prior authority of the BSP. The authority to accept or create deposits is provided under S. 101 of the MORB (The Classifications, Powers and Scope of Authorities of Banks) as among the special powers that can be performed by banks. In addition to universal and commercial banks, the other institutions that are authorized to accept deposits are: • Non-stock savings and loan associations (NSSLAs). NSSLAs may accept deposits only from its members and shall not transact business with the general public (RA 8367). NSSLAs are regulated by the BSP (Manual of Regulations for Non-Bank Financial Institutions, N Regulations). • Cooperatives. A cooperative bank may accept deposits only from its members. Cooperatives are under the regulation and supervision of the Cooperative Development Authority (RA 9520).
EC5	The supervisor or licensing authority publishes or otherwise makes available a current list of licensed banks, including branches of foreign banks, operating within its jurisdiction in a way that is easily accessible to the public.
Description and findings re EC5	A list of licensed banks and branches of foreign banks operating within BSP's jurisdiction is published at the BSP website. The listing contains the name and contact information, including the website, if available, of each supervised institution. The list is updated whenever there are changes in the status, such as change of name, a merger or acquisition, or a closure, through Circular Letters which are available on the BSP website. In addition, the list of BSP-supervised financial institutions with approved special authorities (such as additional derivatives, trust authority, e-money issuers) are posted on the BSP website.
Assessment of Principle 4	Compliant

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	BSP laws and regulations clearly establish the permissible activities of supervised banks, and naming conventions are controlled. Taking of deposits is restricted to identified BSP authorized institutions. A list of licensed banks is publicly available.
Principle 5	**Licensing criteria.** The licensing authority has the power to set criteria and reject applications for establishments that do not meet the criteria. At a minimum, the licensing process consists of an assessment of the ownership structure and governance (including the fitness and propriety of Board members and senior management) [/11] of the bank and its wider group, and its strategic and operating plan, internal controls, risk management and projected financial condition-(including capital base). Where the proposed owner or parent organization is a foreign bank, the prior consent of its home supervisor is obtained.
Essential criteria	
EC1	The law identifies the authority responsible for granting and withdrawing a banking license. The licensing authority could be the banking supervisor or another competent authority. If the licensing authority and the supervisor are not the same, the supervisor has the right to have its views on each application considered, and its concerns addressed. In addition, the licensing authority provides the supervisor with any information that may be material to the supervision of the licensed bank. The supervisor imposes prudential conditions or limitations on the newly licensed bank, where appropriate.
Description and findings re EC1	S. 6 of the RA No. 8791 or the GBL provides BSP the authority to grant or withdraw banking licenses. It provides: "No person or entity shall engage in banking operations or quasi-banking functions without authority from the BSP: Provided, however, that an entity authorized by the BSP to perform universal or commercial banking functions shall likewise have the authority to engage in quasi-banking functions. The determination of whether a person or entity is performing banking or quasi-banking functions without BSP authority shall be decided by the MB. To resolve such issue, the MB may, through the appropriate supervising and examining department of the BSP, examine, inspect or investigate the books and records of such person or entity. Upon issuance of this authority, such person or entity may commence to engage in banking operations or quasi-banking functions and shall continue to do so unless such authority is sooner surrendered, revoked, suspended or annulled by the BSP in accordance with this Act or other special laws. No person or entity shall engage in banking operations or quasi-banking functions without authority from the BSP."

[/11] This document refers to a governance structure composed of a board and senior management. The Committee recognizes that there are significant differences in the legislative and regulatory frameworks across countries regarding these functions. Some countries use a two-tier board structure, where the supervisory function of the board is performed by a separate entity known as a supervisory board, which has no executive functions. Other countries, in contrast, use a one-tier board structure in which the board has a broader role. Owing to these differences, this document does not advocate a specific board structure. Consequently, in this document, the terms "board" and "senior management" are only used as a way to refer to the oversight function and the management function in general and should be interpreted throughout the document in accordance with the applicable law within each jurisdiction.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	The SEC shall register the articles of incorporation and by-laws of any bank or any amendments thereto upon the issuance by the BSP of the Certificate of Authority to Register. The local government entities concerned also issue business permits before a bank can commence its operations. After completing all the requirements, the Certificate of Authority to Operate is issued to the bank to commence its banking operations. Circular No. 902 provides that the authority to establish a bank shall be automatically revoked if the bank is not organized and opened for business within one year after receipt by the organizers of the notice of approval by the MB of their application but does not provide any additional grounds for revocation. S. 30 of the NCBA provides that the MB may summarily and without need for prior hearing forbid the institution from doing business in the Philippines and appoint the PDIC as receiver, if upon report of the head of the supervising and examining department, the MB finds that a bank or quasi-bank: a. is unable to pay its liabilities as they become due in the ordinary course of business; b. has insufficient realizable assets, as determined by the BSP, to meet its liabilities; or c. cannot continue in business without involving probable losses to its depositors or creditors; or d. has willfully violated a cease and desist order under S. 37 that has become final, involving acts or transactions which amount to fraud or a dissipation of the assets of the institution BSP also retains authority to license certain activities of existing banks; BSP has issued regulations granting the authority to revoke such licenses. Circular No. 947 sets forth the expectations and criteria of the BSP with respect to granting of licenses and authorities of BSP supervised institutions. The Circular further states that the BSP reserves the right to withdraw or revoke the license and/or authority or enforce appropriate actions when an institution no longer meets the criteria or standards required to be met for the exercise of the license and/or authority. The ability of local governments to revoke permissions or licenses of banks operating under their jurisdiction could present potential legal complications or uncertainties. Under the Local Government Code, local government units can impose taxes and fees on businesses which include banks and financial institutions, the non-payment of which may result to the non-granting of business permits to the banks and financial institutions. The continuous operation of banks without such permits would then make the business illegal despite the presence of a bank license, S. 28-A of the amendments to the NCBA seeks to mitigate this concern by providing that the “suspension or revocation of any government license necessary for the operation of a regulated bank must be done only with prior consultation with the BSP.”

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	This amendment does not set a time frame for providing 'prior notice' and the amendment does not require prior approval of the BSP, leaving local government empowered to negatively impact the legal operations of licensed banks, even if they consult with BSP. Such a situation could lead to unfavorable consequences, considering the uncertainty in the legal standing or operations of such entity. In practice, these concerns have not arisen, given that coordination mechanisms have been established with local governments.
EC2	Laws or regulations give the licensing authority the power to set criteria for licensing banks. If the criteria are not fulfilled or if the information provided is inadequate, the licensing authority has the power to reject an application. If the licensing authority or supervisor determines that the license was based on false information, the license can be revoked.
Description and findings re EC2	S. 8 of the GBL provides that the MB may authorize the organization of a bank or QB subject to relevant conditions (See EC 3). BSP has the power to reject an application if the information provided is inadequate. There is no explicit provision in the GBL or implementing regulations that authorizes the revocation of a banking license in the event an application is determined to be based upon false information. It is reasonable to infer that such authority exists under the BSP's general grant of authority; although an explicit regulatory expression would provide greater clarity and enforceability.
EC3	The criteria for issuing licenses are consistent with those applied in ongoing supervision.
Description and findings re EC3	S. 8 of the GBL provides that the MB may authorize the organization of a bank or quasi-bank subject to the conditions, among others that the minimum capital requirements prescribed by the MB for each category of banks are satisfied. Under the GBL, the MB shall take into consideration their capability in terms of their financial resources and technical expertise and integrity. The GBL requires that the bank licensing process "...shall incorporate an assessment of the bank's ownership structure, directors and senior management, its operating plan and internal controls as well as its projected financial condition and capital base." Circular No. 902 provides that new domestic banks should have suitable/fit shareholders, adequate financial strength, a legal structure in line with its operational structure, a management with sufficient expertise and integrity to operate the bank in a sound and prudent manner. S. 2 of "An Act Allowing the Full Entry of Foreign Banks in The Philippines" provides standards related to the approval of entry applications of foreign banks. In particular, the MB shall: (i) ensure geographic representation and complementation; (ii) consider strategic trade and investment relationships between the Philippines and the country of incorporation of the foreign bank; (iii) study the demonstrated capacity, global reputation for financial innovations and stability in a competitive environment of the applicant; (iv) see to it that reciprocity rights are enjoyed by Philippine banks in the applicant's country; and (v) consider willingness to fully share their technology. It further provides that only established, reputable and financially sound foreign banks shall be allowed entry and such foreign bank applicant must be widely owned and publicly-listed in its country of origin, unless it is owned and controlled by the government of its country of origin.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	Circular No. 858 provides the guidelines and criteria in approving the establishment of new foreign banks as well as the application documents required to be submitted to the BSP. Circular No. 947 provides the prudential criteria in determining the eligibility of applicants to be granted certain licenses and/or authorities to conduct specific activities. Among the minimum conditions is that the applicant bank should have no major supervisory concerns in governance, risk management systems, and internal controls and compliance system and have complied with the directives and/or not subject of specific directives and/or enforcement actions by the BSP. Each of these Circulars set forth distinct criteria. For example, Circular No. 902 requires new bank applicants to demonstrate "suitable/fit shareholders, adequate financial strength, a legal structure in line with its operational structure, a management with sufficient expertise and integrity to operate the bank in a sound and prudent manner." Under Circular No. 902, an applicant must submit evidence of financial capacity of incorporates and subscribers, a corporate plan and feasibility study with projections. Circular No. 858 relating to foreign entry applications focuses on geographic representation, global reputation, and 'financially sound' applicant. Circular No. 947 is centered on effective corporate governance, risk management and internal controls. While these criteria are consistent with standards applied during ongoing supervision, they are not co-extensive and could be rationalized to seek consistency across the licensing criteria. Common criteria should ensure that foreign or domestic applicants for new banks demonstrate adequate corporate governance, risk management, and internal controls, as is required for applicants that are existing banks seeking additional authorities, thus ensuring greater consistency with standards related to ongoing supervision.
EC4	The licensing authority determines that the proposed legal, managerial, operational and ownership structures of the bank and its wider group will not hinder effective supervision on both a solo and a consolidated basis. [/12] The licensing authority also determines, where appropriate, that these structures will not hinder effective implementation of corrective measures in the future.
Description and findings re EC4	BSP licensing regulations and standards require information regarding legal, managerial, operational and ownership structures of applicants, and obtains information regarding the 'wider group.' With respect to the licensing of new banks, the ownership structure is assessed through the documents submitted by the applicant bank which include the conglomerate map/structure where the corporate subscriber belongs, the corporate subscriber's list of stockholders including the ultimate beneficial owners. Moreover, foreign bank applicants are required, as part of the application package, to describe its ownership and control structure in adequate detail, including whether it is a part of a financial or commercial conglomerate, and disclose related parties, if any, that are operating in the Philippines.
EC5	The licensing authority identifies and determines the suitability of the bank's major shareholders, including the ultimate beneficial owners, and others that may exert significant influence. It also assesses the transparency of the ownership structure, the sources of initial capital and the ability of shareholders to provide additional financial support, where needed.

[/12] Therefore, shell banks shall not be licensed (reference document: BCBS paper on shell banks, January 2003).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	S. 8 of the GBL states that in the exercise of the authority granted herein, the MB shall take into consideration the capability of the organization of the bank in terms of their financial resources and technical expertise and integrity. The bank licensing process shall incorporate an assessment of the bank's ownership structure, directors and senior management, its operating plan and internal controls as well as its projected financial condition and capital base. S. 102 of the MORB, which provides for the Basic Guidelines in Establishing Domestic Banks, states that a new banking organization must have suitable/fit shareholders, adequate financial strength, a legal structure in line with the operational structure, a management with sufficient expertise and integrity to operate the bank in a sound and prudent manner. Further, Appendix 33 of the MORB provides the guidelines in the evaluation of incorporators, subscribers, directors and officers, as follows: (1) The incorporators, subscribers and proposed directors and officers must be persons of integrity and of good credit standing in the business community. The subscribers must have adequate financial strength to pay for their proposed subscriptions in the bank; (2) The incorporators, subscribers and proposed directors and officers must not have been convicted of any crime involving moral turpitude, and unless otherwise allowed under the provisions of existing laws are not officers or employees of a government agency, instrumentality, department or office charged with the supervision of, or the granting of loans to banks; (3) A bank may be organized with not less than five (5) nor more than fifteen (15) incorporators; (4) The number and nationality of the members of the Board of directors of the bank shall be subject to the limits prescribed under S. 132 of the MORB; (5) No appointive or elective public official, whether full-time or part-time shall at the same time serve as officer of a bank except in cases where such service is incident to financial assistance provided by the government or a government-owned or –controlled corporation to the bank or in cases allowed under existing laws; (6) The proposed directors and officers of the bank shall be subject to qualifications and other requirements under S. 132 and 137 of the MORB; and (7) The disqualifications of directors and officers prescribed under S. 138 of the MORB shall also apply. In addition, S. 122 (d) of the MORB provides that newly established banks shall, before being allowed to operate, submit the following: 1. An alphabetical list of stockholders with the number and percentage of voting shares of stock owned by them; 2. A separate list containing the names of stockholders who own voting shares of stock in the bank and who are related to each other within the fourth degree of consanguinity or affinity, whether legitimate, illegitimate or common-law (in the case of individuals) as well as corporations which are wholly-owned or a majority of the stock of which is owned by any of such stockholders, including their subsidiaries; and 3. An affidavit under oath from each of the stockholders attesting, among other things, that he/she/it is the bona fide owner of the voting shares of stock of the bank in

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	his/her/its own right, and not as an agent, assignee, proxy, nominee or a dummy of any other person, natural or juridical. The applicant for a new bank must also submit evidence of financial capacity of each individual Filipino/non-Filipino incorporators/subscribers. While Appendix 33 of the MORB requires the submission of a list of shareholders, including ultimate beneficial owners, the suitability information required of incorporators and subscribers does not extend to same. This omission would be material were a new bank to be established by a conglomerate group, although no such applications have been received in recent experience. There is lack of clarity regarding the standard to be met in order to demonstrate adequate 'financial strength' of incorporators and subscribers. Appendix 33 requires generally that incorporators and subscribers submit 'evidence of financial capacity,' and, at a later point, requires that 'subscribers must have adequate financial strength to pay for their proposed subscriptions in the bank.' This could be interpreted to limit the review of financial strength to support the initial capital subscription and omit a requirement that incorporators or subscribers demonstrate financial capacity to provide additional support to the bank, if needed, beyond their initial subscription. This additional capacity is especially material in relation to the license of rural banks, which are generally small, family-run operations which, as a group, have demonstrated financial fragility, with many having suffered capital deficiencies and an inability to restore the institution to minimum required capital levels, resulting in multiple closures.
EC6	A minimum initial capital amount is stipulated for all banks.
Description and findings re EC6	S. 8 of the GBL provides that the MB may authorize the organization of a bank provided that the minimum capital requirements prescribed by the MB for each category of banks are satisfied. Circular No. 854 provides the new minimum capitalization of banks. The minimum capitalization shall be required upon: (a) establishment of a new bank; (b) conversion of an existing bank from a lower to a higher category bank and vice versa; and (c) relocation of the head office of a thrift or rural bank in an area of higher classification. The minimum capitalization of universal and commercial banks increases as the branch network increases. In the case of thrift, rural and cooperative banks, the minimum capitalization is not only dependent on the branch network but also on the location of the bank's principal/head office. Appendix 107 of the MORB provides that banks to be established must comply with the minimum capitalization of banks prescribed under S. 121 of the MORB. Further, the paid-up capital shall be no less than the minimum required capital. S. 103 of the MORB states that a foreign bank subsidiary/branch shall comply with the minimum capital and prudential capital ratios applicable to domestic banks of the same category.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	Under Circular 854, minimum initial capital requirements vary depending upon the type of bank and the number of branches. For Universal Banks and Commercial Banks, the minimum capitalization (no branches; head office only) is Php 3 Billion (approx. US$ 57.8 million) and Php 2 Billion (approx. US$ 38.5 million) respectively.
EC7	The licensing authority, at authorization, evaluates the bank's proposed Board members and senior management as to expertise and integrity (fit and proper test), and any potential for conflicts of interest. The fit and proper criteria include: (i) skills and experience in relevant financial operations commensurate with the intended activities of the bank; and (ii) no record of criminal activities or adverse regulatory judgments that make a person unfit to uphold important positions in a bank.[/13] The licensing authority determines whether the bank's Board has collective sound knowledge of the material activities the bank intends to pursue, and the associated risks.
Description and findings re EC7	S. 8 of the GBL provides that the bank licensing process shall incorporate an assessment of a bank's directors and senior management. S. 102, Appendix 33 of the MORB provides the guidelines in the evaluation of incorporators, subscribers, directors and officers. S. 132 of the MORB sets out minimum qualifications for directors, including 'fit and proper' requirements and requires submission of documentary proof and certification to support BSP's review and approval. The role and duties of the board of directors is elaborated in S. 132 of the MORB and the board's governance and conduct are evaluated during the regular examination cycle. See also EC5. BSP reviews and evaluates proposed Board members and senior management in accordance with these guidelines. After approval of the new bank, members of the Board are required to attend a seminar on corporate governance, which should be in accordance with the BSP-prescribed syllabus on corporate governance for first time directors. This requirement was adopted for Board members to be equipped with adequate knowledge on good governance and management of the bank.
EC8	The licensing authority reviews the proposed strategic and operating plans of the bank. This includes determining that an appropriate system of corporate governance, risk management and internal controls, including those related to the detection and prevention of criminal activities, as well as the oversight of proposed outsourced functions, will be in place. The operational structure is required to reflect the scope and degree of sophistication of the proposed activities of the bank.[/14]
Description and findings re EC8	S. 8 of the GBL provides that the bank licensing process shall incorporate an assessment of the bank's ownership structure, directors and senior management, its operating plan and internal controls as well as its projected financial condition and capital base.

[/13] Please refer to Principle 14, Essential Criterion 8.

[/14] Please refer to Principle 29.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC8	Appendices 2 and 33 of the MORB require, among others, the submission of corporate plan and feasibility study. The corporate plan shall describe in meaningful details the business model and strategies of the bank. Moreover, the bank shall submit the chart of organization and its list of principal officers, compliance with minimum security measures as well as an undertaking that the manual of operations embodying the policies and operating procedures covering all risk areas of the proposed bank have been prepared. BSP has issued Circulars that set forth standards addressing corporate governance expectations (including risk management and internal controls) (Circular No. 947), as well as standards on the management of contracts and outsourcing of banking functions (Circular No. 899). However, these standards are not directly tied to the application process and do not mandate reviews of compliance with such standards prior to approval of the license—to ensure that appropriate systems and controls 'will be in place.' Similarly, while Anti-Money Laundering (AML) standards have been issued, appropriate elements have not been incorporated into the new bank licensing process to ensure that the applicant will have effective governance and controls related to the detection and prevention of criminal activities 'in place.'
EC9	The licensing authority reviews pro forma financial statements and projections of the proposed bank. This includes an assessment of the adequacy of the financial strength to support the proposed strategic plan as well as financial information on the principal shareholders of the bank.
Description and findings re EC9	S. 8 of the GBL provides that the bank licensing process shall incorporate an assessment of the bank's ownership structure, directors and senior management, its operating plan and internal controls as well as its projected financial condition and capital base. Appendices 2 and 33 of the MORB require applications for foreign operations and new domestic bank applicants respectively, to submit among other items, the corporate plan and projected financial statements. Moreover, the applicant for a new bank must also submit evidence of financial capacity of each individual Filipino/non-Filipino incorporators/subscribers. The strategic plan and projected financial statements of the applicant bank are reviewed by management of the BSP's FSS. Staff analysis is incorporated in a memorandum submitted to the MB for approval. The applicant bank is expected to present its business model, corporate strategies and financial projections including the underlying assumptions. It should also demonstrate that it is financially sound and capable of conducting business in the Philippines in a safe and sound manner.
EC10	In the case of foreign banks establishing a branch or subsidiary, before issuing a license, the host supervisor establishes that no objection (or a statement of no objection) from the home supervisor has been received. For cross-border banking operations in its country, the host supervisor determines whether the home supervisor practices global consolidated supervision.
Description and findings re EC10	Circular No. 858, Appendix 2 of the MORB requires the submission of a Certification from the foreign bank applicant's home country supervisory authority that: 1. It has no objection to the foreign bank's investment;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC10	2. It will provide the BSP with relevant supervisory information, including derogatory information, related to the applicant bank, to the extent allowed under existing laws; 3. The foreign bank applicant is compliant with the capital requirements as prescribed by the laws and regulations of its country of origin; and 4. Philippine banks may establish subsidiaries and/or branches in the foreign bank applicant's home country, subject to compliance with the host country's rules and regulations governing admission generally applicable to all foreign banks. During the evaluation of a foreign bank's application, it is also determined whether the counterpart supervisory authority in the home country has an existing cross-border MOU with the BSP. At present, BSP does not have in place a cross-border MOU with the United States, nor with the European Central Bank. See discussion in BCP 3. The Circular does not set forth an explicit requirement that BSP review and determine that the home supervisor 'practices global consolidated supervision.' It does not appear that BSP has in place a defined framework to assess the adequacy of a home supervisor's approach to consolidated supervision or its adequacy, although there was evidence of such checks in file reviews.
EC11	The licensing authority or supervisor has policies and processes to monitor the progress of new entrants in meeting their business and strategic goals, and to determine that supervisory requirements outlined in the license approval are being met.
Description and findings re EC11	Once the chartering process is already completed, the new bank is endorsed to the appropriate Financial Supervision Department (FSD) for continuing supervision. The new entrant's compliance with the supervisory requirements/conditions for the approval of its license is handed off to the assigned FSD. There are no separate guidelines or procedures mandating an on-site review at initiation of operations or more frequent review of newly licensed banks and such institutions may only be examined at the regularly scheduled examination. Such examinations have been mandated to occur at least annually, but amendments to the BSP charter now allow greater flexibility in scheduling/conducting examinations whereby, for example, small or rural banks may be examined less frequently (e.g., once every three years). With the movement towards less frequent regular examinations, BSP should establish and formalize a clear policy regarding the monitoring or examination of newly licensed institutions to ensure that adequately frequent contact is achieved to effectively monitor progress of new entrants.
Assessment of Principle 5	Largely Compliant
Comments	BSP possesses adequate authority to set criteria and reject applications for banking licenses. The licensing process involves assessments of ownership structure and governance of the banking group. Prior consent of foreign authorities is obtained in order to license entry of a foreign banking organization. Licensing regulations and standards do not clearly identify grounds for revocation (especially when based upon false information), do not mandate a review of the suitability of ultimate beneficial owners, and apply standards that are not consistently employing standards related to ongoing supervision, especially governance, internal controls and risk management standards, ensuring such are

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	'in place' upon entry into the banking system. A system to ensure prompt monitoring of new entrants is lacking. Recommendations: • Clarify in regulations or supervisory guidance the grounds supporting revocation (beyond the grounds supporting appointment of PDIC as receiver), including the ability to revoke when applications are determined to be submitted based upon false information. • Amend licensing criteria to ensure a review of the suitability of ultimate beneficial owners, where applicable, and specify that there must be a demonstration of financial strength of incorporators or subscribers adequate to provide additional financial support beyond the initial subscription level. • Amend licensing criteria to set objective criteria for licensing of new banks, foreign banks, and to grant licenses for additional authorities to apply standards consistent with ongoing supervision equally across applicants, including, importantly, ensuring that applicants have adequate and consistent governance, internal controls and risk management systems 'in place' upon commencing operations. • Clarify licensing guidelines or procedures to mandate more frequent review of newly licensed banks upon entry into the banking system. • Ensure that ongoing supervision incorporates a review of relevant banks' compliance with applicable local tax, licensing or other supervisory requirements. • Continue close coordination with local government units to coordinate regarding licensing and permitting processes.
Principle 6	**Transfer of significant ownership.** The supervisor[15] has the power to review, reject and impose prudential conditions on any proposals to transfer significant ownership or controlling interests held directly or indirectly in existing banks to other parties.
Essential criteria	
EC1	Laws or regulations contain clear definitions of "significant ownership" and "controlling interest."
Description and findings re EC1	S. 122 of the MORB provides the only definition pertaining to change of control of a financial institution and is subject to limitations. (While BSP refers to various sections of the MORB that provide definitions of 'control' (MORB S. 131, 362, and 371), these are not incorporated into S. 122 of the MORB). S. 122 speaks only in terms of transfer of 'ownership or control of the voting shares of a bank.' Importantly, the language of the NCBA amendments (S. 25-A) restricts BSP prior approval only to the transfer of 'voting shares.' Given the conglomerate ownership of multiple significant D-SIBs in the Philippines, where bank ownership chains cascade up through intermediate corporate structures to ultimate beneficial owners, the apparent restriction in S. 25-A to the transfer of voting shares, the lack of a clear definition of beneficial ownership, and the current lack of clarity in the definition of 'control' could restrict BSP's ability to review and approve the transfer of significant controlling interests that are indirectly held by ultimate beneficial owners of the bank or banking group. In the absence of clear authority, BSP's ability to approve transfers and assess the suitability of those persons or entities that maintain ultimate beneficial ownership and control over D-SIBs operating under BSP supervision is impaired.

[15] While the term "supervisor" is used throughout Principle 6, the Committee recognizes that in a few countries these issues might be addressed by a separate licensing authority.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC2	There are requirements to obtain supervisory approval or provide immediate notification of proposed changes that would result in a change in ownership, including beneficial ownership, or the exercise of voting rights over a particular threshold or change in controlling interest.
Description and findings re EC2	The new BSP Charter S. 25-A provides that transfers or acquisitions, or a series thereof, of at least 10 percent of the voting shares in banks or QBs shall require prior approval of the BSP. The selling or conveying stockholder shall submit such transfer or acquisition for approval by the BSP within such period as may be prescribed by the MB. Under the existing regulations (S. 122 MORB), prior approval of the MB shall be required on transaction involving voting shares of stock of a bank, if such transaction, in itself or in relation with other/previous transactions will: (a) Result in ownership or control of more than twenty percent (20 percent) of voting shares of stock of a bank by any person whether natural or juridical or which will enable such person to elect, or be elected as, a director of such bank; or (b) Effect a change in the majority ownership or control of the voting shares of stock of the bank from one (1) group of persons to another group: provided that in no case shall such transaction be approved unless the bank concerned shall immediately comply with the prescribed minimum capital requirement for new banks, notwithstanding any approved capital build-up program. The evaluation of requests for transfers of shares of stock is being handled by the appropriate supervising department of the FSS. BSP has indicated that a review of existing regulations is taking place given the recent changes set forth in the NCBA, reducing the threshold for prior approval from 20 percent to 10 percent of voting shares. As discussed in EC1, the lack of regulatory clarity regarding the definition of control or beneficial ownership and the restriction of BSP approval authority only to the transfer of voting shares could result in transfers of beneficial ownership of banks without BSP prior approval. BSP would be notified of changes to beneficial ownership, through periodic reporting that requires banks to submit a conglomerate 'map', which identifies ultimate beneficial owners during the conduct of on-site examinations. In addition, S. 122 of the MORB mandates that the Corporate Secretary disclose the ultimate beneficial owners of bank shares held in the name of Philippine Central Depository Nominee Corporation (PCDNC) including those of numbered, trust and custodial accounts in an annual (or quarterly whenever changes occur) report on Consolidated List of Stockholders and Their Stockholdings. However, such information would be obtained only after-the-fact and would not provide immediate notification of proposed changes in beneficial ownership.
EC3	The supervisor has the power to reject any proposal for a change in significant ownership, including beneficial ownership, or controlling interest, or prevent the exercise of voting rights in respect of such investments to ensure that any change in significant ownership meets criteria comparable to those used for licensing banks. If the supervisor determines

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	that the change in significant ownership was based on false information, the supervisor has the power to reject, modify or reverse the change in significant ownership.
Description and findings re EC3	As discussed in EC1, the lack of regulatory clarity regarding the definition of control or beneficial ownership and the restriction of BSP approval authority only to the transfer of voting shares would similarly result in an ability to reject proposed transfers of beneficial ownership. Laws and regulations otherwise provide clear authority to approve and reject proposals for proposed changes in voting shares of the bank S. 25-A provides that, "without BSP approval, no such transfer or acquisition (of 10 percent or more of voting shares) shall have legal effect nor shall the same be recognized in the books of the institution or by any government agency, and the transferor-stockholders shall remain accountable and responsible therefor. Transfer of actual control or management of the institution to the new stockholders or their representatives prior to BSP approval shall make the transferor, the transferee and any person responsible therefor liable under S. 36 and 37 of the Act." Similarly, S. 122 of the MORB provides that transactions in voting shares of stock of banks, to the extent of the excess over any of the prescribed ceilings, are "...declared unlawful and void: (1) Any transaction involving voting shares of stock of a bank, if such transaction, in itself, or in relation with other/previous transaction/s shall result in the ownership and control by an individual or corporation of voting shares of stock in excess of any of the prescribed limits of stockholdings in a bank. (2) Any act, contract, agreement or arrangement, such as voting trust agreement or proxy, which vests in any person, whether natural or juridical, the right to vote or the control of the voting shares of stock of a bank, if such arrangement in itself, or in relation with other/previous transaction/s, shall result in the acquisition of the right to vote or the control of voting shares of stock of the bank, in excess of the prescribed ceilings. S. 122 further provides that any request for approval of transactions resulting in significant ownership (above the prescribed limit of voting shares and requiring prior MB approval), "...shall be accompanied by the same papers/documents required of incorporators/stockholders of newly established banks." These include evidence on the integrity, probity, financial capacity, business experience and educational background, among others, of the individual stockholders and of the persons behind the corporate stockholders (see Appendix 33, MORB). BSP regulations place the onus on the Corporate Secretary to ascertain that information submitted to the BSP is accurate and appropriately sworn to by the proposed recipient of such shares, prior to the registration of any transaction. The Corporate Secretary shall be subject to administrative sanctions for violating prescribed obligations, without prejudice to the BSP's filing of appropriate criminal charges as provided under S. 35 of the NCBA for the willful making of misleading statements. BSP regulations do not explicitly set forth a power to reverse or modify its approval in cases when a transfer of ownership was approved based on false information. However, as noted, BSP may pursue enforcement actions on the BSFI, and/or its directors and officers, including its corporate secretary, especially in cases involving the submission of false

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	information to BSP. And, BSP asserts that it has the inherent power to reverse or modify previously approved transfer of ownership based on false information as unlawful and void transactions.
EC4	The supervisor obtains from banks, through periodic reporting or on-site examinations, the names and holdings of all significant shareholders or those that exert controlling influence, including the identities of beneficial owners of shares being held by nominees, custodians and through vehicles that might be used to disguise ownership.
Description and findings re EC4	S. 173 of the MORB requires banks to submit a complete list of stockholders and their stockholdings in a prescribed form annually, as well as quarterly when any change occurs within the reference quarter. S. 122 of the MORB mandates that the corporate secretary disclose the ultimate beneficial owners of bank shares held in the name of PCDNC including those of numbered, trust and custodial accounts in the annual (or quarterly whenever changes occur) report on Consolidated List of Stockholders and Their Stockholdings. The appropriate supervising departments of the FSS have conducted activities to verify banks' compliance with the required disclosure of the beneficial owners of shares held under PCDNC.
EC5	The supervisor has the power to take appropriate action to modify, reverse or otherwise address a change of control that has taken place without the necessary notification to or approval from the supervisor.
Description and findings re EC5	As discussed in EC1, the lack of regulatory clarity regarding the definition of control or beneficial ownership and the restriction of BSP approval authority only to the transfer of voting shares would similarly result in an ability to modify or reverse transfers of beneficial ownership that have taken place with approval from BSP. As noted in EC 3 above, S. 25-A of the NCBA provides that transfers or acquisitions, or a series thereof, of at 10 percent of the voting shares in banks or QBs shall require the prior approval of the BSP; and that "without BSP approval, no such transfer or acquisition shall have legal effect nor shall the same be recognized in the books of the institution or by any government agency, and the transferor-stockholders shall remain accountable and responsible therefor. Transfer of actual control or management of the institution to the new stockholders or their representatives prior to BSP approval shall make the transferor, the transferee and any person responsible therefor liable under S. 36 and 37 of the Act." Similarly, S. 122 of the MORB provides that transactions in voting shares of stock of banks, to the extent of the excess over any of the prescribed ceilings, are "…declared unlawful and void: Also, as noted above, the corporate secretary is mandated to hold in abeyance the registration of the subject transaction until MB approval is obtained, and funds infused by a new subscriber are held in escrow until approval is granted under S. 122 of the MORB. These provisions effectively prevent a transfer of voting shares in excess of the prescribed limits from taking place without MB approval.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	Failure to secure the required MB approval for transfer of shares shall render the parties involved subject to the criminal and administrative sanctions prescribed under S. 35 and 37 of the NCBA, without prejudice to the appropriate legal actions for the rescission and invalidation of the sale or transfer.
EC6	Laws or regulations or the supervisor require banks to notify the supervisor as soon as they become aware of any material information which may negatively affect the suitability of a major shareholder or a party that has a controlling interest.
Description and findings re EC6	BSP laws or regulations, or supervisory requirements, do not explicitly require notification to BSP of material negative information affecting suitability of major shareholders or parties that have controlling interests. While there are requirements to report on the identification of ultimate beneficial owners, the requirements do not include submission of information that may affect the suitability of parties that have controlling interests. As discussed in EC1, the lack of regulatory clarity regarding the definition of control or beneficial ownership and the restriction of BSP approval authority only to the transfer of voting shares would similarly result in an inability to pass upon the suitability of ultimate beneficial owners.
Assessment of principle 6	Materially Non-Compliant
Comments	The recently enacted NCBA in S. 25-A could operate to restrict BSP's authority to pre-approve transfers of ownership to those transactions involving transfers of voting shares. The NCBA grant of BSP prior approval authority does not extend to ownership of significant controlling interests, held indirectly. In addition, existing regulations lack clarity in the definition of 'control' or 'significant controlling interest,' do not set forth a definition of beneficial ownership and are tied to ownership or control of voting shares. And, BSP laws or regulations, or supervisory requirements, do not explicitly require notification to BSP of material negative information affecting suitability of parties that have direct or indirect controlling interests. Given the conglomerate ownership of multiple significant D-SIBs in the Philippines, where bank ownership chains cascade up through intermediate corporate structures to ultimate beneficial owners, the application of S. 25-A, the lack of regulatory clarity regarding the definition of 'control' or 'significant controlling interest' to include ultimate beneficial ownership, or indirect control of voting shares, could impair BSP's ability to review and approve transfers of significant controlling interests and assess suitability of ultimate beneficial owners. Recommendation: • Review and amend the legal and regulatory framework related to transfer of significant controlling interests to include the definition of ultimate beneficial owner or direct and indirect significant controlling interest; • Ensure BSP has the power to review, reject and impose prudential conditions upon the transfer of controlling interest or significant ownership, including beneficial ownership, of a bank held directly or indirectly; • Ensure BSP has the power to review and enforce the suitability of beneficial owners and obtain timely information regarding material changes to their suitability.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Principle 7	**Major acquisitions**. The supervisor has the power to approve or reject (or recommend to the responsible authority the approval or rejection of), and impose prudential conditions on, major acquisitions or investments by a bank, against prescribed criteria, including the establishment of cross-border operations, and to determine that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.
Essential criteria	
EC1	Laws or regulations clearly define: (a) what types and amounts (absolute and/or in relation to a bank's capital) of acquisitions and investments need prior supervisory approval; and (b) cases for which notification after the acquisition or investment is sufficient. Such cases are primarily activities closely related to banking and where the investment is small relative to the bank's capital.
Description and findings re EC1	S 24 of the GBL provides that a universal bank may … "invest in the equities of allied and non-allied enterprises as may be determined by the MB. Allied enterprises may either be financial or non-financial." S. 24 places limits in relation to 'net worth' of the bank (defined as the "total of the unimpaired paid-in capital including paid-in surplus, retained earnings and undivided profit, net of valuation reserves and other adjustments as may be required by the BSP.") The limits established are as follows: "24.1. The total investment in equities of allied and non-allied enterprises shall not exceed fifty percent (50 percent) of the net worth of the bank; and 24.2. The equity investment in any one enterprise, whether allied or non-allied, shall not exceed twenty-five percent (25 percent) of the net worth of the bank." S. 30 of the GBL provides: A commercial bank may … invest only in the equities of allied enterprises as may be determined by the MB. Allied enterprises may either be financial or non-financial. S. 30 places limits on such investments in relation to net worth and provides: 30.1. The total investment in equities of allied enterprises shall not exceed thirty-five percent (35 percent) of the net worth of the bank; and, 30.2. The equity investment in any one enterprise shall not exceed twenty-five percent (25 percent) of the net worth of the bank. The acquisition of such equity or equities is subject to the prior approval of the MB which shall promulgate appropriate guidelines to govern such investments." The following acquisitions and investments by banks need prior supervisory approval: (a) All investments in allied or non-allied undertakings include corporate affiliations or structures as stated in S. 371 of the MORB; (b) All investments in equities of financial allied undertakings as specified in S. 372 of the MORB;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	(c) Equity investments in excess of forty percent (40%) of the total voting stock of a non-financial allied undertaking as defined in S. 375 of the MORB; (d) Equity investments directly or through subsidiaries in non-allied enterprises except for those belonging to categories listed in S. 376-A of the MORB; and, (e) The establishment or acquisition of subsidiaries or affiliates abroad, in accordance with S. 377 of the MORB. Notification after the fact (within 30 banking days after the investment) is sufficient for investments by a universal bank or by its wholly or majority-owned subsidiaries in non-allied activities belonging to those categories enumerated in S. 376-A of the MORB. It also sets limits on investment in a single non-allied enterprise to 35 percent of the total equity or 35 percent of the total voting stock of the enterprise. The definition of financial allied undertakings, non-financial allied undertakings, non-allied undertakings are set forth in S. 372, 375 and 376-A of the MORB as follows: Financial Allied Undertakings (S. 372): (a) Leasing companies including leasing of stalls and spaces in a commercial establishment: Provided, that bank investment in/acquisition of shares of such leasing company shall be limited/ applicable only in cases of conversion of outstanding loan obligations into equity; (b) Banks; (c) Investment Houses; (d) Financing companies; (e) Credit card companies; (f) Banks catering to small and medium scale industries including venture capital corporation, subject to the provisions of S. 374; (g) Companies engaged in stock brokerage/ securities dealership; and, (h) Companies engaged in foreign exchange dealership/brokerage. In addition, universal banks may invest in the following as financial allied undertakings: a) Insurance companies; and b) Holding company: Provided, That the investments of such holding company are confined to the equities of allied undertakings and/or non-allied undertakings of universal banks allowed under BSP regulations. Non-financial Allied Undertakings (S. 375) S. 375 enumerates the non-financial allied undertakings banks may engage in depending the corporation's primary purpose in the articles of incorporation, as follows: a) Universal and commercial banks/thrift banks 1) Warehousing companies; 2) Storage companies; 3) Safe deposit box companies; 4) Companies primarily engaged in the management of mutual funds but not in the mutual funds themselves;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	5) Management corporations engaged or to be engaged in an activity similar to the management of mutual funds; 6) Companies engaged in providing computer services; 7) Insurance agencies/brokerages; 8) Companies engaged in home building and home development; 9) Companies providing drying and/or milling facilities for agricultural crops such as rice and corn; 10) Service bureaus, organized to perform for and in behalf of banks and non-bank financial institutions the services allowed to be outsourced enumerated in S. 112: Provided, that data processing companies may be allowed to invest up to forty percent (40 percent) in the equity of service bureaus; 11) Philippine Clearing House Corporation, Philippine Central Depository, Inc. and Fixed Income Exchange; 12) Companies engaged in merchant acquiring business; and, 13) Such other similar activities as the MB may declare as non- financial allied undertakings of banks. Universal banks may further invest in health maintenance organizations. In addition, thrift banks may also invest in the equities of companies enumerated in Item "b" of this Section. b) Rural banks/cooperative banks 1) Warehousing and other postharvest facilities; 2) Fertilizer and agricultural chemical and pesticides distribution; 3) Farm equipment distribution; 4) Trucking and transportation of agricultural products; 5) Marketing of agricultural products; 6) Leasing; 7) Automated Teller Machine networks; and, 8) Other undertakings as may be determined by the MB.
EC2	Laws or regulations provide criteria by which to judge individual proposals
Description and findings re EC2	S. 50 of the GBL mandates the MB to establish criteria for reviewing major acquisitions or investments by a bank including corporate affiliations or structures that may expose the bank to undue risks or in any way hinder effective supervision. S. 371 of the MORB implements the above Section of the GBL and provides guidelines for major acquisitions or investments by banks including corporate affiliations or structures. The Board of a bank is mandated to consider the criteria outlined in its decision to approve any such investment. The Board must submit a certification that the criteria enumerated has been considered, together with other minimum required documents/information when applying for BSP approval. S. 371 sets forth the criteria to be considered by the Board, as follows: "Criteria for major investments. Any major investment by a bank should be approved by the bank's Board. In acting on such investments, the Board shall consider the following: (1) Such investment must be in accordance with the bank's business plan and management objectives, taking into consideration the economic developments and future prospects. The interests of the different stakeholders of the bank—shareholders, depositors and creditors—should always be considered before any investment is made.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	(2) Such investments will complement/ support the main business of the banks. Extra caution should be taken when investing in activities where the bank has no managerial or technical expertise, or businesses/industries, which are high-risk. (3) Bank management shall provide for an efficient and effective "exit mechanism" or contingency plan in case the investee's operations fail or do not prosper. S. 377 of the MORB lays out the minimum requirements for an application for authority to establish or acquire subsidiaries and affiliates abroad and provides conditions for the approval of such application.
EC3	Consistent with the licensing requirements, among the objective criteria that the supervisor uses is that any new acquisitions and investments do not expose the bank to undue risks or hinder effective supervision. The supervisor also determines, where appropriate, that these new acquisitions and investments will not hinder effective implementation of corrective measures in the future. [16] The supervisor can prohibit banks from making major acquisitions/investments (including the establishment of cross-border banking operations) in countries with laws or regulations prohibiting information flows deemed necessary for adequate consolidated supervision. The supervisor takes into consideration the effectiveness of supervision in the host country and its own ability to exercise supervision on a consolidated basis.
Description and findings re EC3	As noted in EC 2 above, BSP regulations require that new acquisitions or investments be reviewed in order to assess whether the investment is in accordance with the bank's business plan and management objectives and will complement or support the main business of the bank. Guidelines advise that 'extra caution' should be taken regarding high risk acquisitions or investments. Among the conditions listed for the approval of an application to establish or acquire a subsidiary or affiliate abroad in S. 377 of the MORB is the submission of a certification from the host country that the duly authorized personnel/examiners of the BSP will be authorized to examine the proposed subsidiary or affiliate, thereby allowing the BSP to exercise supervision on a consolidated basis. The guidelines do not directly set forth a clear objective criterion requiring a determination whether host jurisdiction consolidated supervision is effective. Investment by Filipino banks in overseas subsidiaries or operations is minimal. In reviewing applications, both on-site and offsite supervisors assess the viability and sustainability of the bank's business model. The assessment of new acquisitions/investments generally covers their potential impact to the safety and soundness of the financial institution and capability of the financial institution to manage related risks. The processing of requests for approval of acquisitions/investment is conducted by the appropriate supervising departments of the FSS. Personnel tasked to process said requests are expected to have a clear understanding of the enforcement framework of the BSP and familiarity with the scope and the limitations of the BSP's authority to prescribe corrective measures. The appropriate supervising departments also closely coordinate with other concerned departments to better identify the types of investments that tend to hinder the implementation of corrective measures.

[16] In the case of major acquisitions, this determination may take into account whether the acquisition or investment creates obstacles to the orderly resolution of the bank.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	Information sharing MOUs with relevant regulators are in place or being sought in order to ensure adequate coordination and information flows.
EC4	The supervisor determines that the bank has, from the outset, adequate financial, managerial and organizational resources to handle the acquisition/investment.
Description and findings re EC4	S. 371 of the MORB notes that any major investment by a bank should be in accordance with its business plan and management objectives, taking into consideration economic developments and prospects. S. 371 also provides a list of information/documents to be submitted by a bank intending to invest in allied or non-allied undertakings to the BSP, including, among others, the management contract, a list of members of Board and senior management, financial information and other information about financial strengths of the company, and the interest to be held by the bank and the manner in which such interest will be held. S. 371 provides that to establish a subsidiary or affiliate abroad, an applicant bank should meet the standard pre-qualification requirements for grant of banking authority, while S. 377 of the MORB provides qualification requirements for proposed officers of the entity. The information provided by the bank in accordance with S. 371 of the MORB, combined with the BSP's own understanding of the bank via off-site supervision and on-site examination, provides the supervisor with an understanding of whether the bank has adequate financial, managerial and organizational resources to handle the acquisition/investment.
EC5	The supervisor is aware of the risks that non-banking activities can pose to a banking group and has the means to take action to mitigate those risks. The supervisor considers the ability of the bank to manage these risks prior to permitting investment in non-banking activities.
Description and findings re EC5	S. 372 and 375 of the MORB require prior approval for equity investments in financial allied undertakings and equity investments in excess of 40 percent of the total voting stock of non-financial allied undertakings, while S. 376-A of the MORB notes that prior approval of the MB is required for the broad category of non-allied undertakings in which only universal banks may invest, directly or through a subsidiary. S. 371 of the MORB provides the conditions on BSP approval, which include, among others, the condition to address financial, managerial, safety and soundness, compliance, or other concerns. BSP may disapprove a proposed investment if it finds that the proposal would constitute an unsafe and unsound practice, or would violate any law, regulation, MB directive, or any condition imposed by, or written agreement with, the BSP. During the application review, BSP on- and off-site examiners are consulted in order to assess whether the bank's proposed merger/acquisition meets applicable guidelines. The application and staff recommendations are considered by the MB and, as needed, bank management is engaged in the review process.
Assessment of Principle 7	Compliant
Comments	BSP possesses adequate powers to approve or reject and impose prudential conditions upon acquisition or investments by a bank. BSP laws and regulations set forth clear expressions of permitted investments and thresholds, and establishes criteria for approvals,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	including investments by, or in, foreign operations. BSP reviews and assesses major acquisitions and applies reasonable prudential standards. It should be noted, however, that BSP does not possess the power to approve major acquisitions by a bank's parent or the parent's affiliate; and as a result, significant non-banking risks may be added to a conglomerate group without notice, review or approval of BSP.
Principle 8	**Supervisory approach**. An effective system of banking supervision requires the supervisor to develop and maintain a forward-looking assessment of the risk profile of individual banks and banking groups, proportionate to their systemic importance; identify, assess and address risks emanating from banks and the banking system as a whole; have a framework in place for early intervention; and have plans in place, in partnership with other relevant authorities, to take action to resolve banks in an orderly manner if they become non-viable.
Essential criteria	
EC1	The supervisor uses a methodology for determining and assessing on an ongoing basis the nature, impact and scope of the risks: (a) which banks or banking groups are exposed to, including risks posed by entities in the wider group; and (b) which banks or banking groups present to the safety and soundness of the banking system The methodology addresses, among other things, the business focus, group structure, risk profile, internal control environment and the resolvability of banks, and permits relevant comparisons between banks. The frequency and intensity of supervision of banks and banking groups reflect the outcome of this analysis.
Description and findings re EC1	<u>Regulatory Perimeter</u> BSP has been granted authority to supervise, and conduct regular or special examinations of, banking institutions and QBs, including their subsidiaries and affiliates engaged in allied activities. S. 28 of the NCBA, as amended, provides that the supervising and examining department head, personally or by deputy, shall examine the operations of every bank and QB, including their subsidiaries and affiliates engaged in allied activities, and other entities which under this Act or special laws are subject to the BSP supervision, in accordance with the guidelines set by the MB taking into consideration sound and prudent practices. BSP's supervisory responsibilities extend to a wide range of banking operations, each with a distinct set of permissible activities and authorities; these include universal banks, commercial banks, rural banks, thrift banks and cooperative banks. Recent legislation has extended supervisory authority over money service businesses, credit granting businesses, and payment system operators. Despite this wide scope of responsibility, almost 50 percent of banking assets are held by the top 5 universal banking institutions. BSP's supervisory approach reflects a risk-based focus of examination time and resources on the largest and more complex banking groups. <u>Recent Restructuring of BSP's Supervision Function</u> BSP has implemented a new organizational structure that has moved to integrate previously separate on- and off-site staff units and operations. The Financial Supervision

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Sector (FSS) group was approved by the MB in its Resolution (Res.) No. 520 dated 26 March 2018, with the objective of facilitating consolidated supervision and risk-based approach to examination of supervised entities. The FSS is subdivided into five (5) subsectors namely, Financial Supervision Subsectors (FSSSs) I to III, Policy and Specialized Supervision Subsector (PSSS), and the Financial Technology Subsector (FTSS). Under the new structure, on-site and off-site supervision of each banking group is conducted under one group of supervisors. The reorganization took effect from January 1, 2019. The FSSS teams are each allotted banks (and banking groups) across the full range of supervised institutions; each FSSS being assigned D-SIBs and non-D-SIBs. The FSDs are structured in such a way that only one group of supervisors will handle a particular banking group, from the parent bank to its allied subsidiaries and affiliates. The PSSS consists of the Supervisory Policy and Research Department (SPRD), Department of Supervisory Analytics (DSA), Financial System Integrity Department (FSID), and the Treasury and Asset Management Supervision Department (TAMSD). Lastly, the FTSS is comprised of the Payment Systems Oversight Department, and the Technology Risk and Innovation Supervision Department. These departments work in coordination with the FSDs in the conduct of on-site examination and can provide support to the examination teams for issues such as IT infrastructure, capital markets, trust and fiduciary activities, and anti-money laundering. The DSA is the central depository of reports from supervised entities. The DSA collates information provided by regulated banks, analyses them and provides reports to the FSS. The SPRD is the central policy-making department of the Sector. This recent restructuring is in its early phases of implementation, and this assessment is primarily based upon a review of activities that occurred prior to the reorganization, while acknowledging BSP's new approach and structure. <u>Methodology for determining and assessing on an ongoing basis the nature, impact and scope of risks</u> BSP relies on a variety of regulatory reports, micro- and macro-economic inputs, and thematic reviews (discussed in more detail in the following ECs) in order to determine the risks faced by supervised institutions and risks presented the banking system more broadly. BSP employs such analyses into designing the supervisory plan (frequency and intensity), to conduct thematic, special and regular on-site examinations. BSP assesses multiple factors within its supervisory planning and implementation, addressing business focus, group structure, risk profile and internal controls. BSP guidelines establish eight (8) categories of risk for supervision purposes (credit, market, interest rate, liquidity, operational, compliance, strategic and reputation) and focus on the quality of the bank's board or senior management to identify, measure, monitor and control such risks. (MORB, Appendix 69). A methodology has been employed to identify D-SIBs, and such firms are required to comply with heightened prudential standards, including a capital surcharge and the development of recovery plans. BSP has established an Internal Capital Adequacy

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Assessment Process (ICAAP) regimen for its banks, which provides insight into business models and risk profile. Recent regulations require a comprehensive governance structure and serve as the basis for review of banks' internal controls and structures. ICAAP stress test results and BSP-conducted periodic stress tests provide forward-looking assessments of the institutions' risk profiles. BSP rates institutions employing a CAMELS Rating and Risk Assessment System (Supervisory Guidance (SG) No. 2009-21) that serves as basis for supervisory actions (i.e., the intensity of supervision and the gravity of enforcement actions). Ratings range from 1 to 5, with a 5 rating being the highest or strongest. BSP is moving to revise its rating framework, and adopt a framework focused more on key systemic risks and activities. BSP employs a ROCA Rating System (SG No. 2006-34) for foreign bank branches. The ROCA rating divides a foreign branch's overall activities into four components representing the major activities of the branch that may raise supervisory concern: risk management, operational controls, compliance and asset quality. Under the system, a foreign branch is assigned a composite rating of 1 to 5. A rating of 5 indicates the highest rating and the lowest level of supervisory concern, while a rating of 1 indicates the lowest rating and the highest level of supervisory concern. D-SIBs are designated by BSP employing identified criteria, and the list of D-SIBs is updated annually. Those identified as D-SIBs are required to maintain additional Common Equity Tier 1 (CET1) of between 150 and 250 basis points of the bank's Risk-Weighted Assets. D-SIBs must also meet higher supervisory expectations. For example, in the annual submission of their ICAAP document, D-SIBs must have in place acceptable recovery plans (Circular No. 904) which will be carried out in the event of breaches in capital (and other) thresholds. BSP conducted a review of their supervisory approach and has undertaken to address identified gaps including improvements to the analysis of a bank's impact on the financial system, calibration of supervisory activities in relation to the bank's impact and risk profile, develop policies to clarify the use of proportionality in setting prudential requirements, developing a formalized framework for conducting business model analysis, defining an effective way for peering banks, and incorporating more dynamic assessment of banks given the reduced ability to render judgment on qualitative factors (e.g., Management) in between onsite examinations. The Supervisory Assessment Framework Review (SAFR) underway at BSP/FSD is reviewing these elements and revisiting the effectiveness of the CAMELS rating approach.
EC2	The supervisor has processes to understand the risk profile of banks and banking groups and employs a well-defined methodology to establish a forward-looking view of the profile. The nature of the supervisory work on each bank is based on the results of this analysis.
Description and findings re EC2	The BSP "Revised CAMELS Rating and Risk Assessment System (March 2009)" (SG 2009–21) requires a determination of the quantity and direction of risk (e.g., a review of changes to key ratios and the direction of change, relative to peer group). Trends associated with key risk indicators across the rating factors are assessed (e.g. trends in non-performing loans,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	earnings, etc.). Furthermore, in assigning an aggregate risk rating, examiners are instructed to consider whether the firm presents high, moderate or low inherent risk, whether risk management systems appropriately mitigate inherent risks, whether the board and senior management have demonstrated the capacity to identify emerging threats, and whether there are significant weaknesses in risk management that could present potential financial loss (among other factors). The ROEs contain the overall rating (i.e., CAMELS, ROCA), an assessment of the overall financial condition and risk management system of the institution, and its risk profile and direction. The BSP conducts regular on-site exam and off-site surveillance activities. The conduct of on-site and off-site examination processes are supported by SG and guided by Quality Management Standards (QMS). The supervisory cycle is comprised of the following processes: (i) Develop Institutional Profile A comprehensive understanding of the supervised institution is captured in the Institutional Overview (IO). The IO provides the BSFI's risk profile, business model and strategic direction, quality of Board and senior management oversight, quality of risk management, controls and self-assessment functions, key risk areas, and BSP's supervisory approach and plan. It also provides the list of stockholders, Board of directors and principal officers, financial highlights and other relevant information. (ii) Risk Assessment SG No. 2015–01 provides the off-site risk profiling framework for assessing the riskiness of supervised institutions using a predetermined set of criteria and employing a 4-risk profile classification/rating: very low, low, lower medium and medium. The financial institutions subject to risk profiling (every June and December) are as follows: 1. Complex but not D-SIBs – these include (i) universal banks and commercial banks, and (ii) thrift and rural banks identified as complex banks under SG No. 2013-05; 2. Simple banks not under the PCA framework 3. NSSLAs not under the PCA framework 4. Banks and NSSLAs required to execute a LOC or transitioned to enhanced supervision but are not under the PCA framework. D-SIBs are excluded from this off-site risk profiling given their designation, and are subject to more intensive examinations, and heightened prudential requirements (see below). (iii) Supervisory Plan The supervisory plan is documented in the IO and is reviewed and approved by FSD management. The BSP conducts on-site examinations with an interval of at least 12 months between regular examinations. The MB, by an affirmative vote of at least five (5) members, may authorize a special examination if the circumstances warrant. Consolidated supervision through simultaneous on-site examination on the supervised bank, its subsidiaries and affiliates belonging to one conglomerate structure is performed. The examination assesses the institution's risk profile and whether the risk management framework and practices are commensurate with the existing risk exposures and strategic direction. The assessment of performance and risk management practices includes horizontal analysis regarding how the institution compares to its peers and the banking industry.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	(iv) Scoping examination activities The Examiner-in-Charge (EIC) together with the Department-in-Charges (DEICs), as applicable, prepare the Scope Memorandum, which contains the type of on-site supervisory assessment (i.e., regular, special or overseeing), examination methodology to be adopted (i.e., focused or baseline examination), scope of examination activities, key risk areas of focus including specific examination procedures and sampling techniques, staffing, examination timelines, and deliverables. SG No. 2015-02 provide guidance regarding the conduct of examination and overseeing of banks, quasi-banks and their subsidiaries/affiliates. The SG further provides the coverage, criteria and cycle relative to the conduct of focused examination. Additional guidance is provided regarding the scoping of examinations (SG 2009–33, amended by 2011–03). (v) Conduct examination activities and report conclusion The main output of the examination is the Report of Examination (ROE), which contains the overall rating (i.e., CAMELS, ROCA), an assessment of the overall financial condition and risk management system of the institution, and its risk profile and direction. Significant issues and areas of concern are identified and discussed with the concerned banks. The BSP requires management to provide plans to remediate significant issues. Directives in the ROE are then imposed (including sanctions whenever applicable), as approved by the appropriate BSP authorities, with specific timeframes. Results of on-site examination are communicated to the Board of directors and management. Action plans after the release of the ROE are monitored by the respective supervising departments and results of the examination are considered in the development of the IO, supervisory plan and risk assessment. The assessors reviewed a sample of ROEs for both small and large institutions and found the reports to provide well-written, organized and comprehensive reviews of the firm's risk profile, main business lines and activities, financial information and compliance with regulatory standards, including a detailed set of recommendations and instructions to the firm related to required remediation efforts. The ROEs reviewed were of high quality and reflected in depth and substantive oversight of the firms. See EC 11 for a discussion of enforcement tools and monitoring processes.
EC3	The supervisor assesses banks' and banking groups' compliance with prudential regulations and other legal requirements.
Description and findings re EC3	BSP's supervisory approach is founded upon oversight of the capabilities and effectiveness of the Board and senior management to fulfill their responsibility to ensure the firm is operated in a manner consistent with prudential and legal requirements. Regulations enhancing corporate governance requirements and addressing effectiveness of regulatory reporting set expectations for firms. BSP assesses banks' and banking groups' compliance with prudential regulations and other legal requirements through its on-site examination process. Circular No. 969 revised the corporate governance guidelines and include expectations on governance process with regard to reporting and ensuring regulatory compliance. The Audit Committee is expected to be responsible in overseeing the financial reporting

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	framework (i.e., financial reporting process, practices, and controls) and to ensure that the reporting framework enables the generation and preparation of accurate and comprehensive information and reports. Further, institutions are expected to ensure that their risk reporting is accurate (reports should be reconciled and validated), comprehensive, and clear and useful. Circular No. 963 sets forth the BSP's expectation on banks to establish an effective reporting system with an appropriate governance process that enables the generation and timely submission of reports that are in accordance with the BSP's reporting standards. The guideline provides that reports submitted to the BSP must be complete, accurate, consistent, reliable and timely. It is expected that banks have adequate internal controls in place to ensure adherence to the reporting standards. Banks which are not compliant with the reporting standards will be imposed monetary and/or non-monetary sanctions. Further, if the results of the assessment disclose significant deficiencies in the bank's reporting system, the bank shall be required to submit a Board-approved action plan with specified time frame. Non-implementation of the required corrective measures within the specified time frame shall be grounds to subject the bank to the BSP Supervisory Enforcement Policy.
EC4	The supervisor takes the macroeconomic environment into account in its risk assessment of banks and banking groups. The supervisor also takes into account cross-sectoral developments, for example in non-bank financial institutions, through frequent contact with their regulators.
Description and findings re EC4	In the development of the IO and supervisory plan, BSP takes into account certain macro-economic information, which can provide insights into cross-sectoral developments and non-bank financial institutions. Macro-economic inputs are obtained primarily through the Financial Stability Report (FSR) and from information gained from the conduct of cross-sectoral interagency forums. Insights into the potential risks posed by macro-economic shocks are analyzed in conjunction with the reviews of ICAAP stress test results, and BSP conducted stress testing. <u>Financial Sector Forum</u> The FSF facilitates consultations and the exchange of information among its members on matters related to the supervision and regulation of financial institutions under its respective jurisdiction. In the October 2017 FSF meeting, the issue of investing in crowdfunding, foreign exchange trading, and virtual currency was raised in view of their riskiness and inability of existing regulations to fully capture their business model. As a result of the FSF discussions, the BSP issued an advisory regarding online foreign exchange brokerage and trading platforms (M-2018-032). The meetings and inputs from the FSF are not statutorily mandated and the analysis and outputs are developed at the discretion of its members. <u>Financial Stability Coordination Council</u> The FSCC was established in January 2014 to identify, manage and mitigate the build-up of systemic risks to safeguard the stability of the Philippine financial system. It is a voluntary inter-agency council composed of the BSP, the SEC, the PDIC, the IC and the DOF with the

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	BSP Governor designated as the chairman of the Executive Committee. The FSCC meets quarterly and the main agenda item is the Systemic Risk Review. The technical work of the FSCC is principally undertaken by the Office of Systemic Risk Management (OSRM) of the BSP, which is tasked to develop frameworks for continuing surveillance and tracking of systemic risks, measure the buildup of vulnerabilities through continuing research, assess systemic implications of national, regional and global policy initiatives to the domestic financial system, and recommend and/or implement policy options, positions, communication plans, advocacy initiatives, and learning programs related to financial stability. The FSCC published its first FSR in June 2018. The FSR takes a thematic assessment of the various risks that could pose a challenge to the continued growth of the Philippine economy as well as the resilience of the Philippine financial system. <u>Banking System Risk Analysis Report</u> The Banking System Risk Analysis (BSRA) report utilizes statistical analysis tools such stress-testing and thresholds model in identifying emerging risks, both on a micro- and macro-level. The BSRA flags BSP management on the emerging risks with supporting technical analysis on a quarter-on-quarter and year-on-year bases, and shows the supervisory actions taken by the FSS, as well as the mitigating measures undertaken by banks concerned. The BSRA also recommends policy measures that will facilitate in-depth and meaningful analysis of emerging risks and vulnerabilities. <u>Banking Sector Outlook Survey</u> The Banking Sector Outlook Survey (BSOS) gathers the sentiments of the Presidents/Chief Executive Officers/Country Managers of banks in the country within a two-year horizon. The BSOS aims to provide the BSP with additional perspective on the evolution of banks' business models and provide supervisory and market perspectives on emerging issues and trends.
EC5	The supervisor, in conjunction with other relevant authorities, identifies, monitors and assesses the build-up of risks, trends and concentrations within and across the banking system as a whole. This includes, among other things, banks' problem assets and sources of liquidity (such as domestic and foreign currency funding conditions, and costs). The supervisor incorporates this analysis into its assessment of banks and banking groups and addresses proactively any serious threat to the stability of the banking system. The supervisor communicates any significant trends or emerging risks identified to banks and to other relevant authorities with responsibilities for financial system stability.
Description and findings re EC5	BSP develops a BSRA Report, a FSR, and maintains co-operative arrangements with other regulatory agencies. These reports are comprehensive and assess trends and emerging risks presented the financial sector and banking industry. The analyses and reports are shared within existing interagency and industry fora, and there are internal processes to encourage discussion of emerging risks within BSP/FSD. In particular, within BSP, there is a bi-monthly "Meeting on Surveillance and Crisis Management" which aims to discuss cross-cutting issues, emerging risks, and corresponding supervisory actions. Emerging risks or

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	trends are shared within the FSF. Such analyses are employed to scope annual examinations and/or conduct special examinations.
EC6	Drawing on information provided by the bank and other national supervisors, the supervisor, in conjunction with the resolution authority, assesses the bank's resolvability where appropriate, having regard to the bank's risk profile and systemic importance. When bank-specific barriers to orderly resolution are identified, the supervisor requires, where necessary, banks to adopt appropriate measures, such as changes to business strategies, managerial, operational and ownership structures, and internal procedures. Any such measures take into account their effect on the soundness and stability of ongoing business.
Description and findings re EC6	BSP requires D-SIBs to develop recovery plans, which are assessed during a review of ICAAP. Circular No. 904 provides the guidelines on recovery plan of D-SIBs. Among the supervisory requirements is the plan to set forth concrete and reasonable actions that a bank will take to restore its viability in cases of significant deterioration of its financial condition in different scenarios. Recovery options are expected to include actions that reduce the risk profile, raise or conserve capital and address liquidity pressures, and the D-SIB is expected to seriously consider specific drastic measures that could modify its structure and/or business model. The adequacy of recovery plans is assessed by BSP during regular examinations as an element of the ICAAP Supervisory Review Process (SRP). While recovery plans may provide insights to resolvability, such as identifying obstacles to divestiture or restructuring, they do not substitute for conducting a resolvability assessment. At present, there is no resolvability assessment process in place, in conjunction with PDIC, with respect to BSP supervised firms, including its D-SIBs. At present, the authorities are not developing bank-specific resolution plans that would set out the resolution strategy and operating plan for the orderly resolution of regulated banks, even large or complex entities or D-SIBs. Resolvability assessments would assess the feasibility of whether the resolution strategy and operational plan are an intrinsic part of the resolution planning process. The development of resolution plans and the assessment of resolvability is especially challenging to BSP and PDIC given the complex, conglomerate structures within which large institutions, including D-SIBs, operate. While BSP's supervisory authority may not extend to the parent or its affiliates, BSP has the power to require a BSFI to consider its structure and operations within the wider group and adopt measures to address impediments to their resolvability.
EC7	The supervisor has a clear framework or process for handling banks in times of stress, such that any decisions to require or undertake recovery or resolution actions are made in a timely manner.
Description and findings re EC7	BSP relies upon its PCA and Banks for Resolution (BRes) Frameworks, as well as the Financial Crisis Management Framework (FCMR) to handle banks in times of crisis. BSP Circular No. 523 on the PCA Framework provides that a bank shall be initiated into the PCA Framework under identified conditions. The initiation of PCA, approval of the MOU, declaration of failure of PCA, lifting of PCA status and re-initiation to PCA shall be reported to the PDIC within two banking days from the date of receipt of MB Resolution, for notation.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC7	Banks declared failure of PCA shall be considered as BRes Framework. BRes banks have serious problems that exhibit severe deficiencies in capital, poor operating performance and/or critically deficient liquidity, poor corporate governance and significant weaknesses in business processes and risk management, which are unlikely to be addressed in the near term. SG No. 2019–02 aims to: 1) Provide guidelines and procedures on resolution options: a. Negative Resolution—includes prohibition from doing business, deferral of action on the recommendation in the ROE with grounds for closure; or b. Positive Resolution—takeover of a qualified third-party investor/willing and capable management, significant existing stockholders' infusion, lifting of sanctions relative to PCA failure and transition to enhanced supervision or revert to normal supervision. 2) Facilitate the effective and timely resolution of problem banks; and 3) Strengthen BSP's coordination with PDIC, taking into consideration its power under its Charter, as amended. In particular, coordination includes scheduling of bank examination, joint onsite examination, meeting with PDIC representatives and notification to PDIC (i.e., advice on the prohibition from doing business, notification of the "Positive Resolution," and notification on joint onsite examination). The PCA and BRes frameworks are not designed or implemented to effectively and fully address crisis events. The PCA and BRes frameworks are implemented as enhanced supervision tools and are employed primarily to return troubled firms to financial health and stability. The BRes framework only authorizes BSP to 'facilitate' mergers or acquisitions, and only while an institution is open and operating. The BRes framework does envision reaching a point where the PDIC is appointed receiver, and it is possible that such action could take place quickly. However, the current implementation of PCA/BRes is ponderous and does not avoid undue regulatory forbearance and require prompt action, see discussion at BCP 11. More vital is that resolution plans have not been developed for supervised firms, including D-SIBs, nor have resolvability assessments been conducted. These elements are vital in order to ensure that crisis or stress events are addressed in a timely fashion. It is acknowledged that the BSP works to assess the build-up of risks, trends and concentrations within and across the banking system, in conjunction with other regulators, within the FCMR adopted by the BSP, PDIC, SEC and IC on April 1, 2016 (it was further amended on September 2, 2016). The Framework is to be supported by internal operational 'handbooks' developed by key agencies. The Handbooks address BSP's surveillance mechanism during normal times and protocols in times of financial crisis. The Framework is founded upon on existing resolution tools and processes, which do not include bank-specific resolution plans, and has not been applied in real crisis events.
EC8	Where the supervisor becomes aware of bank-like activities being performed fully or partially outside the regulatory perimeter, the supervisor takes appropriate steps to draw the matter to the attention of the responsible authority. Where the supervisor becomes

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC8	aware of banks restructuring their activities to avoid the regulatory perimeter, the supervisor takes appropriate steps to address this.
Description and findings re EC8	Banking activities are broadly defined, and most financial or 'bank-like' activities fall within BSP's regulatory ambit (banking, investment houses, trust). BSP maintains information-sharing MOAs with relevant domestic authorities and has cited an instance where coordination conducted by nonbank entities that posed risk to the system has occurred. There has been no instance reported or detected regarding a restructuring effected in order to avoid regulation. Recent amendments to the BSP charter have brought within BSP's regulatory perimeter certain activities, including money service business, credit granting agencies and payment system providers. BSP is establishing new staff structures and is developing policies and procedures to address these activities that were recently outside their regulatory perimeter. FSD has initiated the establishment of an off-site surveillance function to closely monitor the affairs of financial institutions that are not under the supervision of the BSP using various media (i.e., online, print, broadcast). Given the restrictions that limit BSP's authorities related to the broader non-banking conglomerate groups and their activities, bank-like activities that may be performed could escape BSP oversight.
Assessment of Principle 8	Largely Compliant
Comments	BSP maintains an effective system of banking supervision that is evolving to enhance current abilities to develop a more forward-looking and risk-based approach to oversight of banks, bank groups and systemically important firms. BSP reviews and assesses risks to the banking system as a whole and imports such analysis into its oversight of individual banks. At present, there is no resolvability assessment process in place, in conjunction with PDIC, with respect to BSP supervised firms, including its D-SIBs. The authorities have not developed bank-specific resolution plans that would set out the resolution strategy and operating plan for the orderly resolution of regulated banks, even large or complex entities or D-SIBs. BSP's framework for early intervention and its approach to assessing resolvability of firms, especially D-SIBs, is not fully developed. Recommendations: • Develop and implement, in conjunction with PDIC, policies and standards to assess resolvability of firms, especially D-SIBS, in an orderly fashion. • Develop and implement policies and standards requiring regulated financial institutions to support a resolvability assessment, which would include consideration of inter-connectedness, structure and operations within the wider group and adopt measures to address impediments to resolvability.
Principle 9	**Supervisory techniques and tools**. The supervisor uses an appropriate range of techniques and tools to implement the supervisory approach and deploys supervisory

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Principle 9	resources on a proportionate basis, taking into account the risk profile and systemic importance of banks.
Essential criteria	
EC1	The supervisor employs an appropriate mix of on-site [/17] and off-site [/18] supervision to evaluate the condition of banks and banking groups, their risk profile, internal control environment and the corrective measures necessary to address supervisory concerns. The specific mix between on-site and off-site supervision may be determined by the particular conditions and circumstances of the country and the bank. The supervisor regularly assesses the quality, effectiveness and integration of its on-site and off-site functions, and amends its approach, as needed.
Description and findings re EC1	As the result of its internal assessment of supervisory operations, BSP has recently restructured its supervisory structure and has integrated previously separate on- and off-site staff and activities. Effective January 2019, the FSS organizational has combined off-site supervision and onsite examination into one department FSD. FSD conducts risk-focused on-site examination of banks with an interval of at least 12 months between regular examinations. BSP's examinations are conducted with a mix of generalist staff, supported by specialist/expert teams and off-site analysis. Exam scopes regularly include a review of a supervised institution's risk profile and internal controls and imposes corrective measures. Staffing for smaller and less complex banks is proportionate to such banks' risk profile and operations. D-SIBs are ensured the most frequent and intensive examinations. Cross-cutting risks and horizontal peer analysis is conducted. Regular management meetings are the primary forum to review and discuss issues identified across firms and consider best practices. A staff level roundtable has been established in order to encourage the sharing of supervisory information across the FSS teams. In addition, BSP employs a variety of off-site supervisory tools to evaluate firms under their supervision. Given the new operational structure, which allocates D-SIBs across separate supervisory teams, BSP should continue to develop processes and fora to ensure that supervisory issues and concerns are shared, and best practices identified in order to bring to bear a uniform and consistent supervisory response.
EC2	The supervisor has a coherent process for planning and executing on-site and off-site activities. There are policies and processes to ensure that such activities are conducted on a thorough and consistent basis with clear responsibilities, objectives and outputs, and that there is effective coordination and information sharing between the on-site and off-site functions.
Description and findings re EC2	BSP supervisory process revolves around the planning and execution of the annual examination. Off-site analysis feeds into the development of an IO which drives the examination planning.

[17/] On-site work is used as a tool to provide independent verification that adequate policies, procedures and controls exist at banks, determine that information reported by banks is reliable, obtain additional information on the bank and its related companies needed for the assessment of the condition of the bank, monitor the bank's follow-up on supervisory concerns, etc.

[18/] Off-site work is used as a tool to regularly review and analyze the financial condition of banks, follow up on matters requiring further attention, identify and evaluate developing risks and help identify the priorities, scope of further off-site and on-site work, etc.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	The processes for planning and executing on-site and off-site activities are set forth in multiple SGs that have been issued to provide guidance on responsibilities, objectives and outputs. Examiners are guided by the Manual of Examination Procedures for BSFIs (REF-SES-Onsite-02-21-000). Quality controls are in place through the adoption of QMS. Conduct of on-site examination is performed in accordance with the On-Site examination QMS while off-site surveillance is guided by the off-site QMS. FSD management reviews and approves key documents, such as the ROE. FSD management heads meet monthly to review supervisory plans and operations.
EC3	The supervisor uses a variety of information to regularly review and assess the safety and soundness of banks, the evaluation of material risks, and the identification of necessary corrective actions and supervisory actions. This includes information, such as prudential reports, statistical returns, information on a bank's related entities, and publicly available information. The supervisor determines that information provided by banks is reliable [/19] and obtains, as necessary, additional information on the banks and their related entities.
Description and findings re EC3	The BSP requires a range of prudential reports from supervised institutions (see discussion in Principle 10). Appendix 7 of the MORB specifies the reports (and frequency, by institution type) that are to be submitted to the BSP. These reports include, but not limited to, the following: (1) Financial Reporting Package (FRP) (2) Published Balance Sheet (3) Capital Adequacy Ratio Report (4) Report on Real Estate Exposures (5) Liquidity Coverage Ratio Report/Minimum Liquidity Ratio Report (6) Leverage Ratio Report (7) Report on Material Related Party Transactions (8) Conglomerate Structure (9) Credit and Equity Exposures to Individuals/Companies/Groups aggregating Php 1.0 million and above to be submitted on quarterly basis (10) Foreign Exchange (FX) Position Report (11) ICAAP Document and Recovery Plan (12) Uniform Stress Testing Report (13) DOSRI (Directors, Officers, Stockholders and Related Interests) Report (14) Report on Required Reserves (15) Report on Crimes and Losses (crime-related incidents to which banks have been exposed) (16) Annual Report. The Bank Performance Report (BPR) provides detailed information about a bank's financial condition across several time periods and how it compares with its peers and the industry as a whole.

[19/] Please refer to Principle 10.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	This is complemented by the Bank Dashboard which provides a quick but comprehensive summary of the financial and non-financial information of individual banks as gathered from reports prescribed for submission, as well as qualitative assessments and analysis coming from offsite supervision and onsite examination. The Bank Dashboard also includes a description of the bank's business model, corporate strategies and its primary risk concerns. In addition to the regular review and assessment of the operations of individual banks, a Heat Map is developed to analyze the level of riskiness of key areas of the industry on a range of 1 to 4 (with 4 as highest) through the application of certain risk measurement criteria covering asset quality, liquidity, profitability, and solvency. BSP relies upon the institutions as the first line of defense to ensure accuracy of prudential reports. Regulations set forth requirements regarding the integrity and accuracy of reports submitted to the BSP. BSP conducts additional validation of prudential report data when received and pursues deficiencies in quality or timeliness of information reported.
Description and findings re EC3	Circular No. 963 sets forth the BSP's expectation on banks to establish an effective reporting system with an appropriate governance process that enables the generation and timely submission of reports that are in accordance with the BSP's reporting standards. The guideline provides that reports submitted to the BSP must be complete, accurate, consistent, reliable and timely. It is expected that banks have adequate internal controls in place to ensure adherence to the reporting standards. Banks which are not compliant with the reporting standards will be imposed monetary and/or non-monetary sanctions. Further, if the results of the BSP assessment disclose significant deficiencies in the bank's reporting system, the bank shall be required to submit a Board-approved action plan with specified time frame. Non-implementation of the required corrective measures within the specified time frame shall be grounds to subject the bank to the BSP Supervisory Enforcement Policy. Circular No. 969 regarding corporate governance standards provides expectations on oversight and accuracy of financial and risk reporting. The Audit Committee is expected to be responsible in overseeing the financial reporting framework (i.e., financial reporting process, practices, and controls) and to ensure that the reporting framework enables the generation and preparation of accurate and comprehensive information and reports. Institutions are expected to ensure that their risk reporting practices comply with the principles of accuracy (reports should be reconciled and validated), comprehensiveness, and clarity and usefulness. In cases where additional information is needed between examinations or when there is an ongoing study requiring information not captured in the prudential reports, the BSP, through the FSDs, conducts a survey for that purpose.
EC4	The supervisor uses a variety of tools to regularly review and assess the safety and soundness of banks and the banking system, such as: (a) analysis of financial statements and accounts; (b) business model analysis; (c) horizontal peer reviews; (d) review of the outcome of stress tests undertaken by the bank; and

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC4	(e) analysis of corporate governance, including risk management and internal control systems. The supervisor communicates its findings to the bank as appropriate and requires the bank to take action to mitigate any particular vulnerabilities that have the potential to affect its safety and soundness. The supervisor uses its analysis to determine follow-up work required, if any.
Description and findings re EC4	BSP receives and reviews supervised firms' financial statements, conducts business model analysis and horizontal peer reviews, reviews the outcomes of stress test undertaken within the firms' ICAAP, Real Estate Stress Test (REST) requirements, BSP-conducted stress tests, and assesses compliance with corporate governance standards. Findings are communicated to banks' senior management and Boards of directors primarily through issuance of the ROE, but frequent interactions during the on-site examination are common. Ad hoc, periodic contacts with Board members or senior management do occur in between examinations. The ROE is provided to the BSP and the bank's Board, and the firm is required to develop a plan to address the examination issues and concern. FSD then evaluates the viability of the bank's plans and monitors remediation. The assessment of business model is currently embedded in the IO and incorporated into development of the scope of on-site examination. The assessment includes an analysis of the sustainability, viability, safety and soundness of the business model and how the business model is related to the bank's risk assessment, ICAAP and stress testing. The results of the assessment are reflected in the ROE. Horizontal peer analysis is conducted through the BPR.
EC5	The supervisor, in conjunction with other relevant authorities, seeks to identify, assess and mitigate any emerging risks across banks and to the banking system as a whole, potentially including conducting supervisory stress tests (on individual banks or system-wide). The supervisor communicates its findings as appropriate to either banks or the industry and requires banks to take action to mitigate any particular vulnerabilities that have the potential to affect the stability of the banking system, where appropriate. The supervisor uses its analysis to determine follow-up work required, if any.
Description and findings re EC5	BSP develops information related to individual bank and system-wide risks and employs a variety of vehicles to communicate to banks and other regulators. BSP requires banks to conduct its own internal, stress tests. Supervisory policies and actions have resulted, including thematic supervisory work performed across identified emerging risks (e.g., related party transaction). <u>BSP Uniform Stress Testing Framework for banks</u> The BSP implemented the uniform stress testing framework for universal and commercial banks. The exercise is being conducted twice a year, in June and December. The framework aims to provide the BSP with information to formulate appropriate policies and measures to address emerging risks in the Philippine banking system. It also sets out the specific approaches that banks should, at a minimum, undertake when they different types of risks to stress tests. The risk parameters used are exposures to credit and market risk. The credit risk stress testing focused on three categories: (i) exposure to top 20 conglomerates; (ii) exposures by economic activity; and (iii) consumer finance portfolio;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	focusing on the top 12 conglomerates in the country. Meanwhile, market risk, used the simple sensitivity analysis with parallel shift on interest rates per tenor buckets and foreign exchange rates. A report on the results of the uniform stress testing is prepared by the OSRM. Banking System Risk Analysis Report The BSRA report utilizes statistical analysis tools such as stress-testing and thresholds modelling in identifying emerging risks, both on a micro- and macro- level. The BSRA flags to BSP management any emerging risks, with supporting technical analysis, on a quarter-on-quarter and year-on-year bases, and shows the supervisory actions taken by the FSS, as well as the mitigating measures undertaken by the banks concerned. The BSRA also recommends policy measures that will facilitate in-depth and meaningful analysis of emerging risks and vulnerabilities. The BSRA synthesizes previous stand-alone reports on real estate exposures, consumer loans and non-performing loans of universal, commercial and thrift banks, risk-based capital adequacy ratios (CAR) of universal and commercial banks and their subsidiary banks and QBs, risk-based CAR of stand-alone banks under the Basel 1.5 capital framework, cross-border financial position of universal, commercial and thrift banks, LCR and leverage ratio of universal and commercial banks, stress testing exercises on loan write-offs (real estate, consumer, conglomerates), and market risk. Banking Sector Outlook Survey The BSOS gathers the sentiments of the Presidents/Chief Executive Officers/Country Managers of banks in the country within a two-year horizon. The BSOS aims to provide the BSP with additional perspective on the evolution of banks' business models and provide supervisory and market perspectives on emerging issues and trends Financial Sector Forum The FSF, discussed above, also serves as a forum for discussing emerging risks across the financial system.
EC6	The supervisor evaluates the work of the bank's internal audit function, and determines whether, and to what extent, it may rely on the internal auditors' work to identify areas of potential risk.
Description and findings re EC6	Circular No. 871 sets out the BSP regulations on Internal Audit (IA). The circular provides the responsibilities of the Board, audit committee, senior management (particularly the head of the IA function) and all personnel regarding internal controls and IA. The Circular further provides on the required professional competence, independence and objectivity, charter and scope of the IA function. Assessment of the adequacy of the IA function is conducted during on-site examination. See BCP 26 on Internal Control and Audit.
EC7	The supervisor maintains sufficiently frequent contacts as appropriate with the bank's Board, non-executive Board members and senior and middle management (including heads of individual business units and control functions) to develop an understanding of

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC7	and assess matters such as strategy, group structure, corporate governance, performance, capital adequacy, liquidity, asset quality, risk management systems and internal controls. Where necessary, the supervisor challenges the bank's Board and senior management on the assumptions made in setting strategies and business models.
Description and findings re EC7	BSP communication with banks' Boards, independent directors, and senior management, are primarily conducted during or surrounding the on-site examination process. Ad hoc communications in-between examinations are not uncommon but are not on an established (e.g., quarterly) schedule and, depending upon the issue, may require prior consultation with the senior BSP officials or the MB before a communication is conducted. On-site examination procedures such as bank visits, walk-throughs, interviews, exit discussions with the members of the bank's Board and senior management are conducted. Frequent communication with senior bank management occurs during evaluation of replies on the ROEs, processing of requests/queries from the banks, evaluation of documents submitted (ICAAP, stress testing, etc.), and other concerns arising from supervisory work. BSP has challenged banks' assumptions during the conduct of on-site examinations and has provided detailed directives in ROEs.
EC8	The supervisor communicates to the bank the findings of its on- and off-site supervisory analyses in a timely manner by means of written reports or through discussions or meetings with the bank's management. The supervisor meets with the bank's senior management and the Board to discuss the results of supervisory examinations and the external audits, as appropriate. The supervisor also meets separately with the bank's independent Board members, as necessary.
Description and findings re EC8	Following discussions with Board and senior management, the final ROE is communicated to bank management. BSP meets with senior management and the Board to discuss results of the examination. SGs require discussion of the ROE exclusively with independent directors (SG No. 2018-01). Under this SG, examiners shall hold a meeting with the independent directors to discuss issues, concerns, and/or feedback on the control and self-assessment functions, implementation of code of ethics, handling of issues on conflict of interest and implementation of whistle blowing policy, or other key areas of interest to the examination team of the independent directors. The discussion should also cover key examination issues that may affect the safety and soundness of the institution. Material adverse findings by the external auditor are disclosed/reported to the BSP. Significant issues or concerns raised by external auditors are evaluated. In case these warrant supervisory actions, the bank is given opportunity to explain. The concerned FSD will evaluate the explanation and will make the appropriate recommendation. The issues raised by the external auditors will also be considered during on-site examination. The BSP does not meet regularly with external auditors, such as in preparation for the annual examination.
EC9	The supervisor undertakes appropriate and timely follow-up to check that banks have addressed supervisory concerns or implemented requirements communicated to them. This includes early escalation to the appropriate level of the supervisory authority and to the bank's Board if action points are not addressed in an adequate or timely manner.
Description and findings re EC9	After the release of the ROE to the Board, the bank is given 30 calendar days to submit a report containing (1) actions that have been taken on each directive including the documentary evidence to support the Board and senior management's representation; and (2) plan of actions on those directives that are not yet fully complied with and the

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC9	corresponding committed timelines. Non-compliance with BSP directives will result in more stringent supervisory actions, which may include monetary and non-monetary sanctions, execution of a LOC, or placing the bank under PCA. SG 2016-10 provides the internal policies and procedures related to the handling of LOCs. The SG provides a basic prescribed period of one (1) year within which to comply with the commitments in the LOC in order to address the identified supervisory issues and concerns. The one-year timeline is generally not extendible except in meritorious cases. Failure to substantially comply with the commitments stated in the LOC would warrant escalated enforcement actions and may involve imposition of appropriate sanctions on the institution and/or its responsible directors/officers. SG 2016–03 on enhanced supervision provides guidelines on the PCA period of (1) year from the date of PCA initiation within which to implement corrective measures to address the underlying problems or concerns. The PCA period can only be extended in exceptional cases, which should not exceed three (3) years and with prior MB approval. BSP monitors outstanding supervisory issues or concerns via regular monitoring during monthly FSD management meetings, and quarterly updates on LOCs and PCAs are developed and submitted to the MB. In practice, follow-up on directives and LOCs are conducted primarily during on-site examinations. LOCs can and have been amended and extended and firms can linger within PCA status for prolonged periods. See discussion under BCP 11.
EC10	The supervisor requires banks to notify it in advance of any substantive changes in their activities, structure and overall condition, or as soon as they become aware of any material adverse developments, including breach of legal or prudential requirements.
Description and findings re EC10	Existing regulations require prior approval of the BSP for certain substantive changes in firms' activities and structure, including, for example, obtaining additional permissions/licenses (trust, derivatives, e-banking licenses), establishment of branches by foreign or domestic institutions, engaging in mergers or acquisitions and investment in equity instruments of another bank or NBFI over certain thresholds. BSP holds the bank management responsible for the immediate reporting of breaches in prudential requirements like CAR and LCR, and the activation of recovery plans. Circular No. 900 on operational risk management framework provides the guidelines on the required notification/reporting to BSP related to operational risk events. As prescribed, institutions should notify the BSP within 10 calendar days from the date of discovery, any operational risk events that may result in any of (i) significant operational losses or exposures; (ii) activation of business continuity plan; or (iii) any material change in business and operating environment. Upon receipt of notification, the BSP may require, if warranted, the reporting firm to submit a report detailing the causes and impact of such events and an acceptable action plan to address the issue and any other weakness identified. In addition, external auditors are also required under S. 174 and Appendix 55 of the MORB, to submit to the BSP within 15 calendar days after the closing of the audit engagement a

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC10	notarized certification that there are no matters (e.g., fraud, dishonesty, breach of laws, etc.) to report. There is no explicit regulatory mandate to inform BSP of 'material adverse developments', generally, although in practice communication of any such events has been received in a timely fashion.
EC11	The supervisor may make use of independent third parties, such as auditors, provided there is a clear and detailed mandate for the work. However, the supervisor cannot outsource its prudential responsibilities to third parties. When using third parties, the supervisor assesses whether the output can be relied upon to the degree intended and takes into consideration the biases that may influence third parties.
Description and findings re EC11	BSP has contracting authority to retain third party consultants or advisors. To date, the BSP has not appointed independent third parties to conduct supervisory tasks. S. 58 of the GBL provides that the MB may require a bank to engage the services of an independent auditor to be chosen by the bank from a list of external auditors acceptable to the MB. The terms of engagement are prescribed either on a continuing basis where the auditor shall act as resident examiner or on the basis of special engagements.
EC12	The supervisor has an adequate information system which facilitates the processing, monitoring and analysis of prudential information. The system aids the identification of areas requiring follow-up action.
Description and findings re EC12	BSP receives various reports and data from supervised institutions, primarily via the FRP, adequate to support prudential analysis. The data intake and validation processes involve a two-step process where completeness and accuracy are determined, unacceptable reports rejected, late reporting identified, and flagged for follow up. Inadequate or untimely reports are identified promptly, and 'habitual' offenders are referred to the FSD teams for follow up. Data systems are being upgraded to allow for the submission of data through a web portal (presently) and BSP is moving to develop a comprehensive data warehouse. The data warehousing project is a bank-wide initiative to be executed in phases. Business intelligence tools available through the Data Warehouse will enable users to define essential report parameters with options for automated generation business and analytical reports and data analysis. Among the relevant information accessible through the Data Warehouse are the capital adequacy ratios and statistics, SME and Agri-Agra compliance profile, reserve position and reports, trust statistics, financial statements (i.e. balance sheet, income statement and corresponding schedules), trust reports, reported crimes and losses, special authorities, and directors/officers of supervised institutions, other key prudential banking indicators/statistics and the BPR, which presents a comprehensive statistical comparative of a bank's three-year historical performance vis-à-vis its peer group and industry.
Assessment of Principle 9	Compliant
Comments	BSP employs an effective range of examination techniques and tools to support its supervisory processes and approach in relation to BSP regulated financial institutions. On-site and off-site monitoring has been integrated into supervisory departments assigned a range of financial institutions, and multiple bank-specific and macro-economic analyses are taken into consideration in scoping and conducting examinations. The integration of

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	examination activities was implemented at the beginning of 2019, with advance preparatory steps being taken, and will take time to fully complete and assess performance under the new structure. Examinations incorporate a comprehensive review of financial statement and accounts, business model analysis and horizontal peer reviews, and incorporate stress testing results. Findings are communicated to the bank via the ROE in an adequate timely fashion, with clear directives setting forth supervisory expectations. Mandated corrective actions are monitored and followed in monthly and quarterly updates and reviewed in depth during on-site examinations. The scope and intensity of examinations reflect the size, complexity and risk profile of the bank, employing bank-level and banking system analysis, including peer reviews.
Principle 10	**Supervisory reporting**. The supervisor collects, reviews and analyses prudential reports and statistical returns [/20] from banks on both a solo and a consolidated basis, and independently verifies these reports through either on-site examinations or use of external experts.
Essential criteria	
EC1	The supervisor has the power [/21] to require banks to submit information, on both a solo and a consolidated basis, on their financial condition, performance, and risks, on demand and at regular intervals. These reports provide information such as on- and off-balance sheet assets and liabilities, profit and loss, capital adequacy, liquidity, large exposures, risk concentrations (including by economic sector, geography and currency), asset quality, loan loss provisioning, related party transactions, interest rate risk, and market risk.
Description and findings re EC1	BSP has the power to require banks to submit information, on both a solo and a consolidated basis, on their financial condition, performance, and risks, on demand and at regular intervals. S. 25 of the NCBA provides that the department heads and the examiners of the FSS departments are authorized to, among others, "compel the presentation of all books, documents, papers or records necessary in their judgment to ascertain the facts relative to the true condition of any institution as well as the books and records of persons and entities relative to or in connection with the operations, activities or transactions of the institution under examination, subject to the provision of existing laws protecting or safeguarding the secrecy or confidentiality of bank deposits as well as investments of private persons, natural or juridical, in debt instruments issued by the Government." S. 28 of the NCBA requires banks to afford the head of the appropriate supervising and examining departments and to his authorized deputies, full opportunity to examine its books, cash and available assets and general condition at any time during banking hours when requested to do so by the BSP. S. 60 of the GBL provides that every bank, QB or trust entity shall submit to the BSP financial statements in such form and frequency as may be prescribed. Such statements shall show the actual financial condition and results of operations of the institution and of its branches, offices, subsidiaries and affiliates, and other information as may be required by BSP regulations.

[20/] In the context of this Principle, "prudential reports and statistical returns" are distinct from and in addition to required accounting reports. The former are addressed by this Principle, and the latter are addressed in Principle 27.

[21/] Please refer to Principle 2.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	BSP regulations require that supervised institutions submit reports that provide information regarding on- and off-balance sheet assets and liabilities, profit and loss, capital adequacy, liquidity, large exposures, risk concentrations (including by economic sector, geography and currency), asset quality, loan loss provisioning, related party transactions, interest rate risk, and market risk. Appendix 7 of the MORB provides the list of reports to be submitted to the BSP. The following reports are to be submitted on both solo and consolidated basis: Financial Reporting Package The FRP is a set of financial statements for prudential reporting purposes composed of the Balance Sheet, Income Statement and Supporting Schedules. The FRP provides information on a bank's on-and off-balance sheet accounts, profit and loss, liquidity, asset concentrations, asset quality, loan loss provisioning, interest rate risk and market risk, among others. The FRP template is being revised to update the accounts to comply with PFRS 9 *Financial Instruments* although mapping of old accounts with PRFS 9 accounts is provided under Circular No. 1011. S. 175 of the MORB provides the requirements on quarterly publication of financial statements on solo and consolidated basis. There is a policy initiative to amend the guidelines and templates on Published Balance Sheet to disclose a more comprehensive set of indicators of the financial soundness of a bank. The exposure draft is being revised to incorporate the comments received from the industry and Financial Supervision Sector departments. Capital Adequacy Ratio Report S. 125 and Appendix 59 of the MORB set forth the guidelines implementing the revised risk-based capital adequacy framework for the Philippine banking system to implement the Basel III recommendations. The guidelines apply to all universal banks and commercial banks, as well as their subsidiary banks and QBs. S. 125 requires that banks "shall submit a report of their risk-based capital adequacy ratio on a solo basis (head office plus branches) and on a consolidated basis (parent bank plus subsidiary financial allied undertakings, but excluding insurance companies) quarterly to the appropriate supervising department of the BSP in the prescribed forms within the deadlines, i.e., fifteen (15) banking days and thirty (30) banking days after the end of reference quarter, respectively." S. 127 and Appendix 62 of the MORB provide the guidelines implementing the simplified risk-based capital adequacy framework (Basel 1.5) for stand-alone thrift banks, rural banks and cooperative banks, which took effect on 1 January 2012. S. 127 requires such banks to "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., rural banks and Venture Capital Corporations for thrift banks, and rural banks and cooperative banks] quarterly in the prescribed forms within the deadlines, i.e., fifteen (15)

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	banking days and thirty (30) banking days after the end of the reference quarter, respectively. Report on Expanded Real Estate Exposures BSP Memorandum No. M-2012-046 dated September 21, 2012) requires the submission by universal, commercial and thrift banks and their trust departments of an Expanded Report on Real Estate Exposures on a solo and consolidated basis. Such report was enhanced under Circular No. 976 that will require the submission of more granular information on real estate exposures. Liquidity Coverage Ratio (LCR) Report/Minimum Liquidity Ratio (MLR) Report S. 145-A and Appendix 72 of the MORB provide the implementing guidelines of the LCR framework, which is applicable to all universal and commercial banks including branches of foreign banks. Such banks shall report their LCR position for liquidity risk exposures on monthly (solo) and quarterly (consolidated) basis. Pursuant to Circular No. 996, the same LCR requirement was extended to subsidiary banks and QBs of universal and commercial banks on a monitoring basis. See discussion at BCP 24 regarding needed improvements to liquidity risk reporting and management. Leverage Ratio Report S. 129 and Appendix 116 of the MORB provide the implementing guidelines of the Basel III Leverage Ratio Framework. The guidelines shall apply to universal and commercial banks and their subsidiary banks/QBs. S. 129 requires that "…banks shall submit the Basel III Leverage Ratio reporting template, including required disclosure templates, on both solo and consolidated bases for monitoring purposes." Reports on Related Party Transactions (RPT) (solo basis only) There are weekly, twice annual, and other reports on transactions involving bank's directors, officers, stockholders and their related interests and material exposures to related parties. Reports on Large Exposures (solo basis only) Report on Credit and Equity Exposures to Individuals/Companies/Groups aggregating Php 1.0 million and above to be submitted on quarterly basis. FX Position Report (consolidated basis only) The Manual on Foreign Exchange Transactions requires banks to submit their monthly foreign exchange position report on a consolidated basis. ICAAP Document Universal and commercial banks are required to prepare an ICAAP document on a banking group-wide basis to be submitted to BSP annually. Foreign bank branches are also required

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	to prepare an ICAAP document in accordance with the nature, size, and complexity of their business in the Philippines. In the case of D-SIBs, they must submit a recovery plan covering all institutions in the banking group as well as affiliates assessed by the D-SIB as essential to restore, or will have an impact on, the banking group's viability and financial position. The recovery plan shall be integrated in the bank's ICAAP Document. Organizational Structure and Operational Policies S. 173 of the MORB requires banks to submit to the FSS information on bank's profile and any or all of the documents/information on bank's organizational structure and operational policies and any changes therein shall also be reported to the BSP. Appendix 9 of the MORB provides the list of documents/information on organizational structure and operational policies which shall include such other documents/information that may be required from time to time by the supervisory/regulatory department.
EC2	The supervisor provides reporting instructions that clearly describe the accounting standards to be used in preparing supervisory reports. Such standards are based on accounting principles and rules that are widely accepted internationally.
Description and findings re EC2	BSP provides reporting instructions that clearly describe the accounting standards to be used in preparing supervisory reports. While certain adjustments are made for regulatory reports, regulated institutions are required to submit financial statements that are based on accounting principles and rules that are widely accepted internationally. Regulated banks are required to submit information that comprises an FRP. The FRP is a set of financial statements for prudential reporting purposes composed of the Balance Sheet, Income Statement and Supporting Schedules. It provides information on a bank's on-and off-balance sheet accounts, profit and loss, liquidity, asset concentrations, asset quality, loan loss provisioning, interest rate risk and market risk, among others. It is divided into five parts, namely: (1) General Instructions, which describe the overall reporting requirements; (2) Structure of the FRP (3) Revised Manual of Accounts; (4) Line Item Instructions for the Balance Sheet, Income Statement and Supporting Schedules; and (5) Report Formats for solo and consolidated reports which are designed to provide clear guidelines and instructions to banks. The current FRP template is to be revised to implement the recent changes under PFRS 9. The scope of information to be submitted under the FRP varies in relation to the complexity or classification of banks. For universal and commercial banks, the entire FRP report (balance sheet, income statement and all the supporting schedules) is required to be submitted quarterly. For thrift banks, the balance sheet, income statement and the supporting schedules except for derivatives activities are required to be submitted quarterly. For rural and cooperative banks, the simplified FRP report format is required which is also composed of the balance sheet, and income statement but only the supporting schedules which reflect accounts and transactions that are within the generally authorized activities of rural and cooperative banks are submitted.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	The FRP is also submitted on a solo and consolidated basis. Solo basis shall refer to the combined financial statements of the head office and branches/other offices. Consolidated basis shall refer to the combined financial statements of parent bank and subsidiaries consolidated on a line by line basis. Only banks with financial allied subsidiaries, excluding insurance subsidiaries, shall submit the report on consolidated basis. S.172 of the MORB provides that banks shall adopt the PFRS which are in accordance with generally accepted accounting principles in recording transactions and in the preparation of financial statements and reports to BSP. For purposes of prudential reporting to the BSP, banks shall adopt in all respect the PFRS, except in preparing consolidated financial statements and in accounting for ROPA (real estate and other properties acquired). However, the financial audit reports of banks are required to be, in all respect, PFRS compliant.
EC3	The supervisor requires banks to have sound governance structures and control processes for methodologies that produce valuations. The measurement of fair values maximizes the use of relevant and reliable inputs and is consistently applied for risk management and reporting purposes. The valuation framework and control procedures are subject to adequate independent validation and verification, either internally or by an external expert. The supervisor assesses whether the valuation used for regulatory purposes is reliable and prudent. Where the supervisor determines that valuations are not sufficiently prudent, the supervisor requires the bank to make adjustments to its reporting for capital adequacy or regulatory reporting purposes.
Description and findings re EC3	BSP regulations require banks to have sound governance structures and control processes related to valuation. Standards related to the use of internal models is set forth within existing regulations addressing risk factors, and BSP is moving to develop standalone regulations pertaining to model risk management. BSP assesses banks' valuation used for regulatory purposes during on-site examinations. Valuation methodologies and the related assumptions, as well as the results of the external or internal validation are discussed and reviewed during on-site examination. BSP has the authority to adjust valuations and impose higher capital requirements. BSP has recently updated its corporate governance regulations detailing Board responsibilities and, in particular, requiring that Boards establish both an audit and risk oversight committee (Circular No. 969). The Audit Committee is responsible to oversee the financial reporting framework (i.e., financial reporting process, practices, and controls) and to ensure that the reporting framework enables the generation and preparation of accurate and comprehensive information and reports. The Risk Oversight Committee is responsible to oversee the firm's enterprise risk management framework and ensure that there is periodic review of the effectiveness of the risk management systems and recovery plans. Similarly, S. 142 of the MORB requires supervised banks to adopt an effective risk management framework, which includes "…policies, supported by appropriate processes and control procedures, designed to ensure that the risk identification, aggregation, mitigation and monitoring capabilities are commensurate with the bank's size, complexity,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	risk profile, and systemic importance. The risk governance framework shall consider the entities in the conglomerate and shall be applied on a group-wide scale." With respect to financial instruments, Circular No. 1021 was adopted to align existing regulations with the provisions of PFRS 13 on Fair Value Measurement and requires that banks "…shall have adequate governance structures and control processes to ensure that valuations are prudent and reliable for risk management and financial reporting purposes. These processes shall be consistently applied across the institution and integrated within the overall governance framework and risk management systems." With respect to market risk, S. 144 and Appendix 70 of the MORB provide the guidelines on market risk management which include active Board and senior management oversight, market risk measurement models/methodologies, and an effective internal audit and independent validation process. With respect to loan-loss reserves, Circular No. 855 provides that all banks should develop and document a sound loan loss methodology that can reasonably estimate provisions for loans and other credit accommodations and risk assets in a timely manner. Banks are expected to use their experience and research and the guidance under Circular No. 855 to ensure that allowance for credit losses are adequate and approximates the expected losses in the credit portfolio. The detailed guidelines on the use of the expected credit loss model in measuring impairment are provided under Circular No. 1011. With respect to ICAAP, Circular No. 639 on the ICAAP and SRP provides that a bank's ICAAP (i.e., methodologies, assumptions and procedures) and other policies supporting it (e.g., capital policy, risk management policy, etc.) should be formally documented and they should be reviewed and approved by the Board. Regarding external audit review of valuations, Memorandum No. M-2014-011 sets out the expectation for an effective external audit function and provides that the external auditor's scope of audit should include determining whether valuations used by banks are prudent, reliable and consistent. In particular, the external auditor shall evaluate whether the methodologies, assumptions and valuations policies including provisioning for loan losses are appropriate and consistent with the applicable financial reporting framework.
EC4	The supervisor collects and analyses information from banks at a frequency commensurate with the nature of the information requested, and the risk profile and systemic importance of the bank.
Description and findings re EC4	BSP collects information from supervised banks employing multiple regulatory reports. Reports are required at a level of detail and frequency commensurate with the type of bank and activity (universal/commercial/rural/trust/cooperative). S. 173 of the MORB, requires banks to submit periodic reports at varied frequencies (Appendix 7). For example, the Consolidated Daily Report of Condition and Report on Required and Available Reserves on Deposits and Deposit Substitutes are submitted on a weekly basis. LCR position for liquidity risk exposures are submitted on a monthly (solo) and quarterly (consolidated) basis. The FRP (solo) for universal and commercial banks is required monthly while for thrift and rural banks, quarterly. The CAR report is submitted

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	quarterly. Data from the reports submitted by banks are aggregated and analyzed for submission to the MB (e.g., the BSRA is submitted to the Board quarterly). BSP analyses information submitted through its off-site risk profiling framework (SGs No. 2015-01) which requires an assessment of the riskiness of a BSP supervised financial institution using a predetermined set of criteria and applying a 4-risk profile classification/rating (very low, low, lower medium and medium). Information collected is also employed to develop a "Heat Map" which supports the analysis of the level of riskiness of key areas of the industry on a range of 1 to 4 (with 4 as highest) through the application of certain risk measurement criteria covering asset quality, liquidity, profitability, and solvency. Regulatory reports submitted, e.g., the FRP, are relied upon to develop the IO employed to scope and conduct on-site examinations.
EC5	In order to make meaningful comparisons between banks and banking groups, the supervisor collects data from all banks and all relevant entities covered by consolidated supervision on a comparable basis and related to the same dates (stock data) and periods (flow data).
Description and findings re EC5	Reporting requirements established by BCP are supported with filing instructions and definitions, are submitted in standardized forms, employ comparable reporting dates/timeframes, templates and taxonomy, and are subject to a validation process. Data is collected both on a solo and consolidated basis, as appropriate. The information is comparable across similar firms and is employed for peer analysis. BSP may collect data on an ad hoc basis, as needed on topics of concern.
EC6	The supervisor has the power to request and receive any relevant information from banks, as well as any entities in the wider group, irrespective of their activities, where the supervisor believes that it is material to the condition of the bank or banking group, or to the assessment of the risks of the bank or banking group or is needed to support resolution planning. This includes internal management information.
Description and findings re EC6	Under S. 4 of the GBL, BSP has "…supervision over the operations of and exercise regulatory powers over quasi-banks, trust entities and other financial institutions which under special laws are subject to BSP supervision." Under this authority, BSP has the power to request and receive information from supervised banks, its subsidiaries and financial allied affiliates. However, BSP authority does not extend to obtaining information from non-regulated entities in the wider group (except with respect to individual transactions), including those that are engaged in non-banking activities, especially the activities of non-allied affiliates. Bank secrecy laws operate to restrict the availability of information regarding the identity of depositor account holders. S. 23 of the NCBA, as amended, grants authority to the BSP to require from any person or entity, including government offices and instrumentalities, or government-owned or -controlled corporations, "any data": but such authority is constrained to data that is to be used "for statistical and policy development purposes in relation to the proper discharge of its functions and responsibilities", and is explicitly constrained by extant Bank Secrecy Laws

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	("…provided, that the release of disaggregated data gathered shall be subject to prevailing confidentiality laws.") BSP is cognizant of the limitations imposed by these constraints and employs 'work-arounds' to gain some visibility into conglomerate, or 'wider group' information. The BSP employs reporting that requires the submission of a conglomerate 'map' and on reports with information regarding related party transactions and large exposures to gain some insights, but these are not fully satisfactory. In recognition of this gap in information, the sharing of information submitted by entities belonging in a conglomerate is being studied at the Financial Conglomerate Supervision Committee (FCSC) under the auspices of the FSF.
EC7	The supervisor has the power to access [/22] all bank records for the furtherance of supervisory work. The supervisor also has similar access to the bank's Board, management and staff, when required.
Description and findings re EC7	BSP has the power to access supervised bank records to conduct its supervisory work. BSP has open access to the bank's Board, management and staff, when required. However, Bank Secrecy Laws restrict access to information related to depositors. S. 25 of NCBA provides FSS department heads and examiners of FSS with the power to administer oaths to any director, officer or employee of any bank and to compel the presentation of all books, documents, papers or records necessary to ascertain the facts relative to the true condition of any bank, subject to the provisions of laws protecting confidentiality of bank deposits. S. 28 of NCBA provides that the head of appropriate supervising and examining department, personally or by deputy, shall examine the books of every banking institution during regular examination or special examination. The bank concerned shall afford the head of appropriate supervising and examining department and to his authorized deputies' full opportunity to examine its books. Circular No. 957 provides for the conduct of examination, which includes the interview of any bank's directors, officers, and personnel; and the verification, review, and evaluation of documents and records, including making copies of records, taking possession thereof and keeping them under the custody of the BSP after giving proper receipts therefor. The issuance also goes to define and identify what constitutes "records."
EC8	The supervisor has a means of enforcing compliance with the requirement that the information be submitted on a timely and accurate basis. The supervisor determines the appropriate level of the bank's senior management is responsible for the accuracy of supervisory returns, imposes sanctions for misreporting and persistent errors, and requires that inaccurate information be amended.
Description and findings re EC8	BSP has adequate means of enforcing compliance with its reporting and information requirements and acts to ensure that the information is submitted on a timely and accurate basis.

[22/] Please refer to Principle 1, Essential Criterion 5.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC8	The Board (in particular the Audit Committee) and senior management (in particular the Chief Risk Officer, where required) is held responsible for the accuracy of supervisory returns. BSP has the authority to impose sanctions for misreporting and persistent errors, through the implementation of validation and review processes (which includes the tracking of inaccurate or non-responsive submissions) and acts to require that inaccurate information be amended. Appendix 7 of the MORB lists the reports required of banks and the frequency and deadline of submissions. S. 173 of the MORB provides the different categories of reports classified based on prudential importance and the required signatories per category of report. Circular No. 747 on the Revised Compliance Framework for Banks provides, in part, that the Chief Compliance Officer of a bank shall also be responsible for ensuring the integrity and accuracy of all documentary submissions to the BSP. Smaller banks (e.g., rural banks) are allowed to have its compliance officer fulfill requirements imposed upon a Chief Risk Officer at larger institutions. Circular No. 963 on Bank Responsibility for the Generation and Timely Submission of Required Reports to the BSP sets out the BSP's expectation on banks to establish an effective reporting system with an appropriate governance process that enables the generation and timely submission of reports that are in accordance with BSP's reporting standards. Non-compliance with reporting standards could merit monetary penalties and even non-monetary sanction for banks considered as habitual violators. S. 171 of the MORB sets-out the sanctions on reports for non-compliance with reporting standards. It defines the following: a. Erroneous report—A report submitted within the prescribed deadline but is found to be non-compliant with the BSP reporting standards described in S. 171 shall be classified as "Erroneous." Submission of an Erroneous Report shall be considered as willful failure to comply with a regulation. b. Delayed report—A report that was able to comply with the BSP reporting standards after the submission deadline for said report shall be classified as "Delayed". Submission of a compliant report after the submission deadline shall be considered as willful delay in submission of reports. c. Unsubmitted—A report that was not submitted or was submitted but not able to comply with the BSP reporting standards, by the time the next report becomes due or upon the lapse of thirty (30) banking days from the report's submission deadline, whichever comes first shall be classified as "Unsubmitted". Non-submission of reports shall be considered as willful refusal to comply with a regulation. The applicable monetary penalty shall be based on a prescribed fine for each occurrence (in case of Erroneous reports) or for each day (in case of Delayed or Unsubmitted reports)

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC8	which will accumulate until such time the report has been determined compliant with the prescribed reporting standards. A demerit point system is applied for the purpose of determining habituality (repetitive incurrence of reporting violations). When a bank is considered habitual in incurring reporting violations, the BSP shall require the bank to undertake measures to address the root cause/s of the problem. The bank may also be subject to non-monetary sanctions provided under S. 37 of the NCBA, as well as restriction/suspension of branching privileges and other special authorities involving the offering of new products and services to the public. The non-monetary sanctions shall continue to be in effect until the habituality is considered addressed. The habituality is considered addressed and the non-monetary sanctions will be lifted if the bank did not incur any demerit points (i.e., none of the reports of the bank was classified as either Erroneous, Delayed, Erroneous and Delayed, or Unsubmitted) for at least three (3) consecutive months from the time the habituality was observed. Erroneous reports are considered not submitted until the correct/amended reports are submitted to the BSP.
EC9	The supervisor utilizes policies and procedures to determine the validity and integrity of supervisory information. This includes a program for the periodic verification of supervisory returns by means either of the supervisor's own staff or of external experts.[/23]
Description and findings re EC9	BSP has established policies and procedures that require banks to ensure the validity and integrity of supervisory information. Regulatory reports are subject to a validation process and are reviewed upon the development of the IO at the commencement of the examination cycle. External auditors are required to certify that financial reports are accurate and consistent with accounting standards. Circular No. 963 sets forth the BSP's expectation on banks to establish an effective reporting system with an appropriate governance process that enables the generation and timely submission of reports that are in accordance with the BSP's reporting standards. The guideline provides that reports submitted to the BSP must be complete, accurate, consistent, reliable and timely. It is expected that banks have adequate internal controls in place to ensure adherence to the reporting standards. Banks which are not compliant with the reporting standards can be subject to monetary and/or non-monetary sanctions. Further, if the results of the assessment disclose significant deficiencies in the bank's reporting system, the bank shall be required to submit a Board-approved action plan with specified time frame. Non-implementation of the required corrective measures within the specified time frame shall be grounds to subject the bank to the BSP Supervisory Enforcement Policy. Circular Letter No. CL-2018-074 was issued on the updated validation rules used by the BSP to determine whether the entries in the FRP are either balanced and reconciled or cited with mathematical defects requiring correction and the submission of amendments that are subject to penalty. A User Guide explains and describes the validation process.

[23/] Maybe external auditors or other qualified external parties, commissioned with an appropriate mandate, and subject to appropriate confidentiality restrictions.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC10	The supervisor clearly defines and documents the roles and responsibilities of external experts,[/24] including the scope of the work, when they are appointed to conduct supervisory tasks. The supervisor assesses the suitability of experts for the designated task(s) and the quality of the work and takes into consideration conflicts of interest that could influence the output/recommendations by external experts. External experts may be utilized for routine validation or to examine specific aspects of banks' operations.
Description and findings re EC10	To date, the BSP has not appointed external experts, such as external auditors, to conduct supervisory tasks or to examine specific aspects of bank's operations. BSP may require supervised institutions to employ external experts. S. 58 of the GBL provides that the MB may require a bank to engage the services of an independent auditor to be chosen by the bank from a list of external auditors acceptable to the MB. The terms of engagement shall be as prescribed by the MB which may either be on a continuing basis where the auditor shall act as resident examiner or on the basis of special engagements.
EC11	The supervisor requires that external experts bring to its attention promptly any material shortcomings identified during the course of any work undertaken by them for supervisory purposes.
Description and findings re EC11	To date, the BSP has not appointed external experts such as external auditors to conduct supervisory tasks or to examine specific aspects of bank's operations.
EC12	The supervisor has a process in place to periodically review the information collected to determine that it satisfies a supervisory need.
Description and findings re EC12	BSP has revised its data collection when there is a new/revised prudential standard, in response to supervisory needs or risks observed, to allow for the domestic application of revised international standards or to align requirements across regulated industries where needed. BSP has modified, and is presently working to modify, required prudential reports. For example, in 2013, a task force was formed to rationalize the reports submitted to the DSA, International Operations Department and Department of Economic Statistics; hence, certain reports were revised and discontinued as provided under Circular No. 846. A second review of reports submitted to BSP has been started in 2018.
Assessment re Principle 10	Compliant
Comments	BSP has an effective set of reporting requirements to view and analyze prudential reports on a solo and consolidated basis. BSP has adequate power to require and receives reports from supervised firms regarding financial condition, performance and risks. BSP regulations require banks to demonstrate effective governance and internal controls, including valuations, and has effectively review banks' governance and internal control processes, acting in relevant instances to challenge banks' valuation methodologies and assumptions. BSP has been inhibited from requiring submission of all relevant information from the wider banking group, given the restrictions on its supervisory remit. BSP has employed its available bank reporting requirements and information sources in order to gain a view regarding materiality of group activities in relation to the bank and banking group and it should continue to enhance its methodology and approaches to assessing risks posed by the wider group, including obtaining necessary information to support resolution planning and resolvability analysis.

[24/] Maybe external auditors or other qualified external parties, commissioned with an appropriate mandate, and subject to appropriate confidentiality restrictions. External experts may conduct reviews used by the supervisor, yet it is ultimately the supervisor that must be satisfied with the results of the reviews conducted by such external experts.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Principle 11	**Corrective and sanctioning powers of supervisors**. The supervisor acts at an early stage to address unsafe and unsound practices or activities that could pose risks to banks or to the banking system. The supervisor has at its disposal an adequate range of supervisory tools to bring about timely corrective actions. This includes the ability to revoke the banking license or to recommend its revocation.
Essential criteria	
EC1	The supervisor raises supervisory concerns with the bank's management or, where appropriate, the bank's Board, at an early stage, and requires that these concerns be addressed in a timely manner. Where the supervisor requires the bank to take significant corrective actions, these are addressed in a written document to the bank's Board. The supervisor requires the bank to submit regular written progress reports and checks that corrective actions are completed satisfactorily. The supervisor follows through conclusively and in a timely manner on matters that are identified.
Description and findings re EC1	Supervisory concerns are raised with bank management primarily by issuance and delivery of the ROE upon completion of the annual examination. Examinations have been conducted every 12–14 months; however, with the recent passage of the NCBA, BSP is no longer compelled to examine every supervised institution annually; that requirement has now been moderated to allow BSP to schedule examinations employing a risk-based approach; for example, scheduling rural bank examinations on a greater than annual basis. Off-site monitoring can trigger supervisory actions prior to the conduct of the scheduled annual examination. For example, a violation of regulatory thresholds will result in outreach to bank management. In addition, identified emerging risks (e.g., related-party transactions; anti-money laundering) have driven the conduct of special examinations (which must be approved by the MB). Prior to the formal issuance of the ROE, the examination team communicates on-site issues/concerns noted and obtains bank management's commitment and timelines in addressing such during soft and final exit conferences. FSD also conducts post-examination meetings with the Board prior to release of the ROE. The ROE specifies corrective actions that need to be performed. The ROE is provided to the Board and a written response including a plan of remediation is required. Supervisory concerns noted during on-site examinations which require attention from a supervised institution's Board or management are categorized into three groups, namely, (1) required actions; (2) expected actions; and (3) observations. BSP has issued guidelines to examiners in order to support uniform use of supervisory directives. This is documented under SG 2008-28 (Guidelines on the Standardized Terminology for Communicating Examination Findings and Recommendations. Each grouping has (1) appropriate timeframes, (2) expectations regarding the FI's response, and (3) supervisory follow-throughs. When corrective actions have not been taken, BSP has the ability to escalate issues by requiring formal LOC, issuance of CDOs. Banks with material weaknesses/deficiencies requiring significant corrective actions, these banks are initiated into the PCA Framework, subject to MB approval.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC2	The supervisor has available [25] an appropriate range of supervisory tools for use when, in the supervisor's judgment, a bank is not complying with laws, regulations or supervisory actions, is engaged in unsafe or unsound practices or in activities that could pose risks to the bank or the banking system, or when the interests of depositors are otherwise threatened.
Description and findings re EC2	The Supervisory Enforcement Policy (S. 002 of the MORB) provides a menu of the enforcement actions and supervisory tools available to the BSP as contained in various laws, rules and regulations. SGs providing internal guidance on the implementation of the enforcement policy have been issued (SG No. 2016-09). Refer to EC 4 for additional information regarding enforcement actions and supervisory tools. BSP conceives that the available supervisory tools are deployed in accordance to how they fit into five-phases of supervisory oversight, which seek an increasing intensity as the severity of the problems identified at supervised institutions. Not every phase need be exhausted prior to escalation and severe supervisory responses can be triggered promptly, especially in cases that pose risks to solvency of the bank, the banking system, or to depositors. This continuum is described as follows: (i) Normal Supervision approach—normal degree of supervision consisting of regular on-site examination and off-site monitoring/surveillance; addressing minor problems/weaknesses/deficiencies and compliance lapses; (ii) Enhanced Supervision approach—deployment of escalating enforcement actions to address emerging supervisory concerns before they develop into major problems or remaining unresolved supervisory issues and concerns so as not to relapse to a state of heightened state of risk; (iii) PCA Framework—involves directing the Board of directors of a supervised institution with higher-than-normal risk of failure, to institute measures to restore it to normal operating condition within a reasonable period; (iv) BRes approach—more intrusive supervisory approach for institutions with critically serious problems and persistent uncorrected violations that are unlikely to be addressed in the near term; and (v) Intervention and Resolution—final phase of supervision ending with the appointment of the PDIC as receiver. An integral part of the deployment of enforcement actions is the observance of due process in all cases, allowing bank management an opportunity to respond and submit information or plans intended to dispute or address the corrective action. The institution and/or its directors and officers are afforded fair and reasonable opportunity to explain their side and to submit evidence in support thereof, which are given due consideration in determining the appropriate enforcement action(s) to be imposed.
EC3	The supervisor has the power to act where a bank falls below established regulatory threshold requirements, including prescribed regulatory ratios or measurements. The supervisor also has the power to intervene at an early stage to require a bank to take action to prevent it from reaching its regulatory threshold requirements. The supervisor has a range of options to address such scenarios.

[25] Please refer to Principle 1.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	BSP has the power to act where a bank falls below regulatory thresholds, including regulatory minima and ratios established for capital, liquidity (LCR and NSFR), real estate exposures, and the violation of supervisory limits (e.g., single borrower's and related party transaction limits). BSP relies primarily on the conduct of periodic (e.g., annual or greater) on-site examinations to discover violations. Reports are received regarding compliance with ratios on a periodic (e.g., monthly or quarterly basis) which can drive a supervisory response. The BSP has raised concern whenever the CAR of a bank (i.e., stand-alone thrift, rural and cooperative banks) barely meets the minimum regulatory requirement, by requiring the bank to submit a plan of action to improve capital position with specific timelines. D-SIBs are required, pursuant to Circular No. 904, to prepare and submit recovery plans, that incorporate capital and liquidity-based triggers requiring activation of recovery options prior to the violation of a regulatory threshold. Recovery plans reviewed afford some degree of early warning, with recovery plans being activated, for example, when a bank breaches its regulatory capital level, plus a management buffer of 100 bps. BSP is to be notified of a bank's activation of recovery plans; albeit such has not occurred. Refer also to EC 4.
EC4	The supervisor has available a broad range of possible measures to address, at an early stage, such scenarios as described in essential criterion 2 above. These measures include the ability to require a bank to take timely corrective action or to impose sanctions expeditiously. In practice, the range of measures is applied in accordance with the gravity of a situation. The supervisor provides clear prudential objectives or sets out the actions to be taken, which may include restricting the current activities of the bank, imposing more stringent prudential limits and requirements, withholding approval of new activities or acquisitions, restricting or suspending payments to shareholders or share repurchases, restricting asset transfers, barring individuals from the banking sector, replacing or restricting the powers of managers, Board members or controlling owners, facilitating a takeover by or merger with a healthier institution, providing for the interim management of the bank, and revoking or recommending the revocation of the banking license.
Description and findings re EC4	BSP possesses a broad range of measures to address supervisory concerns. The measures afford BSP the ability to require a bank to take timely corrective action or to impose sanctions expeditiously. The supervisory directives or orders are clear and set out objectives or actions to be taken by supervised institutions. BSP escalates matters via a 'supervisory continuum' and applies more severe supervisory tools relative to the issue to be addressed and to compel compliance. BSP supervisory enforcement policies incorporate principles of due process, allowing financial institutions an opportunity to respond to charges and be heard. Due process requirements can generate delay in enforcement, but BSP maintains authority to take immediate action in severe circumstances. BSP regularly issues supervisory directives upon completion and delivery of the ROE. BSP employs the following form of supervisory directives:

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	1. Required Actions constitute the highest priority in supervisory matters. Written communication to the bank on required actions specifies a timeframe in which the action must be completed. The timeframe for addressing required actions is generally short, may be "immediate," but is almost always within 30 to 90 days. 2. Expected Actions require lesser priority than Required Actions. Written communications specify a timeframe in which actions are expected, although the timeframe (at least initially), may require estimation. For required and expected actions, the institution is expected to provide the BSP with a written response regarding the plan for, progress, and/or achievement of the expected action. 3. Observations constitute supervisors' insight about sound industry practices that, if adopted, are seen to improve the efficiency and effectiveness of the bank. Supervisors raise these observations less formally, most of the times, verbally, in meetings and conferences. Failure to comply with supervisory directives can be escalated, and formal enforcement actions taken. The main categories of enforcement action are the following: a) Corrective actions include the following: 1. BSP Directives—orders and instructions requiring specific actions or to refrain from activities within a prescribed timeline. 2. LOC—a formal enforcement action where the Board is required, upon approval and/or confirmation by the MB to execute a written commitment to undertake a specific positive action or refrain from performing an activity within a given time period. b) Sanctions—sanctions are subject to the prior approval and/or confirmation by the MB. Such sanctions include the following: 1. Supervised Banks a. Restrictions on Activities and Privileges b. Suspension of Authorities, Privileges and Other Activities c. Divestment and/or Unwinding d. Monetary Sanction—Penalties/Fines Against the bank 2. Directors and Officers a. Reprimand b. Restriction on Compensation and Benefits c. Divestment d. Suspension e. Disqualification f. Removal g. Monetary Penalties/Fines c) Other Supervisory Actions—subject to prior MB approval, the BSP, when warranted, may deploy other supervisory actions, such as (i) initiation into the PCA Framework; (ii) issuance of a cease and desist order against the institution as well as its directors

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	and officers; (iii) conservatorship; and (iv) prohibiting the bank from doing business in the Philippines and appointing the PDIC as receiver. <u>Prompt Corrective Action Framework</u> A supervised institution is placed into the PCA Framework (S. 4.6 of the GBL and S. 003 of the MORB) under any or all of the following conditions: 1. When either of the Total Risk-Based Ratio (otherwise known as CAR), Tier 1 Risk-Based Ratio, or Leverage Ratio (Total Capital/Total Assets) falls below 10 percent, 6 percent and 5 percent, respectively, or such other minimum levels that may be prescribed for the said ratios under relevant regulations, and/or the combined capital account falls below the minimum capital requirement prescribed under BSP regulations; 2. The Capital Adequacy, Asset Quality, Management, Earnings, Liquidity and Sensitivity to Market Risk ("CAMELS") composite rating is less than "3" or a Management component rating of less than "3"; 3. A serious supervisory concern has been identified that places a bank at more-than-normal risk of failure in the opinion of the Director of the examination department concerned, which opinion is confirmed by the MB. Such concerns could include, but are not limited, to any one or a combination of the following; a) Finding of unsafe and unsound activities that could adversely affect the interest of depositors and/or creditors (see BSP Circular No. 341 as amended by BSP Circular No. 640; b) A finding of repeat violations of law or the continuing failure to comply with MB Directives; and, c) Significant reporting errors that materially misrepresent the bank's financial condition. Sanctions may be imposed on any bank subject to PCA whenever there is unreasonable delay in entering into a PCA plan or when PCA is not being complied with. These may include any or all of the following: 1. monetary penalty on or curtailment or suspension of privileges enjoyed by the Board or responsible officers; 2. restriction on existing activities that the supervised financial institution may undertake; 3. denial of application for branching and other special authorities; 4. denial or restriction of access to BSP credit facilities; and, 5. restriction on declaration of dividends. Banks initiated into the PCA Framework are required to execute an MOU, which is a bilateral agreement between the bank and BSP and implement the same using a PCA Plan (PCAP), containing measures to restore the entity to normal operating condition within a reasonable period. Said MOU and the PCAP have for their components a Capital Restoration Plan, Business Improvement Plan and Corporate Governance Reform. Submission of the MOU and the PCAP, as well as the attainment of the commitments therein, are to be covered by prescribed timelines. SG No. 2016-03 on the Enhanced Internal Policies and Procedures on Handling Banks Initiated to the PCA Framework provides for the basic/standard provisions of the MOU.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	Cease and Desist Orders S. 37 of the NCBA provides that if the bank and/or the directors and/or officers concerned continue with or otherwise persist in the commission of the indicated unsafe/unsound banking activity or violation, the MB may issue an order requiring the institution and/or the directors and/or officers concerned to cease and desist from the indicated practice or violation, and may further order that immediate action be taken to correct the conditions resulting from such practice or violation. The cease and desist order shall be immediately effective upon service on the respondents. The respondents shall be afforded an opportunity to defend their action in a hearing before the MB or any committee chaired by any MB member created for the purpose, upon request made by the respondents within five days from their receipt of the order. If no such hearing is requested within said period, the order shall be final. If a hearing is conducted, all issues shall be determined based on records, after which the MB may either reconsider or make final its order. Banks for Resolution (BRes) Banks are placed into a BRes status should they not meet the requirements/conditions in the PCA MOU, reflect severe deficiencies in capital, poor operating performance and/or critically deficient liquidity, poor corporate governance and significant weaknesses in business processes and risk management, which are unlikely to be addressed in the near term (i.e., one year or less). Generally, BRes status includes banks declared as PCA failure or candidates for PCA failure. Closure and appointment of PDIC as Receiver S. 30 of the NCBA and S. 53 of the GBL lay the grounds for prohibiting a bank/QB from doing business. Determination of the existence of any of the grounds under S. 30 of the NCBA can be based on a report of the appropriate supervising and examining department of the BSP which may recommend to the MB the prohibition of the institution from doing business. The report can be based on an on-site examination conducted, either solely by the BSP or jointly with the PDIC. The process to prohibit an institution from doing business is set forth in the Prohibition QMS issued June 11, 2018. It provides for the following: 1. Public announcement of bank holiday or suspension of the payments of its deposit liabilities for more than 30 days; 2. Bank run; 3. Result of regular/special/overseeing examination; and 4. Expiration of corporate life. The BSP tracks and monitors LOCs and PCA/BRes status. No tracking mechanism was provided with respect to Directives (required or expected actions). Compliance with directives is primarily achieved during annual on-site reviews. BSP does not maintain a monitoring system that demonstrates the 'lifecycle' of a supervisory issue from directive to LOC and throughout the supervisory 'continuum.' No aging report is available in order to

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	monitor and flag supervisory directives that are not concluded within or in comparison to initial expected remediation dates. Applying the supervisory 'continuum' concept, BSP elevates directives that have not been complied with to require LOCs. LOCs can be amended and, in meritorious cases, be extended subject to defined conditions. PCA and the BRes Framework sits at the end of the supervisory continuum and are intended to bring a supervisory focus on firms that are at risk of failure and, by execution of a PCA MOA, compel prompt remediation of the firm and restoration to financial stability. The BRes Framework is intended primarily to facilitate a merger, acquisition or capital injection. In practice, banks placed into PCA can linger in such status for prolonged periods (years), during which time the firms can remain capital deficient. The PCA framework has not operated effectively to require firms to be placed into resolution at an early stage, and before equity has been exhausted. Escalation of PCA enforcement actions is not clearly tied by law or regulation to stages of decline in regulatory capital levels, and resolution/receivership has not been imposed even where bank owners have demonstrated an inability or unwillingness to recapitalize the firm unless grounds under Sec. 30 of the NCBA, as amended, exist. Institutions that have been closed (forbidden to do business) and for which the PDIC has been appointed receiver have been in a state of negative equity, thus imposing losses upon the deposit insurance fund that could have been avoided or mitigated should prompt action have been taken. Not acting quickly to address and correct significant supervisory concerns, allowing firms to operate with deficient capital and management, with imprudent bank management continuing to operate the institution, encourages moral hazard risks, exposes the deposit insurance fund to loss and can threaten public confidence in the regulatory system. The grounds for prohibition of banks from doing business in the Philippines and appointment of PDIC as receiver to proceed with liquidation of closed banks are provided for in Section 30 of the NCBA. The presence of any of the grounds mentioned is sufficient legal basis to order closure of a bank, are not tied to capital levels and do not mandate that a bank reach a state of negative equity before the bank can be closed. BSP reports instances when closure of banks with positive capital has been ordered in view of presence of ground for closure. Recognizing that banks initiated into the PCA in previous years are observed to linger in their PCA status, FSS conducted in 2014 a reassessment of the portfolio of PCA banks, with the aim of appropriately classifying banks in accordance and consistent with the BSP Enhanced Supervisory Enforcement Regime. The BSP also revisited its PCA framework and issued in 2016 the Enhanced Internal Policies and Procedures in Handling Banks Initiated into the PCA Framework (SG No. 2016-03 dated 10 February 2016). Implementation of PCA was likewise strengthened with the introduction of the PCA QMS to ensure that PCA timelines are observed. Unlike in the banks initiated into PCA from years 2006 to 2014, where the average time period to resolution of PCA status (i.e., closed, declared failure, transitioned to enhanced supervision or lifted to normal supervision) spanned 4.64 years, BSP reports recent

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	improvement in the timelines for banks initiated into PCA from 2015 to present; where the average period to resolution of PCA status is 2.14 years from PCA initiation. Strengthening of internal guidelines on receivership/prohibition from doing business of banks is in process. And, aside from PCA, initiatives, BSP has revisited its LOC Framework and a corresponding SG is under review. BSP is encouraged to continue ongoing revisions to the PCA framework and implement policies and procedures that will operate to ensure that firms placed into PCA status are addressed in a timely fashion, that constrain any undue regulatory forbearance, and place firms into resolution in a prompt and timely fashion.
EC5	The supervisor applies sanctions not only to the bank but, when and if necessary, also to management and/or the Board, or individuals therein.
Description and findings re EC5	BSP has the authority to apply sanctions not only to the bank but also to management and/or the Board, or individuals therein. BSP has applied sanctions to both firms, management and its Board members. S. 37 of the NCBA provides the administrative sanctions on banks and quasi-banks, their directors and/or officers, for any willful violation of any banking law, regulation, or instruction issued by the MB or the Governor, and/or conducting business in an unsafe or unsound manner, among other infractions. The administrative sanctions include fines, suspension of rediscounting privileges, among other sanctions. The MB may, whenever warranted by circumstances, preventively suspend any director or officer of a bank or quasi-bank pending an investigation. S. 003 of the MORB on supervisory enforcement policy also provides sanctions that may be imposed on bank's directors and officers, as provided under existing laws, the BSP rules and regulations, subject to prior MB approval and/or confirmation by the MB. Such sanctions include: reprimand, restriction on compensation and benefits, divestment, suspension, disqualification and removal. Such sanctions are without prejudice to the filing of separate civil or criminal actions against them, when appropriate. Regulations also apply enforcement actions to directors and/or officers concerned in addition to the bank itself, such as on violation of directors, officers, stockholders and related interests (DOSRI) regulations. The BSP also adopted a Sanctions QMS which define the criteria for the evaluation/imposition of sanctions. There are cases wherein the BSP has imposed sanctions, issued warning letters or reprimand to directors or senior officers of certain banks.
EC6	The supervisor has the power to take corrective actions, including ring-fencing of the bank from the actions of parent companies, subsidiaries, parallel-owned banking structures and other related entities in matters that could impair the safety and soundness of the bank or the banking system.
Description and findings re EC6	BSP possesses adequate authority and supervisory tools to restrict supervised institutions' activities in order to protect the safety and soundness of the bank by, for example,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	restricting capital flows, activities, rejecting mergers or acquisitions, or imposing funding or liquidity restrictions. However, the ability to fully protect the bank from the actions of parent companies and affiliates is impaired because such entities fall outside of its regulatory perimeter and direct action against non-regulated entities within the conglomerate group cannot be taken. The available information on conglomerate structure is not fully satisfactory, only updated annually, and there is no requirement that the bank or banking group provide a comprehensive and current view of the group-wide risk concentrations and inter-dependencies. In addition, BSP does not conduct a comprehensive resolvability assessment and resolution plans are not developed. Adequate information on inter-connections and dependencies between the bank and the wider group entities is important to inform BSP decision-making regarding 'ring-fence' actions that may be practical and effective, avoid interruption to critical functions, and mitigate potential systemic impacts. These weaknesses result in BSP not possessing a comprehensive view of the protective actions that would be necessary or appropriate to 'ring-fence' the bank while ensuring that critical economic functions of systemic importance to the financial system are maintained. BSP intends to issue guidelines regarding its supervisory approach to ring-fence the bank from the actions of parent companies, subsidiaries, and other related companies in matters that could impair the safety and soundness of the bank. Refer to CP 8 and related discussion of resolvability assessments.
EC7	The supervisor cooperates and collaborates with relevant authorities in deciding when and how to effect the orderly resolution of a problem bank situation (which could include closure, or assisting in restructuring, or merger with a stronger institution).
Description and findings re EC7	BSP possesses the authority to appoint PDIC as receiver. Under S. 30 of NCBA, a bank or QB which has willfully violated a CDO that has become final, involving acts or transactions which amount to fraud or a dissipation of the assets of the institution; in which cases, the MB may summarily and without need for prior hearing forbid the institution from doing business in the Philippines and designate the PDIC as receiver in the case of banks and direct the PDIC to proceed with the liquidation. Pursuant to a BSP-PDIC MOA and the PDIC Charter, BSP and PDIC co-ordinate on the conduct of joint examinations in order to assess the condition and operations of institutions that are to be placed into receivership. In practice, the joint preparation and communication has been restricted to banks that are placed in the BRes framework and include mainly rural banks and smaller banking operations. While in the BRes status, BSP (with engagement of PDIC) will seek to facilitate a restructuring, merger or acquisition; although it does not possess authority to compel shareholder actions in that regard. PDIC and BSP meet on a regular basis to review the current list of institutions that are placed in either PCA or BRes status. Through these regular meetings, the timing of eventual appointment of PDIC and closure of the institution is coordinated. However, no regular planning has taken place relative to preparing for the potential resolution of other firms, especially D-SIBs. No resolvability analysis nor resolution plan has been developed for D-SIBS.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC7	Given application of the Bank Secrecy Laws, PDIC is prohibited from obtaining depositor information on open institutions, except where a determination has been made that the firm is unsafe and unsound. PDIC has not exercised this potential authority to access depositor information and prepare for resolution. BSP has ongoing working groups to address the following areas of cooperation between the BSP and PDIC: a) Memorandum of Agreement on Information Exchange including sharing of bank reports and related logistics (for revision); b) MOA on Bank Examination (for revision); and c) Unsafe and/or Unsound Practices and related Enforcement Actions such as Cease and Desist Order (CDO) and Directive to Cease and Desist (DCD). In addition, BSP participates in a Technical Working Group on Harmonization of Merger, Consolidation and Acquisition Evaluation (MCA) involving different government agencies (BSP, PDIC, SEC, CDA and PCC). This working group seeks to simplify the requirements and shorten the processing period for MCA proposals of banks, among other objectives. BSP is encouraged to continue to work with PDIC to establish effective coordination mechanisms to ensure that, where appropriate grounds exist, firms are placed into resolution in a prompt and timely fashion.
Assessment re Principle 11	Largely Compliant
Comments	While BSP has an appropriate set of supervisory tools, including an ability to revoke the banking license, the timeframes within which the remediation of identified supervisory issues is concluded or resolved can be extensive. Banks placed into PCA can linger in such status for prolonged periods (years), during which time the banks can remain capital deficient. The PCA framework has not operated in all instances to effectively require firms to be placed into resolution at an early stage, and before equity has been exhausted. BSP has generated improvements in the prompt and timely remediation of PCA status, but more needs to be done. The ability to fully protect the bank from the actions of parent companies and affiliates is impaired because such entities fall outside of its regulatory perimeter, and direct action against non-regulated entities within the conglomerate group cannot be taken. The available information on conglomerate structure is only updated periodically, and there is no requirement that the bank or banking group provide a comprehensive and current view of the group-wide risk concentrations and inter-dependencies. Adequate information on inter-connections and dependencies between the bank and the wider group entities is important to inform BSP decision-making regarding 'ring-fence' actions that may be practical and effective, avoid interruption to critical functions, and mitigate potential systemic impacts. In addition, BSP does not conduct a comprehensive resolvability assessment and resolution plans are not developed, in conjunction with PDIC. These weaknesses result in BSP not possessing a comprehensive view of the protective actions that would be necessary or appropriate to 'ring-fence' the bank while ensuring that critical economic functions of systemic importance to the financial system are maintained.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	Recommendations: • BSP is encouraged to continue ongoing revisions to the PCA framework and implement policies and procedures that will operate to ensure that firms placed into PCA status are addressed in a timely fashion and place firms into resolution in a prompt and timely fashion. • BSP is encouraged to continue to work with PDIC to establish effective coordination mechanisms to ensure that, where appropriate grounds exist, firms are placed into resolution in a prompt and timely fashion. • Develop and implement policies and standards regarding the supervisory approach to ring-fence the bank from the actions of parent companies, subsidiaries, and other related companies in matters that could impair the safety and soundness of the bank. Refer to recommendations under CP 1, related to seeking changes to laws or regulations to empower BSP to obtain adequate information and exercise power to fully protect the bank from the actions of parent companies and affiliates. • Refer to recommendations under CP 8 related to the conduct of resolvability assessments, in conjunction with PDIC.
Principle 12	**Consolidated supervision**. An essential element of banking supervision is that the supervisor supervises the banking group on a consolidated basis, adequately monitoring and, as appropriate, applying prudential standards to all aspects of the business conducted by the banking group worldwide.[26/]
Essential criteria	
EC1	The supervisor understands the overall structure of the banking group and is familiar with all the material activities (including non-banking activities) conducted by entities in the wider group, both domestic and cross-border. The supervisor understands and assesses how group-wide risks are managed and takes action when risks arising from the banking group and other entities in the wider group, in particular contagion and reputation risks, may jeopardize the safety and soundness of the bank and the banking system.
Description and findings re EC1	<u>Consolidated supervision of a banking group</u> The BSP's powers to conduct consolidated supervision are provided in S. 7 of the GBL, which states that the BSP shall have the authority to examine an enterprise which is wholly or majority-owned or controlled by the bank. In addition, S. 25 of RA No. 11211 provides the BSP with the power to "conduct regular or special examinations of banking institutions and quasi-banks, including their subsidiaries and affiliates engaged in allied activities." S. 341 of the MORB provides the definitions of subsidiaries and affiliates. A subsidiary refers to a corporation or firm of which more than fifty percent of the outstanding voting stock is directly or indirectly owned, controlled or held with power to vote by its parent corporation. An affiliate refers to an entity linked, directly or indirectly, to a bank based on the conditions provided by that section.

[26/] Please refer to footnote 11 under Principle 1.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	S. 131 of the MORB further provides that "control" shall exist when there is: a. Power over more than one-half of the voting rights by virtue of an agreement with other stockholders; or b. Power to govern the financial and operating policies of the enterprise under a statute or an agreement; or c. Power to appoint or remove the majority of the members of the Board of directors or equivalent governing body; or d. Power to cast the majority votes at meetings of the Board of directors or equivalent governing body; or e. Any other arrangement similar to any of the above. BCP7 EC1 sets out the requirements of S. 372 and 375 of the MORB, which set out the financial and non-financial allied undertakings in which universal, commercial and thrift banks may invest. Circular No.781 sets out the BSP's approach to consolidation for regulatory purposes. All BSP regulated entities are in the consolidated banking group. Financial institutions under the supervision of IC and the SEC are part of the banking group in most conglomerates, but not all. The CAR requirement is applied to all universal and commercial banks and their subsidiary banks, and QBs on both solo and consolidated [/27] bases. All banking and other relevant financial activities (both regulated and unregulated) conducted by a bank and its subsidiaries will be captured through the consolidation. Majority-owned or majority-controlled financial allied undertakings are fully consolidated on a line-by-line basis. Any exemptions from consolidation have to be pre-approved by the BSP. The BSP's risk-based framework requires supervisors to assign an appropriate CAMELS rating to the lead bank in a consolidated group and all affiliated financial institutions. To perform an effective consolidated analysis, the supervisor has cause to obtain all relevant information from the bank and its affiliates, and to verify transactions flowing between the bank and those affiliates. Banks subject to consolidated supervision are required to report quarterly on their consolidated CAR, liquidity ratios and related party transactions (RPTs)—see BCP 20. Consolidated information on large exposure (LE) and single borrower is not currently collected, but planned revisions to the LE framework will address this issue—see BCP 19. A full set of reporting requirements for banks subject to consolidated supervision is set out in EC2. The off-site consolidated reports inform the scope of on-site examinations, which involve detailed review of related party and other transactions with the wider group to ensure they have been conducted on arm's length terms. ______________________ [27/] Pertains to the reporting entity and its financial allied subsidiaries except insurance companies that are required to be consolidated on a line-by-line basis for the purpose of preparing consolidated financial statements.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	An important element of the BSP's consolidated supervision of banking groups is effective liaison with other domestic regulators. The BSP has signed MOAs with the SEC and the IC, which are the primary domestic regulators of nonbank financial subsidiaries and affiliates of banks. [See BCP3]. The MOAs enable the BSP to share information on the financial condition and the adequacy of the risk management systems and controls of other regulated entities within the consolidated banking group. The BSP's on- and off-site supervisory regime adequately assesses the adequacy of a bank's consolidated group capital and liquidity positions and ensures that RPTs are conducted on an arms-length basis. Concentration risk is not captured adequately because the SBL is not currently applied at the consolidated group level, but revisions to the LE framework will address this issue. <u>Supervision of conglomerate groups</u> The majority of BSP designated D-SIBs are incorporated within a conglomerate structure that includes non-regulated parent companies and affiliates engaged in non-banking activities. There is no provision in existing laws to allow the BSP to acquire information from non-allied affiliates or permit examination of the operations of these firms. The BSP is also constrained from obtaining information from parent companies or entities—see BCP1 EC7. This impedes the BSP's ability to fully determine the impact of such non-regulated entities upon the safety and soundness of the banking group, or to provide supervisory oversight and control over significant inter-dependencies. BSP is cognizant of these restrictions and the need to assess risks posed by the wider group. The BSP's recourse to the parent company and affiliates is through the regulated bank. The BSP can indirectly look into the transactions of a bank's parent (upstream relationship) and other affiliate companies that are not supervised by the BSP, if those companies have transactions with regulated banks. As all transactions with banks are required to be supported with necessary documentation, the BSP can indirectly look at the activities of a bank's parent companies during the examination of banks which have provided loans to the parent. In addition, an off-site review of the activities of the entities that are within the wider group is conducted through the use of publicly available information. Circular No. 895 requires all banks that are part of conglomerates to submit an annual report to the BSP on their conglomerate structure, listing all entities within that structure. A bank within a conglomerate structure is also required to disclose any beneficial owners of shareholdings that are in the name of PCD Nominee Corporation. Supervisors review gearing levels in companies in the wider group through public accounts and, through liaison with the SEC under the auspices of the FSF, establish whether double gearing concerns may present contagion risk to the regulatory consolidated group. All direct lending to companies in the wider group, and to related parties of those companies, are captured in the RPT returns of the regulated bank and assessed on-site to ensure the terms of the loans are at arm's length. Circular No. 895 requires banks' RPT policies to capture a broader spectrum of transactions, covering not only those that give

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	rise to credit and/or counterparty risks but also those that could pose material/special risk or potential abuse to the bank and its stakeholders. This allows BSP examiners to determine the nature of activities undertaken by the bank's parent company aside from those activities financed by borrowings from the bank. On a periodic basis, BSP aggregates available information related to concentrations of credit risk to entities with conglomerate groups, and has stress tested such exposures (employing an estimated non-performing loan shock). Working groups have been established within the FSCC in order to gather information on the amount of leverage displayed by large corporate groups. Recent amendments to the NCBA also allow the BSP to gather information from any person or entity, which would extend to any member of the conglomerate group, but such authority is limited to 'statistical and policy' purposes and, while such an authority may be adequate to gather broader information, it has yet to be employed or tested. The BSP should make full use of this power. BSP should continue to augment its analysis and assessment of conglomerate groups, and enhance the quality and frequency of available information, in order to bring analysis of unregulated entities and activities and the risks they pose to regulated entities into its regular supervisory process. Regulated banks and other entities should be required to demonstrate a comprehensive risk management framework to manage and report group-wide risk concentrations and intra-group transactions and exposures in their ICAAP. BSP should be guided by the Joint Forum's "Principles for the supervision of financial conglomerates" (September 2012) tailored for the unique aspects and complexities of the Philippines banking system and operating environment.
EC2	The supervisor imposes prudential standards and collects and analyses financial and other information on a consolidated basis for the banking group, covering areas such as capital adequacy, liquidity, large exposures, exposures to related parties, lending limits and group structure.
Description and findings re EC2	Banking groups subject to the BSP's consolidation rules are required to comply with the following regulations and to submit the corresponding reports on a consolidated basis: *Published Balance Sheet* • S. 61 of RA 8791 provides that every bank, quasi-bank or trust entity shall publish a statement of its financial condition (i.e., balance sheet and consolidated balance sheet), including those of its subsidiaries and affiliates at least quarterly or in such frequency as may be prescribed by the BSP. *Financial Reporting Package* • S. 172 of the MORB requires banks and their subsidiaries and affiliates to prepare an FRP in accordance with PFRS and Philippine Accounting Standards (PAS). See BCP 10 EC2 for details of the content of the FRP. *Audited Financial Statements* • S. 173 of the MORB requires universal and commercial banks to submit a Report on Consolidated Financial Statements of Banks and their Subsidiaries Engaged in Allied Financial Undertakings together with individual audited financial statements of such subsidiaries.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	*Annual Report* • Circular 956 sets out guidelines on the submission of the Annual Report of Banks. The circular provides the minimum disclosure requirements in the annual report. These should cover all significant matters regarding the bank, including its financial condition, performance, ownership and governance. *Capital Adequacy Ratio (CAR) Report* • S. 125 of the MORB requires banks to submit a quarterly report to the BSP of their risk-based CAR on a solo basis (head office plus branches) and on a consolidated basis (parent bank plus subsidiary financial allied undertakings but excluding insurance companies). • S. 127 of the MORB requires thrift, rural and cooperative banks to submit a quarterly report to the BSP 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. *ICAAP Document* • S. 130 of the MORB sets out the requirements of a bank's ICAAP. It provides for the evaluation of the overall material risks both from banking and nonbanking activities applied on a group-wide basis. The ICAAP document is required to be submitted to BSP by universal and commercial banks on an annual basis at end March. *Liquidity Reports* • S. 145-A of the MORB sets out the implementing guidelines for the LCR framework for universal and commercial banks and requires such banks to submit a quarterly LCR report to the BSP on a consolidated basis. • Circular 1007 sets out the implementing guidelines for the Net Stable Funding Ratio (NSFR) framework for universal and commercial banks and requires such banks to report quarterly on both solo and consolidated bases. *Large Exposures* • S. 361 of the MORB sets out the guidelines on large exposures of banks and their subsidiaries and affiliates to third parties. Consolidated LE information is not currently collected, but planned revisions to the LE framework will introduce consolidated LE reporting—see BCP 19. *Exposures to Related Parties* • Circular 895 requires an annual submission of report on conglomerate structures and quarterly submission of material exposures to related parties, which includes material RPTs of nonbank financial subsidiaries and affiliates—see BCP 20. *Real Estate Exposure* • Circular 976 requires banks to submit an Expanded Report on Real Estate Exposures and a Report on Project Finance Exposures, both on a solo and consolidated basis, on a quarterly basis.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	The supervisor reviews whether the oversight of a bank's foreign operations by management (of the parent bank or head office and, where relevant, the holding company) is adequate having regard to their risk profile and systemic importance and there is no hindrance in host countries for the parent bank to have access to all the material information from their foreign branches and subsidiaries. The supervisor also determines that banks' policies and processes require the local management of any cross-border operations to have the necessary expertise to manage those operations in a safe and sound manner, and in compliance with supervisory and regulatory requirements. The home supervisor takes into account the effectiveness of supervision conducted in the host countries in which its banks have material operations.
Description and findings re EC3	Although the scale of overseas operations of Philippine banks are not material to the overall operations of the banking groups, the BSP ensures as part of its licensing process that there will be effective oversight of the overseas operations by the parent bank. The BSP conducts regular examinations of those operations. The examination includes an assessment of management oversight, financial soundness and regulatory compliance, and involves liaison with the host regulator.
EC4	The home supervisor visits the foreign offices periodically, the location and frequency being determined by the risk profile and systemic importance of the foreign operation. The supervisor meets the host supervisors during these visits. The supervisor has a policy for assessing whether it needs to conduct on-site examinations of a bank's foreign operations, or require additional reporting, and has the power and resources to take those steps as and when appropriate.
Description and findings re EC4	The BSP, as home supervisor, conducts on-site examination of overseas branches/subsidiaries of Philippine banks. Prior notice of the visit and of the scope of the examination is given in advance to the host supervisor, and meetings are held following the examination to discuss any issues that arise. Determination of the frequency of examinations of banks' overseas operations is not risk based. Resolution 1847 of the MB requires foreign branches and subsidiaries of Philippine banks to be examined at least every two years regardless of their risk profile or the scale of their overseas operations. More frequent examination visits have been arranged when major supervisory issues (e.g., AMLA issues) have been identified by the BSP or host regulator.
EC5	The supervisor reviews the main activities of parent companies, and of companies affiliated with the parent companies, that have a material impact on the safety and soundness of the bank and the banking group, and takes appropriate supervisory action.
Description and findings re EC5	See EC1.
EC6	The supervisor limits the range of activities the consolidated group may conduct and the locations in which activities can be conducted (including the closing of foreign offices) if it determines that: (a) the safety and soundness of the bank and banking group is compromised because the activities expose the bank or banking group to excessive risk and/or are not properly managed; (b) the supervision by other supervisors is not adequate relative to the risks the activities present; and/or,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC6	(c) the exercise of effective supervision on a consolidated basis is hindered
Description and findings re EC6	Circular 875 provides the BSP with the general power to limit the range of activities the consolidated group may conduct and the locations in which activities can be conducted (including the closing of foreign offices). This power only extends to the bank and its financial allied subsidiaries and affiliates, and not to entities within a wider conglomerate. The three main categories of enforcement actions are: (1) corrective actions, (2) sanctions, and (3) other supervisory actions. These may include: 1. Restriction on operations, such as lending, investment, and active marketing of deposit products. 2. Restriction on acquisition of major assets. 3. Restriction on cash and property dividend declaration. 4. Restriction of activities relative to authorized licenses or privileges granted to the BSFI. S. 377 of the MORB sets out the limitations and restrictions in a bank's investment in nonfinancial allied and non-allied undertakings. Only universal banks may engage in nonbanking business activities and certain limits and restrictions are set to establish safety nets in these types of investment. For instance, the subsidiaries or affiliates to be established abroad shall not engage in stock trading activity. S. 105 of the MORB sets out the requirements to establish a banking office abroad, which may include branches, agencies, representative offices, remittance centers, remittance desk offices and other offices. The application for an authority to establish an office abroad is subject, inter alia, to certification from the host country that the BSP will be authorized to examine the proposed offices.
EC7	In addition to supervising on a consolidated basis, the responsible supervisor supervises individual banks in the group. The responsible supervisor supervises each bank on a stand-alone basis and understands its relationship with other members of the group.[28/]
Description and findings re EC7	The BSP applies prudential standards at both consolidated level and at the individual bank level for banking groups. Supervisors have a clear understanding of the operations of entities within the consolidated group and the relationship of the individual bank to those entities. Investments in insurance subsidiaries and equity investments in entities that fall outside the consolidated group are deducted from consolidated group capital and the distribution of capital within different financial entities of a banking group according to the allocation of risks are captured appropriately through the consolidation process.
Assessment of Principle 12	Largely Compliant
Comments	The BSP's supervisory regime adequately assesses the adequacy of a consolidated banking groups' capital and liquidity positions and ensures that RPTs are conducted on an arms-length basis. Concentration risk is not currently captured adequately because the single borrower limit is not applied at the consolidated group level, but proposed revisions to the LE framework will address this issue. The majority of BSP designated D-SIBs are incorporated within a conglomerate structure that includes non-regulated parent companies and affiliates engaged in nonbanking activities, but the wider group of companies is not captured within BSP's regulatory perimeter.

[28/] Please refer to Principle 16, Additional Criterion 2.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	All BSP regulated entities are included in consolidated banking groups, but not all financial institutions under the supervision of IC and the SEC are part of those consolidated banking groups. As noted in BCP1, the BSP does not have the power to review and examine the parent or other affiliate companies of BSP supervised firms. Recommendations: • Bring financial institutions in conglomerate structures which are outside the BSP consolidated banking group and which are regulated by other domestic regulators into the consolidated banking group to enable the BSP to capture the risks they pose to the banking group. • Require BSP regulated banks within conglomerate structures specifically to identify all risks arising from companies within their wider group structure in their ICAAP and describe fully the internal controls for reporting and managing such risks.
Principle 13	**Home-host relationships**. Home and host supervisors of cross-border banking groups share information and cooperate for effective supervision of the group and group entities, and effective handling of crisis situations. Supervisors require the local operations of foreign banks to be conducted to the same standards as those required of domestic banks.
Essential criteria	
EC1	The home supervisor establishes bank-specific supervisory colleges for banking groups with material cross-border operations to enhance its effective oversight, taking into account the risk profile and systemic importance of the banking group and the corresponding needs of its supervisors. In its broadest sense, the host supervisor who has a relevant subsidiary or a significant branch in its jurisdiction and who, therefore, has a shared interest in the effective supervisory oversight of the banking group, is included in the college. The structure of the college reflects the nature of the banking group and the needs of its supervisors.
Description and findings re EC1	The BSP has not established supervisory colleges for the five Philippine banks with overseas operations on the basis that the scale of those operations is not material. There are five large banks that have international presences in Hong Kong SAR, Taiwan, China, Japan, Germany, USA, Guam, Israel, Singapore, UAE, Bahrain, Italy, France, Saudi Arabia, and Kuwait, but the operations represent less than 5 percent of any of the respective banks' total assets.
EC2	Home and host supervisors share appropriate information on a timely basis in line with their respective roles and responsibilities, both bilaterally and through colleges. This includes information both on the material risks and risk management practices of the banking group[29/] and on the supervisors' assessments of the safety and soundness of the relevant entity under their jurisdiction. Informal or formal arrangements (such as memoranda of understanding) are in place to enable the exchange of confidential information.
Description and findings re EC2	The BSP has signed information sharing arrangements with the following seven regulatory authorities: a. China Banking Regulatory Commission (China) on October 18, 2005; b. Bank of England (UK) on January 15, 2007 (updated August 3, 2012); c. Financial Supervisory Commission (Taiwan Province of China) on January 31, 2007;

[29/] See Illustrative example of information exchange in colleges of the October 2010 BCBS Good practice principles on supervisory colleges for further information on the extent of information sharing expected.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	d. Federal Financial Supervisory Agency or BaFin (Germany) on February 9, 2007; e. Hong Kong Monetary Authority (Hong Kong SAR) on March 7, 2007; f. Bank of Thailand (Thailand) on December 17, 2017, and g. Australian Prudential Regulation Authority (Australia New Zealand) on June 4, 2014. The Japanese Financial Services Agency and De Nederlandsche Bank have agreed informal information sharing arrangements with the BSP and discussions are in train with U.S. counterparts (Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision and Office of the Comptroller of the Currency) for a possible MOU on home-host supervisory coordination. Austria declined to sign an MOU with the BSP in view of the banking secrecy law. As home supervisor, the BSP shares the results of its examination of foreign offices of domestic banks with host supervisors when requested, and subject to the conditions that (a) information contained in the report is used solely for its supervision of the foreign office; (b) information in the report should be treated with utmost confidentiality; and (c) the host regulator shall not disclose the report or the information therein to other parties without the BSP's consent. The BSP maintains an up-to-date contact list of overseas regulators and there is evidence of two-way information sharing between the BSP and overseas regulators on an informal, ad hoc basis. The MOA with BaFin needs to be reviewed as responsibility for supervision of the German bank's branch has passed to the SSM.
EC3	Home and host supervisors coordinate and plan supervisory activities or undertake collaborative work if common areas of interest are identified in order to improve the effectiveness and efficiency of supervision of cross-border banking groups.
Description and findings re EC3	The BSP has not conducted joint examinations with overseas regulators either as host or home supervisor. As home supervisor, the foreign operations of Philippine banks are not material in host countries and, as a host supervisor, the BSP meets overseas regulators when they conduct examinations of Philippine-based foreign banks both at the start and end of the examinations.
EC4	The home supervisor develops an agreed communication strategy with the relevant host supervisors. The scope and nature of the strategy reflects the risk profile and systemic importance of the cross-border operations of the bank or banking group. Home and host supervisors also agree on the communication of views and outcomes of joint activities and college meetings to banks, where appropriate, to ensure consistency of messages on group-wide issues.
Description and findings re EC4	The limited scale of overseas operations of Philippine banks does not warrant the development of formal communication strategies between the BSP and host regulators.
EC5	Where appropriate, due to the bank's risk profile and systemic importance, the home supervisor, working with its national resolution authorities, develops a framework for cross-border crisis cooperation and coordination among the relevant home and host authorities. The relevant authorities share information on crisis preparations from an early stage in a way that does not materially compromise the prospect of a successful resolution and subject to the application of rules on confidentiality.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	There are foreign banks in the Philippines which are designated as D-SIBs. The failure of any of the parent banks of these operations would present a systemic risk to the Philippine banking sector. As the scale of the Philippine operations of these banks are not material in terms of the overall operations of these banking groups, the BSP is not party to the CMGs set up by those banks. The risk to the Philippine banking sector from the failure of any of these D-SIBs is mitigated in part by the fact that the said banks are subject to the BSP's capital and liquidity regulations. Local capital and liquidity are required to be held in the Philippines. The BSP also requires the parent banks of these D-SIBs to issue notarized guarantees in compliance with S. 75 of the GBL. See BCP 11 for discussion of resolution planning with the PDIC.
EC6	Where appropriate, due to the bank's risk profile and systemic importance, the home supervisor, working with its national resolution authorities and relevant host authorities, develops a group resolution plan. The relevant authorities share any information necessary for the development and maintenance of a credible resolution plan. Supervisors also alert and consult relevant authorities and supervisors (both home and host) promptly when taking any recovery and resolution measures.
Description and findings re EC6	Due to the limited scale of the overseas operations of Philippine banks, the BSP has not engaged with host supervisors on resolution plans for the Philippine banking groups.
EC7	The host supervisor's national laws or regulations require that the cross-border operations of foreign banks are subject to prudential, inspection and regulatory reporting requirements similar to those for domestic banks.
Description and findings re EC7	Foreign banks are required to comply with the same prudential standards as domestic banks under S. 8 of RA 7721, as amended by RA No. 10641, and S. 77 of RA 8791.
EC8	The home supervisor is given on-site access to local offices and subsidiaries of a banking group in order to facilitate their assessment of the group's safety and soundness and compliance with customer due diligence requirements. The home supervisor informs host supervisors of intended visits to local offices and subsidiaries of banking groups.
Description and findings re EC8	As home supervisor, the BSP has full access to conduct on-site examinations of overseas branches/subsidiaries of Philippine banks. Host supervisors are informed in advance of the purpose and scope of the examination and the BSP supervisors visit the host supervisory authority to discuss any issues arising from the examination. Conversely. home country supervisors are allowed to conduct on-site examinations of cross-border establishments in the Philippines.
EC9	The host supervisor supervises booking offices in a manner consistent with internationally agreed standards. The supervisor does not permit shell banks or the continued operation of shell banks.
Description and findings re EC9	The BSP does not permit booking operations or shell banks in the Philippines.
EC10	A supervisor that takes consequential action on the basis of information received from another supervisor consults with that supervisor, to the extent possible, before taking such action.
Description and findings re EC10	The BSP has not had cause to take action based on information provided by it from another supervisor.
Assessment of Principle 13	Compliant
Comments	The overseas activities of Philippine banks are not material to their overall operations, but the BSP has established MOAs and less formal information sharing arrangements with

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	relevant host countries. As noted in BCP3, the MOA with BaFin should be reviewed as supervisory responsibility for the relevant bank has transferred to the SSM.
Prudential Regulations and Requirements	
Principle 14	**Corporate governance**. The supervisor determines that banks and banking groups have robust corporate governance policies and processes covering, for example, strategic direction, group and organizational structure, control environment, responsibilities of the banks' Boards and senior management,[30/] and compensation. These policies and processes are commensurate with the risk profile and systemic importance of the bank.
Essential criteria	
EC1	Laws, regulations or the supervisor establish the responsibilities of a bank's Board and senior management with respect to corporate governance to ensure there is effective control over the bank's entire business. The supervisor provides guidance to banks and banking groups on expectations for sound corporate governance.
Description and findings re EC1	S. 132 of the MORB outlines specific duties and responsibilities of the Board as a collective body, including the requirement to: define a bank's corporate culture and values; approve the bank' objectives and strategies and in overseeing management's implementation, appointment/selection of key members of senior management and heads of control functions and for the approval of a sound remuneration and other incentives policy for personnel; approving and overseeing the bank's corporate governance framework. S. 134 of the MORB outlines the duties and responsibilities of the officers including the requirement to: set the tone of good governance from the top; oversee the day-to-day management of the bank; ensure duties are effectively delegated to the staff, establish a management structure that promotes accountability and transparency and promote and strengthen checks and balances systems in the bank. S. 132 of the MORB outlines the duties and responsibilities of the Chairman of the Board and S. 134 of the MORB outlines the duties and responsibilities of the CEO. S. 136 of the MORB outlines BSP's expectations of FI's management of related party transactions.
EC2	The supervisor regularly assesses a bank's corporate governance policies and practices, and their implementation, and determines that the bank has robust corporate governance policies and processes commensurate with its risk profile and systemic importance. The supervisor requires banks and banking groups to correct deficiencies in a timely manner.
Description and findings re EC2	BSP's on-site examination framework includes the assessment of a bank's policies in terms of adequacy, applicability relative to its risk profile and size of operations. Part of this assessment includes the on-site examiners holding meetings with the Board of directors of banks to discuss key supervisory issues and concerns and also to emphasize the need to implement immediate reforms. The BSP also imposes enforcement actions on the Board and key officers for governance issues noted. The Assessors noted that there are cases wherein the BSP has issued warning letters or reprimands to directors or senior officers of certain banks where action was required to address deficiencies.

30/ Please refer to footnote 21 under Principle 5.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	The supervisor determines that governance structures and processes for nominating and appointing Board members are appropriate for the bank and across the banking group. Board membership includes experienced non-executive members, where appropriate. Commensurate with the risk profile and systemic importance, Board structures include audit, risk oversight and remuneration committees with experienced non-executive members
Description and findings re EC3	Banks' governance structures are guided by S. 15 of the GBL and S. 132 of the MORB in its determination of the numbers of members for the Board of directors (e.g., at least five members—two of which are independent directors—to a maximum of 15 members—not less than 1/3 make up independent members). For RBs, at least 1 independent director is required. S. 133 of the MORB stipulates that banks have an audit committee, risk oversight committee and a corporate governance committee as well as a related party transaction committee for universal and commercial banks (note that non-complex banks are only required at a minimum to have an audit committee.) S. 133 of the MORB outlines the Corporate Governance Committees of banks to oversee the review, evaluation and nomination of Board members. BSP's annual on-site examination framework includes the assessment of the bank's overall governance structure as well as the processes for nominating and appointing board members that are appropriate and commensurate with the bank's overall risk profile and size of operations.
EC4	Board members are suitably qualified, effective and exercise their "duty of care" and "duty of loyalty."[31/]
Description and findings re EC 4	S. 132 of the MORB provides the minimum qualifications of the Board of directors and incorporates the concept of "fit and proper rule" that govern the assessment on the suitability of each Board member to include an assessment on the: integrity/probity, physical/mental fitness; relevant education/financial literacy/training; possession of competencies relevant to the job, such as knowledge and experience, skills, diligence and independence of mind; and sufficiency of time to fully carry out responsibilities. It further provides that the position of a director is a position of trust and that the members of the Board of directors should exercise their "duty of care" and "duty of loyalty" to the institution.
EC5	The supervisor determines that the bank's Board approves and oversees implementation of the bank's strategic direction, risk appetite[32/] and strategy, and related policies, establishes and communicates corporate culture and values (e.g., through a code of conduct), and establishes conflicts of interest policies and a strong control environment.

[31/] The OECD (OECD glossary of corporate governance-related terms in "Experiences from the Regional Corporate Governance Roundtables," 2003, www.oecd.org/dataoecd/19/26/23742340.pdf.) defines "duty of care" as "The duty of a board member to act on an informed and prudent basis in decisions with respect to the company. Often interpreted as requiring the board member to approach the affairs of the company in the same way that a 'prudent man' would approach their own affairs. Liability under the duty of care is frequently mitigated by the business judgment rule." The OECD defines "duty of loyalty" as "The duty of the board member to act in the interest of the company and shareholders. The duty of loyalty should prevent individual board members from acting in their own interest, or the interest of another individual or group, at the expense of the company and all shareholders."

[32/] "Risk appetite" reflects the level of aggregate risk that the bank's Board is willing to assume and manage in the pursuit of the bank's business objectives. Risk appetite may include both quantitative and qualitative elements, as appropriate, and encompass a range of measures. For the purposes of this document, the terms "risk appetite" and "risk tolerance" are treated synonymously.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	BSP's on-site annual examination framework assesses the quality of banks' corporate governance processes which includes discussion with management of the bank's strategic direction and a review of the approved strategies/plans, ICAAP, minutes of Board meetings and the related policies and procedures. Board oversight is also assessed through the review of performance against targets/standards, performance of management, succession planning, among others. Corporate culture and values are assessed through interviews/walkthroughs, observation and review of code of conduct/ethics. The BSP also conducts thematic/horizontal discussions with the Board on strategic direction, ICAAP and significant examination issues. Examination issues and concerns noted on different risk areas are also synthesized and feed into the overall assessment of the quality of corporate governance. In recognition of the extent to which the risk culture of a bank supports its formal governance structures and facilitates the balanced consideration and management of risk that may affect the bank's viability, the BSP created a technical working group on the Supervision of Conduct and Culture to study how supervision of conduct and culture can be included in the existing supervisory approach.
EC6	The supervisor determines that the bank's Board, except where required otherwise by laws or regulations, has established fit and proper standards in selecting senior management, maintains plans for succession, and actively and critically oversees senior management's execution of Board strategies, including monitoring senior management's performance against standards established for them.
Description and findings re EC6	S. 132 of the MORB outlines the Board's requirements in the assessment and selection of senior management, including the need for performance monitoring. BSP's annual on-site supervision framework includes the assessment of a bank's Board polices that relate to the selection and maintenance of senior management including whether senior management executes Board strategies within prescribed risk appetite and limits.
EC7	The supervisor determines that the bank's Board actively oversees the design and operation of the bank's and banking group's compensation system, and that it has appropriate incentives, which are aligned with prudent risk taking. The compensation system, and related performance standards, are consistent with long-term objectives and financial soundness of the bank and is rectified if there are deficiencies.
Description and findings re EC7	S. 132 and 135 of the MORB provide that the Board shall approve a remuneration and other incentives policy that is appropriate and consistent with the bank's risk appetite, performance and control environment. BSP's on-site examination framework include an assessment of a bank's propriety and transparency of the compensation and incentives system. This includes an assessment of the adequacy of oversight of the compensation system, as well as a review of the related policies and procedures. The examination also includes an evaluation of the prudence and reasonableness of compensation and granting of incentives (e.g., in the form of loans, advances or other credit accommodations) as well as the related disclosure. BSP flags banks on issues relating to compensation/remuneration.
EC8	The supervisor determines that the bank's Board and senior management know and understand the bank's and banking group's operational structure and its risks, including those arising from the use of structures that impede transparency (e.g., special-purpose or

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC8	related structures). The supervisor determines that risks are effectively managed and mitigated, where appropriate.
Description and findings re EC8	BSP's on-site examination conducts an assessment of the adequacy of the banking group's parent oversight of subsidiaries and affiliates, with the expectation that the same quality of governance is observed across the group. Assessors note that this review of Board and senior management knowledge of group's operational structures is key given the extensive conglomerate structures that banking group operate within in the Philippines.
EC9	The supervisor has the power to require changes in the composition of the bank's Board if it believes that any individuals are not fulfilling their duties related to the satisfaction of these criteria.
Description and findings re EC9	S. 138 of the MORB outlines the grounds for disqualification of a Board member. S. 002 of the MORB provides a range of enforcement tools available to the BSP to administer sanctions to directors and officers if required and include: reprimand, restriction on compensation and benefits, divestment, suspension, disqualification, removal and monetary penalties/fines. Assessors noted BSP has made use of these enforcement tools.
Assessment of Principle 14	Compliant
Comments	BSP's Corporate Governance regulations and guidelines are comprehensive, with appropriate and clearly articulated requirements for Boards and senior management. BSP's on-site examination framework adequately reviews banks' compliance with BSP's regulations.
Principle 15	**Risk management process**. The supervisor determines that banks[33/] have a comprehensive risk management process (including effective Board and senior management oversight) to identify, measure, evaluate, monitor, report and control or mitigate[34/] all material risks on a timely basis and to assess the adequacy of their capital and liquidity in relation to their risk profile and market and macroeconomic conditions. This extends to development and review of contingency arrangements (including robust and credible recovery plans where warranted) that take into account the specific circumstances of the bank. The risk management process is commensurate with the risk profile and systemic importance of the bank.[35/]
Essential criteria	
EC1	The supervisor determines that banks have appropriate risk management strategies that have been approved by the banks' Boards and that the Boards set a suitable risk appetite to define the level of risk the banks are willing to assume or tolerate. The supervisor also determines that the Board ensures that:

[33/] For the purposes of assessing risk management by banks in the context of Principles 15 to 25, a bank's risk management framework should take an integrated "bank-wide" perspective of the bank's risk exposure, encompassing the bank's individual business lines and business units. Where a bank is a member of a group of companies, the risk management framework should in addition cover the risk exposure across and within the "banking group" (see footnote 19 under Principle 1) and should also take account of risks posed to the bank or members of the banking group through other entities in the wider group.

[34/] To some extent the precise requirements may vary from risk type to risk type (Principles 15 to 25) as reflected by the underlying reference documents.

[35/] It should be noted that while, in this and other Principles, the supervisor is required to determine that banks' risk management policies and processes are being adhered to, the responsibility for ensuring adherence remains with a bank's Board and senior management.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC1	(a) a sound risk management culture is established throughout the bank; (b) policies and processes are developed for risk-taking, that are consistent with the risk management strategy and the established risk appetite; (c) uncertainties attached to risk measurement are recognized; (d) appropriate limits are established that are consistent with the bank's risk appetite, risk profile and capital strength, and that are understood by, and regularly communicated to, relevant staff; and (e) senior management takes the steps necessary to monitor and control all material risks consistent with the approved strategies and risk appetite.
Description and findings re EC1	In general, BSP's risk-based supervisory reviews takes into consideration a bank's risk management systems and processes by assessing: active and appropriate Board and senior management oversight; adequate risk management policies and procedures; appropriate risk measurement methodologies, limits structure, monitoring and management information system; and comprehensive internal controls and independent IA. BSP on-site supervisory framework assesses the capability of a bank's Board of directors and senior management to identify, measure, monitor and control the risk inherent in an institution's activities, including that ability to assess any uncertainties of risk measurement/models. BSP assesses whether a bank's Board approved policies and processes for risk-taking are commensurate with the risk profile and risk appetite of the bank and whether management operates within the prescribed risk limits. On-site examiners assess the risk management culture of both senior management and the Board. Assessors note that BSP's exposure draft policy (released for industry consultation) on reputational risk management aims to provide preliminary guidance on the BSP's supervisory approach on a bank's management of reputational risk and sets out BSP's expectations for the bank's adoption of a sound reputational risk management framework that is commensurate to its size, nature, complexity of operations and overall risk profile.
EC2	The supervisor requires banks to have comprehensive risk management policies and processes to identify, measure, evaluate, monitor, report and control or mitigate all material risks. The supervisor determines that these processes are adequate: (a) to provide a comprehensive "bank-wide" view of risk across all material risk types; (b) for the risk profile and systemic importance of the bank; and (c) to assess risks arising from the macroeconomic environment affecting the markets in which the bank operates and to incorporate such assessments into the bank's risk management process.
Description and findings re EC2	Circular No. 971 provides BSP's guidance on Risk Governance to banks and stipulates that a bank should have a risk management framework commensurate with its risk profile, which embodies a risk appetite framework that shall include policies supported by appropriate control procedures and processes, designed to ensure effective risk identification, aggregation, mitigation and monitoring of all material risks.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	BSP's supervisory risk assessment approach together with its on-site supervision framework assesses a bank's ability to provide a bank-wide view of risk across all material risk types, takes into consideration the systemic importance of the bank and assesses emerging risk from the macroeconomic environment. BSP assesses the adequacy of the bank's ICAAP, specifically with respect to the identification of vulnerabilities in times of financial distress through sensitivity analysis, scenario analysis and stress testing are also reviewed and challenged in connection with the assessment of the viability of the recovery plan.
EC3	The supervisor determines that risk management strategies, policies, processes and limits are: (a) properly documented; (b) regularly reviewed and appropriately adjusted to reflect changing risk appetites, risk profiles and market and macroeconomic conditions; and (c) communicated within the bank The supervisor determines that exceptions to established policies, processes and limits receive the prompt attention of, and authorization by, the appropriate level of management and the bank's Board where necessary.
Description and findings re EC3	Circular No. 969 states that a Risk Oversight Committee is to oversee the risk management framework and ensure that there is periodic review of the effectiveness of the risk management systems and recovery plans. It shall ensure that corrective actions are promptly implemented to address risk management concerns. In this respect, the committee shall advise the Board on the bank's overall current and future risk appetite, oversee senior management's adherence to the risk appetite statement (based on the quality of compliance with the limit structure, policies, and procedures relating to risk management and control, and performance of management, among others), and report on the state of risk culture of the bank. BSP's on-site examination framework assesses Board-approved strategies, risk policy manual and risk limits. In particular, limit-setting processes are reviewed to determine whether risk appetite is appropriately translated into risk limits that are reasonable in view of business model and capital. The process of identifying and reporting limit breaches is also reviewed to determine whether breaches are escalated, reported and properly addressed. Frequency, volume and timing of limit breaches are also checked to determine if limits are still reflective of the bank's current operations and risk profile.
EC4	The supervisor determines that the bank's Board and senior management obtain sufficient information on, and understand, the nature and level of risk being taken by the bank and how this risk relates to adequate levels of capital and liquidity. The supervisor also determines that the Board and senior management regularly review and understand the implications and limitations (including the risk measurement uncertainties) of the risk management information that they receive.
Description and findings re EC4	BSP's annual on-site examination framework includes an assessment of the accuracy and integrity, completeness, timeliness and adaptability of a bank's risk data aggregation and that reporting systems are being evaluated. This assessment is carried through (i) review of risk reports (including stress testing), which show impact of risk exposures to capital and liquidity and comparison of these reports with prudential reports, audited financial statements and other available information, (ii) walkthrough, (iii) test of balances,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	(iv) analytical procedures, among others. Internal and external audit reports are also reviewed to determine information systems or risk reporting issues and how these are being addressed. If deficiencies are detected, the BSP may require a bank (through directives in the report of examination) to strengthen its MIS as a result of the on-site examination on instances wherein weaknesses in the data aggregation and reporting processes/systems are noted. BSP directives include the adoption, improvement or maintenance of an appropriate credit MIS to facilitate proper classification/tagging and aggregation of loans as to type/industry/status/loss classification and effective comprehensive and timely monitoring and reporting loan exposures, including credit concentration and breaches in internal limits, to Board and management.
EC5	The supervisor determines that banks have an appropriate internal process for assessing their overall capital and liquidity adequacy in relation to their risk appetite and risk profile. The supervisor reviews and evaluates banks' internal capital and liquidity adequacy assessments and strategies.
Description and findings re EC5	All universal and commercial banks are required to prepare an ICAAP and BSP reviews the adequacy of the assumptions behind the capital planning process during its annual on-site examinations. The review covers the bank's capital planning process and how strategic planning, risk management and stress testing feed into the ICAAP. Board oversight, particularly how the body challenges key assumptions in the ICAAP including identification of vulnerabilities in times of financial distress through sensitivity analysis, scenario analysis and stress testing, are reviewed and challenged in connection with the assessment of the viability of the recovery plan. In addition, BSP also assesses a bank's sufficiency of contingency funding planning during the on-site examination, including a review of the timeliness and appropriateness of action plans/strategies by the Board/risk oversight committee to ensure adequacy of both liquidity and capital relative to the results of measurement of material risks. Assessors noted that, if BSP disagrees with the adequacy of a Board's ICAAP, assumptions are challenged but the request to increase Board's internal capital/liquidity limits are not recommended. It is noted that although BSP's Charter (NCBA) has been amended in February 2019 to empower the BSP to require banks to hold capital beyond the minimum requirements, it has not made of use of this power to date. In addition, Assessors have suggested that BSP consider rolling out the concept of ICAAP to its smaller banks, taking into consideration the nature, size and complexity of the bank. Last, given BSP is moving towards a more risk based on-site supervision framework, BSP should consider how it will review a bank's ICAAP and contingency funding plans without going on-site. It is noted that the ICAAP guidance is somewhat outdated (2009) and should be revisited to ensure the regulatory requirements are robust and are linked to the setting of prudential capital requirements.
EC6	Where banks use models to measure components of risk, the supervisor determines that: (a) banks comply with supervisory standards on their use;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC6	(b) the banks' Boards and senior management understand the limitations and uncertainties relating to the output of the models and the risk inherent in their use; and (c) banks perform regular and independent validation and testing of the models The supervisor assesses whether the model outputs appear reasonable as a reflection of the risks assumed.
Description and findings re EC6	BSP assesses a bank's use of various models during the on-site examination process and takes into consideration the following: (a) a bank's compliance with the various regulations that embed the use of models (Circular No. 989 Stress testing; Circular No. 971 Risk Governance; Circular Nos. 981 Liquidity Risk; 900 Operational Risk; 855 on Credit Risk; 544 Market Risk; 639 ICAAP); (b) adequacy of the bank's Board and senior management awareness and understanding of the limitations and uncertainties related to the output of models through the assessment of information and minimizes provided to the Board and Risk Oversight Committee; (c) BSP reviews a bank's independent validation and testing of models. However, only the market risk specialists perform regular reviews of market risk and IRB models. Assessors noted BSP's on-going policy initiative to develop a Model Risk Management (MRM) regulation (exposure draft released to the industry for consultation) designed to be commensurate with a bank's size, nature, complexity, sophistication, risk appetite and risk exposure, with emphasis on governance and control structure, particularly the Board and management's responsibility to ensure that MRM forms part of its risk culture. The MRM framework of universal and commercial banks is expected to incorporate model development, validation, implementation and use and governance policies and controls. Thrift, rural and cooperative banks are expected to adopt a simplified MRM approach. At a minimum, these banks shall provide an inventory of all their models and develop/adopt a system that will enable the identification and assessment of material and relevant models. To the extent feasible, a foreign bank branch shall comply with the requirements imposed on universal and commercial banks. When a foreign bank branch relies on models that have been approved by its Head Office or parent bank, it shall ensure that such models are appropriate for its domestic requirements as well.
EC7	The supervisor determines that banks have information systems that are adequate (both under normal circumstances and in periods of stress) for measuring, assessing and reporting on the size, composition and quality of exposures on a bank-wide basis across all risk types, products and counterparties. The supervisor also determines that these reports reflect the bank's risk profile and capital and liquidity needs, and are provided on a timely basis to the bank's Board and senior management in a form suitable for their use.
Description and findings re EC7	During on-site examinations, BSP assesses the adequacy of a bank's MIS by examining the accuracy and integrity, completeness, timeliness and adaptability of risk data aggregation and reporting systems on a bank wide-basis, as well as sufficiency of controls which are being evaluated through the review of risk reports, audited financial statements and other available information, interviews with senior management/walkthrough, test of balances, and analytical procedures. Internal and external audit reports are also reviewed to determine information systems or risk reporting issues and how these are being addressed.
EC8	The supervisor determines that banks have adequate policies and processes to ensure that

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC8	the banks' Boards and senior management understand the risks inherent in new products,[36/] material modifications to existing products, and major management initiatives (such as changes in systems, processes, business model and major acquisitions). The supervisor determines that the Boards and senior management are able to monitor and manage these risks on an ongoing basis. The supervisor also determines that the bank's policies and processes require the undertaking of any major activities of this nature to be approved by their Board or a specific committee of the Board.
Description and findings re EC8	Risks in new products, material modifications to existing products, and major management initiatives and how these are managed are assessed by BSP during on-site examinations through the review of minutes of Board meetings, policies and procedures, as well as through walkthroughs and interviews with management.
EC9	The supervisor determines that banks have risk management functions covering all material risks with sufficient resources, independence, authority and access to the banks' Boards to perform their duties effectively. The supervisor determines that their duties are clearly segregated from risk-taking functions in the bank and that they report on risk exposures directly to the Board and senior management. The supervisor also determines that the risk management function is subject to regular review by the internal audit function.
Description and findings re EC9	BSP's on-site annual examination framework include the assessment of a bank's risk management framework, including a review of the risk management charter, organizational structure, adequacy of resources (appropriate to the relative complexity of the size of the bank's operations and risk-appetite/profile), reporting lines (directly to Risk Oversight Committee to the Board), duties and responsibilities, risk reports, minutes of meetings, risk management policies and procedures of all major risks, and internal audit reports.
EC10	The supervisor requires larger and more complex banks to have a dedicated risk management unit overseen by a Chief Risk Officer (CRO) or equivalent function. If the CRO of a bank is removed from his/her position for any reason, this should be done with the prior approval of the Board and generally should be disclosed publicly. The bank should also discuss the reasons for such removal with its supervisor.
Description and findings re EC10	Circular No. 971 on credit governance provides that universal and commercial banks should appoint a Chief Risk Officer (CRO) to head the risk management function. The appointment, dismissal and other changes to the CRO or its equivalent position shall have prior approval of the Board. In cases where the CRO will be replaced, the bank shall report the same to the appropriate supervising department of the FSS within five days from the time it has been approved by the Board. Publicly-listed banks are likewise required to report the resignation/removal of officers through Philippine Stock Exchange Disclosure Form 4-8—Change in Directors and/or Officers (Resignation/Removal or Appointment/Election). Assessors noted that the BSP has released a draft exposure regulation to the industry which, once finalized, will require universal and commercial banks and their subsidiary banks/QBs to publicly disclose the removal of their CROs, including Chief Compliance Officers and Chief Audit Executives.
EC11	The supervisor issues standards related to, in particular, credit risk, market risk, liquidity risk, interest rate risk in the banking book and operational risk.
Description and findings re EC11	Circular No. 510 outlines BSP's standards with respect to credit risk, market risk, liquidity risk, interest rate risk in the banking book and operational risk.

[36/] New products include those developed by the bank or by a third party and purchased or distributed by the bank.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC12	The supervisor requires banks to have appropriate contingency arrangements, as an integral part of their risk management process, to address risks that may materialize and actions to be taken in stress conditions (including those that will pose a serious risk to their viability). If warranted by its risk profile and systemic importance, the contingency arrangements include robust and credible recovery plans that take into account the specific circumstances of the bank. The supervisor, working with resolution authorities as appropriate, assesses the adequacy of banks' contingency arrangements in the light of their risk profile and systemic importance (including reviewing any recovery plans) and their likely feasibility during periods of stress. The supervisor seeks improvements if deficiencies are identified.
Description and findings re EC12	Circular No. 904 requires D-SIBs to prepare recovery plans which are embedded in the bank's ICAAP. These plans are reviewed and BSP provides feedback for banks to improve any deficiencies identified. In addition, banks are required to ensure adequate operational risk management processes with respect to business continuity management (Circular No. 900 and 951) and liquidity contingency funding arrangements are in place (Circular Nos. 981). Further, banks are required to conduct stress testing (Circular No. 989 as well as the REST) to raise awareness to the Board of bank's potential vulnerabilities from both a capital and liquidity perspective. At this time, BSP does not share the D-SIB recovery plans with PDIC. It would be beneficial to include the views of the PDIC, as the principal Resolution Authority, to assess the robustness of individual D-SIB recovery plans. It is suggested that the recovery plans are pulled out of the ICAAP and reviewed not only by the lead supervisor but compared across D-SIBs to ensure consistency in the assumptions and to assess the cumulative aspects of the plans (e.g., management actions to be taken when more than one D-SIB is in trouble at the same time). In addition, although the FSCC has approved a FCMR Framework for the domestic regulatory agencies to work towards crisis operational preparedness in dealing with the failure of a major bank, each agency is still working on finalizing their individual crisis management plans. Assessors note that the agreed contingency arrangements amongst the regulatory agencies who sit on the FSCC are very preliminary in nature. Much more work is required to fully develop adequate contingency planning arrangements for the recovery and/failure of a systemic bank.
EC13	The supervisor requires banks to have forward-looking stress testing programs, commensurate with their risk profile and systemic importance, as an integral part of their risk management process. The supervisor regularly assesses a bank's stress testing program and determines that it captures material sources of risk and adopts plausible adverse scenarios. The supervisor also determines that the bank integrates the results into its decision-making, risk management processes (including contingency arrangements) and the assessment of its capital and liquidity levels. Where appropriate, the scope of the supervisor's assessment includes the extent to which the stress testing program: (a) promotes risk identification and control, on a bank-wide basis (b) adopts suitably severe assumptions and seeks to address feedback effects and system-wide interaction between risks;

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC13	(c) benefits from the active involvement of the Board and senior management; and (d) is appropriately documented and regularly maintained and updated. The supervisor requires corrective action if material deficiencies are identified in a bank's stress testing program or if the results of stress tests are not adequately taken into consideration in the bank's decision-making process
Description and findings re EC13	Circular No. 989 requires banks to conduct stress testing exercises that include hypothetical shocks that are incorporated in the sensitivity analysis, as well as ensuring a forward-looking approach to the assumptions. BSP's on-site supervision framework includes an assessment of whether banks perform comprehensive stress testing on material risks, such as credit, market, liquidity risks, and evaluate how the results of stress testing exercises are appropriately incorporated in the capital, liquidity and strategic planning processes, including ICAAP and the involvement of Board and senior management in this process. As part of this assessment, examiners may require banks to change assumptions (by applying more severe assumptions) or take corrective action if the overall stress testing program does not adequately reflect the bank's risk profile, implications of additional capital or liquidity are not sufficient.
EC14	The supervisor assesses whether banks appropriately account for risks (including liquidity impacts) in their internal pricing, performance measurement and new product approval process for all significant business activities.
Description and findings re EC14	BSP's annual on-site examination assess banks' internal pricing mechanisms, performance measurement of these pricing mechanisms as well as reviewing the new product approval process for all significant business activities. (See EC 8 for more detailed information.)
Assessment of Principle 15	Largely Compliant
Comments	Overall, BSP's regulatory framework on risk management governance appears to be adequate for the currently defined risk areas (credit, IRRB, market, operational, etc.). However, given the increasing trends among banks towards greater use of quantitative analysis and models in decision making processes, it is important that BSP finalize the draft exposures pertaining to model risk management. Further, the finalization of the draft exposures on reputational risk as well as updating the regulations to reflect the requirement to publicly disclose the dismissal or replacement of a bank's CEO, CRO, Chief Compliance Officer and Internal Audit Executives is also needed. BSP's current guidance used to assess bank's internal capital (ICAAP) needs to be updated to reflect current practices. In addition, recovery plans should be separated out of ICAAP and shared with PDIC as it would be beneficial to include the views of the resolution authority in the assessment of the robustness of the plans. In addition, although the FSCC has approved a Financial Crisis Management and Resolution Framework for the domestic regulatory agencies to work towards crisis operational preparedness in dealing with a material problem of a major bank, each agency is still working on developing and finalizing their individual crisis management plans. Assessors note that the agreed contingency arrangements amongst the regulatory agencies who sit on the FSCC are very preliminary in nature. Much more work is required to fully develop adequate contingency planning arrangements for the recovery and/failure of a systemic bank.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Comments	Recommendations: • Finalize draft exposures on model risk management, reputational and public disclosure of dismissal of CRO, CO and IA executives; • Develop and operationalize BSP's crisis preparedness involving a systemic financial institution, including working with other regulatory agencies within the FSCC (e.g., sharing D-SIB recovery plans with the PDIC) in order to strengthen and formalize needed contingency arrangements pertaining to the recovery or resolution of a major bank failure; and • Update guidance on ICAAP to reflect current practices.
Principle 16	**Capital adequacy.**[37/] The supervisor sets prudent and appropriate capital adequacy requirements for banks that reflect the risks undertaken by, and presented by, a bank in the context of the markets and macroeconomic conditions in which it operates. The supervisor defines the components of capital, bearing in mind their ability to absorb losses. At least for internationally active banks, capital requirements are not less than the applicable Basel standards.
Essential criteria	
EC 1	Laws, regulations or the supervisor require banks to calculate and consistently observe prescribed capital requirements, including thresholds by reference to which a bank might be subject to supervisory action. Laws, regulations or the supervisor define the qualifying components of capital, ensuring that emphasis is given to those elements of capital permanently available to absorb losses on a going concern basis.
Description and findings re EC1	S. 34 of the GBL of 2000 sets out the statutory requirement for the minimum capital ratio which the net worth of a bank must bear to its total risk assets. It provides that the minimum CAR shall be applied uniformly to banks of the same category and sets out possible sanctions for cases where a bank is not able to comply with the prescribed minimum ratio. Sanctions include limits or prohibitions on the distribution of profits, restriction or prohibition on the acquisition of major assets and the making of new investments. <u>Minimum capital requirements</u> The elements of the regulatory capital base used for computing the risk-based CAR for universal and commercial banks and their subsidiary banks and quasi-banks (QBs) are set out in Circular 781. The capital regime for stand-alone thrift, rural and cooperative banks is described below. Universal and commercial banks and their subsidiary banks and QBs are subject to the following risk-based CARs: a. Common Equity Tier 1 (CET1) must be at least 6.0 percent of risk weighted assets at all times; b. Tier 1 capital must be at least 7.5 percent of risk weighted assets at all times; and, c. Qualifying capital (Tier 1 Capital plus Tier 2 Capital) must be at least 10.0 percent of risk weighted assets at all times. Universal and commercial banks and their subsidiary banks and QBs are also required to maintain a Capital Conservation Buffer of 2.5 percent of risk-weighted assets, comprised of CET1 capital. ______ [37/] The Core Principles do not require a jurisdiction to comply with the capital adequacy regimes of Basel I, Basel II and/or Basel III. The Committee does not consider implementation of the Basel-based framework a prerequisite for compliance with the Core Principles, and compliance with one of the regimes is only required of those jurisdictions that have declared that they have voluntarily implemented it.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	The buffer is meant to promote the conservation of capital and build-up of adequate cushion that can be drawn down by banks to absorb losses during periods of financial and economic stress. The minimum requirements are higher than those prescribed by the Basel Committee. The CAR requirement is applied to all universal and commercial banks and their subsidiary banks, and quasi-banks on both solo and consolidated bases. <u>Qualifying components of capital</u> Qualifying capital consists of the sum of the following elements, net of required deductions: a. Tier 1 capital (going concern capital) is composed of: i. CET1; and ii. Additional Tier 1 (AT1) capital, and b. Tier 2 (gone-concern) capital. The definitions of qualifying capital are set out in Part II of Circular 781. <u>Risk coverage</u> Risks covered by the minimum capital requirements are credit, market and operational risks. *Credit risk*. The BSP only allows the use of the standardized approach for calculating capital charges for credit risk. *Market risk*. Both the standardized and internal model approaches may be used by banks to calculate capital charges for market risk. The BSP's 'Guidelines to incorporate market risk in the risk-based capital framework', which form an Appendix to Section 125 of the MORB, are broadly consistent with the market risk amendment issued in January 1996. The use of internal models is subject to the prior approval of the BSP, which will only be granted when a bank is able to comply with minimum quantitative and qualitative requirements [see also EC 5]. At present, there are only two banks with permission to compute market risk charges using this approach. *Operational risk*. Banks may use the basic indicator approach or the standardized approach for calculating the capital charge for operational risks, although the use of the standardized approach shall be conditional upon the explicit approval of the BSP. Universal and commercial banks under the basic indicator approach use an **α** equivalent to 15 percent, while stand-alone thrift, rural and cooperative banks use an **α** equivalent to 12 percent. The latter accounts for the fact that their exposures are mostly retail in nature. The allocation of capital for risks other than credit, market and operational risks is covered by the BSP's Pillar 2 guidelines—see EC2. To serve as a backstop measure to a bank's CAR, the BSP has adopted the Basel III leverage ratio framework. Circular 881 sets out the requirements of the framework, which applies to universal and commercial banks and their subsidiary banks and QBs. Such banks are

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	required to maintain a minimum leverage ratio of 5.0 percent, which is more conservative than the Basel standard. The capital regime for stand-alone thrift, rural and cooperative banks is a simplified Basel II framework, called "Basel 1.5". The implementing guidelines of Basel 1.5 were issued in Circular 688, which took effect on January 1, 2012. The minimum CAR for stand-alone thrift, rural and cooperative banks is 10 percent and qualifying capital consists of Tier 1 capital (core plus hybrid), and Tier 2 capital (supplementary), net of required deductions from capital. Pillar 1 requirements under Basel 1.5 cover capital charges for credit, market and operational risk. There is no requirement for a capital conservation buffer, and stand-alone thrift, rural and cooperative banks are not subject to the Basel III leverage ratio framework. There is an ongoing initiative to amend Basel 1.5 to align with the Basel III reforms on minimum capital requirements to improve the quality and loss capability of regulatory capital of covered banks. The proposals will require covered banks to meet minimum CET1 and Tier 1 capital of 6.0 percent and 7.5 percent, in addition to the minimum 10 percent requirement. The criteria for CET1, AT1 and Tier 2 capital to be eligible for inclusion as part of qualifying capital will also apply to stand-alone thrift, rural and cooperative banks. The policy proposal has been exposed to industry for comments and awaits MB approval. <u>Minimum Capitalization for Banks</u> Circular 854 sets out the minimum capitalization of banks. The minimum capitalisation varies by type of bank and by number of branches. See BCP 5. <u>Breach of thresholds</u> The BSP can place a bank under PCA when the Total CAR, Tier 1 Risk-Based Ratio, or Leverage Ratio (Total Capital/Total Assets) falls below 10.0, 6.0 and 5.0 percent, respectively. The relevant guidelines for PCA are set out in Circular 523—see BCP 11.
EC2	At least for internationally active banks,[38/] the definition of capital, the risk coverage, the method of calculation and thresholds for the prescribed requirements are not lower than those established in the applicable Basel standards.
Description and findings re EC2	The Philippine banks with limited overseas operations are all universal or commercial banks. They are all subject to the same regulatory framework, which is more conservative than applicable Basel standards. See EC1.
EC3	The supervisor has the power to impose a specific capital charge and/or limits on all material risk exposures, if warranted, including in respect of risks that the supervisor considers not to have been adequately transferred or mitigated through transactions (e.g., securitization transactions)[39/] entered into by the bank.

[38/] The Basel Capital Accord was designed to apply to internationally active banks, which must calculate and apply capital adequacy ratios on a consolidated basis, including subsidiaries undertaking banking and financial business. Jurisdictions adopting the Basel II and Basel III capital adequacy frameworks would apply such ratios on a fully consolidated basis to all internationally active banks and their holding companies; in addition, supervisors must test that banks are adequately capitalized on a stand-alone basis.
[39/] Reference documents: Enhancements to the Basel II framework, July 2009 and: International convergence of capital measurement and capital standards: a revised framework, comprehensive version, June 2006.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	Both on-balance sheet and off-balance sheet risks are included in the calculation of prescribed capital requirements.
Description and findings re EC3	Although S. 108 of its amended Charter provides the BSP with the power to vary individual banks' capital requirements to reflect their risk profile, it has not done so to date. It has, however, raised the risk weighting of certain higher risk assets above international standards, which has had the effect of raising the minimum capital ratios of banks holding those assets. For example, Circulars 468 and 469 imposed capital charges on banks' investments in securitization and structured products, respectively to serve as a disincentive for banks to hold too much of such instruments. The BSP introduced guidelines on Pillar 2 in Circular 639. These apply only to universal and commercial banks. The guidelines require such banks to have an ICAAP in place that takes account of risks not covered by Pillar 1, and sets out future capital plans, including a contingency plan for dealing with divergences and unexpected events (for example, raising additional capital, restricting business, or using risk mitigation techniques). A bank's Board and senior management are held responsible for ensuring that the bank maintains an appropriate level and quality of capital commensurate with all material risks to which it is exposed. Although the ICAAP has served to reinforce the linkages between a bank's risk management and capital adequacy, the SRP of the ICAAP does not result in the BSP setting individual capital requirements above the statutory minimum requirements for banks. The adequacy of a bank's capital is assessed in the CAMELS framework under SG 2009–21. The ICAAP and SRP inform the CAMELS assessment. The BSP is considering introducing a new regulatory framework—SAFR—to replace the CAMELS framework.[40/] It aims to be a more forward-looking supervisory approach, which embeds business model and impact analyses into the risk analysis of a bank. The BSP may wish to consider using the new SAFR model to apply capital ratios above the minimum requirement to individual banks to reflect their risk profile. BSP's prescribed calculation of capital requirements include both on-balance sheet and off-balance sheet risks.
EC4	The prescribed capital requirements reflect the risk profile and systemic importance of banks[41/] in the context of the markets and macroeconomic conditions in which they operate and constrain the build-up of leverage in banks and the banking sector. Laws and regulations in a particular jurisdiction may set higher overall capital adequacy standards than the applicable Basel requirements.
Description and findings re EC4	As noted in EC3, S. 108 of the amended BSP Charter gives the MB power to prescribe minimum risk-based capital adequacy ratios based on internationally accepted standards and with the power to alter those ratios whenever it deems necessary.

[40/] Approval for the implementation of SAFR in 2020 has been agreed subsequent to the BCP assessment.

[41/] In assessing the adequacy of a bank's capital levels in light of its risk profile, the supervisor critically focuses, among other things, on (a) the potential loss absorbency of the instruments included in the bank's capital base, (b) the appropriateness of risk weights as a proxy for the risk profile of its exposures, (c) the adequacy of provisions and reserves to cover loss expected on its exposures and (d) the quality of its risk management and controls. Consequently, capital requirements may vary from bank to bank to ensure that each bank is operating with the appropriate level of capital to support the risks it is running and the risks it poses.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	In addition to the minimum capital requirements that apply to all banks in the Philippines (see EC1), the BSP requires those banks assessed as D-SIBs to meet higher minimum capital requirements to reflect their systemic importance. Circular 856 sets out the regulatory framework for D-SIBs. The aim of the policy is to reduce the probability of failure of D-SIBs by increasing their going-concern loss absorbency and to reduce the extent or impact of failure of D-SIBs on the domestic/real economy. Full implementation of the policy took effect on January 1, 2019. The systemic importance of a bank is assessed in relation to the impact of its failure on the domestic economy using an indicator-based measurement approach. The specific factors considered in the determination of a D-SIB are (a) size; (b) interconnectedness; (c) substitutability/financial institution infrastructure; and (d) complexity. Ten indicators related to these categories are used to identify D-SIBs. Banks that have a score produced by the indicator-based measurement approach that exceeds a cutoff level determined using cluster analysis are classified as D-SIBs. The BSP undertakes the assessment annually. In line with this framework BSP has identified D-SIBs in the Philippines. These are allocated to one of two 'buckets' depending upon their degree of systemic importance. Banks allocated to 'bucket 1' attract an additional capital requirement of 1.5 percent and those allocated to 'bucket 2' attract an additional capital requirement of 2.5 percent. In addition to the D-SIB higher loss absorbency requirement, the BSP also requires all universal banks and commercial banks and their subsidiary banks and QBs to adopt a capital conservation buffer (CCB) of 2.5 percent of risk weighted assets comprised of CET1 capital and, through Circular 1024, the BSP recently introduced the Basel III countercyclical capital buffer (CCyB). The CCyB is initially set at 0 percent but the MB may increase the same to a rate not to exceed 2.5 percent when systemic conditions warrant.
EC5	The use of banks' internal assessments of risk as inputs to the calculation of regulatory capital is approved by the supervisor. If the supervisor approves such use: (a) such assessments adhere to rigorous qualifying standards; (b) any cessation of such use, or any material modification of the bank's processes and models for producing such internal assessments, are subject to the approval of the supervisor; (c) the supervisor has the capacity to evaluate a bank's internal assessment process in order to determine that the relevant qualifying standards are met and that the bank's internal assessments can be relied upon as a reasonable reflection of the risks undertaken; (d) the supervisor has the power to impose conditions on its approvals if the supervisor considers it prudent to do so; and, (e) if a bank does not continue to meet the qualifying standards or the conditions imposed by the supervisor on an ongoing basis, the supervisor has the power to revoke its approval.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	Annex A of Appendix 42 of the MORB sets out the requirements for the use of internal models to measure market risk. The BSP has not issued any regulations or guidance in respect of the use of internal models to measure credit risk. There are foreign-owned banks that were granted permission from the BSP to use internal models to compute their market risk capital requirement shortly after the BSP allowed banks to do so. The local risk models are driven-off the banks' group models, as approved by the home regulators. a) Qualifying standards The BSP only grants approval for the use of models if, in general, the following minimum requirements are met: • The bank's risk management system is conceptually sound and is implemented with integrity; • The bank has a sufficient number of staff skilled in the use of sophisticated models not only in the trading area but also in the risk control, audit, and if necessary, back office areas; • The bank's models have a proven track record of reasonable accuracy in measuring risk, and • The bank regularly conducts stress tests as required in existing regulation. The detailed qualifying standards for the use of an internal model for market risk are set out in Annex A of Appendix 42 of the MORB. b) Cessation of use and modifications Banks are required to inform the BSP of any material change in the models, including changes in the methodology or scope of products covered, to determine whether the models are still acceptable for calculating capital requirements. The models are subject to periodic (at least annual) on-site assessment to ensure that they remain compliant with the BSP's qualitative and quantitative standards, non-compliance with which may cause the BSP to withdraw approval. Annex A of Circular 360 provides that a bank cannot revert to measuring capital charges according to the standardized methodology once it has commenced using the internal model approach, unless the BSP withdraws approval for that model. c) Supervisor's capacity to evaluate a bank's internal assessment process The BSP's capacity to evaluate internal risk models is adequate to meet current needs but will require strengthening as the demands of banks' increase. See BCP 15. Expertise is developed primarily through formal academic studies and training. Consideration should be given to seconding staff to market risk functions in private banks to develop their expertise and to recruitment from the market of individuals with relevant expertise. d) BSP's power to impose conditions on approvals

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	Annex A of Circular 360 allows the BSP to attach certain conditions to the approval of a bank's use of its internal models for computing market risk capital charges. These have been adopted from international standards. The conditions are as follows: • The BSP can set a multiplication factor on the basis of its assessment of the quality of the bank's risk management system subject to an absolute minimum of 3. Banks will be required to add to this factor a "plus" directly related to the ex-post performance of the model (to be determined on a quarterly basis), thereby introducing a built-in positive incentive to maintain the predictive quality of the model. The plus will range from 0 to 1 based on the number of back-testing exceptions. • Banks using models will be subject to a separate capital charge to cover the specific risk of interest rate-related instruments and equity securities as defined in the standardized approach to the extent that this risk is not incorporated into their models. However, for banks using models, the total specific risk charge applied to interest rate-related instruments or to equities should in no case be less than half the specific risk charges calculated according to the standardized methodology. • Banks may, on a transitional basis, be allowed to use a combination of the standardized approach and the models approach to measure their market risk, provided any such "partial" model shall cover a complete risk category (e.g., interest rate risk or foreign exchange risk). Banks may not modify the combination of the two approaches they use without justifying to the BSP that they have a good reason for doing so. • The BSP may require a period of initial monitoring and live testing of a bank's internal model before it is used for supervisory capital purposes. e) Revocation of approval See *(b)* above.
EC6	The supervisor has the power to require banks to adopt a forward-looking approach to capital management (including the conduct of appropriate stress testing).[42/] The supervisor has the power to require banks: (a) to set capital levels and manage available capital in anticipation of possible events or changes in market conditions that could have an adverse effect; and, (b) to have in place feasible contingency arrangements to maintain or strengthen capital positions in times of stress, as appropriate in the light of the risk profile and systemic importance of the bank.
Description and findings re EC6	Circular 639 requires banks to have an explicit, Board-approved capital plan, which states the bank's objectives, the time horizon for achieving those objectives, how the banks will comply with future capital requirements and, in broad terms, the capital planning process and the responsibilities for that process. The capital targets should be consistent with the bank's risk profile, operating environment, and business plan, but other considerations may be taken into account in deciding how much capital to hold, such as external rating goals, market reputation and strategic goals.

[42/] "Stress testing" comprises a range of activities from simple sensitivity analysis to more complex scenario analyses and reverses stress testing.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	If these other considerations are included in the process, banks must be able to show the BSP how they influenced their decisions concerning the amount of capital to hold. The capital plan should also set out any relevant limits related to capital, and a general contingency plan for dealing with divergences and unexpected events (for example, raising additional capital, restricting business, or using risk mitigation techniques). In addition, banks should conduct appropriate scenario/stress tests which take into account, for example, the risks specific to the particular stage of the business cycle. Banks should analyze the impact that new legislation/regulation, actions of competitors or other factors may have on their performance, in order to determine what changes in the environment they could sustain. Supervisors review the assumptions underlying the capital plan, stress testing and contingency plans in the SRP of banks' ICAAPs, and through on-site examinations for those banks not required to submit an ICAAP. There was evidence of effective reviews being undertaken and of challenge to the capital plans submitted by banks.
Assessment of Principle 16	Largely compliant
Comments	An appropriate capital framework is in place for the major banks in the Philippine banking sector, with minimum capital ratios and a leverage ratio set at more conservative levels than applicable Basel standards. The capital framework for stand-alone rural, thrift and cooperative banks is in the process of being revised to align more closely with Basel III. The BSP does not directly vary individual banks' capital requirements to reflect their risk profile but has adjusted certain asset risk weights and has introduced a higher capital regime for D-SIBs. Recommendations: • Set individual capital ratios for banks based on their risk profile as part of the SRP process. • Introduce a simplified ICAAP for the rural, thrift and cooperative banks.
Principle 17	**Credit risk.**[43/] The supervisor determines that banks have an adequate credit risk management process that takes into account their risk appetite, risk profile and market and macroeconomic conditions. This includes prudent policies and processes to identify, measure, evaluate, monitor, report and control or mitigate credit risk[44/] (including counterparty credit risk)[45/] on a timely basis. The full credit lifecycle is covered including credit underwriting, credit evaluation, and the ongoing management of the bank's loan and investment portfolios.
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to have appropriate credit risk management processes that provide a comprehensive bank-wide view of credit risk exposures. The supervisor determines that the processes are consistent with the risk appetite, risk profile, systemic importance and capital strength of the bank, take into account market and macroeconomic conditions and result in prudent standards of credit underwriting, evaluation, administration and monitoring.

[43/] Principle 17 covers the evaluation of assets in greater detail; Principle 18 covers the management of problem assets.

[44/] Credit risk may result from the following: on-balance sheet and off-balance sheet exposures, including loans and advances, investments, inter-bank lending, derivative transactions, securities financing transactions and trading activities.

[45/] Counterparty credit risk includes credit risk exposures arising from OTC derivative and other financial instruments.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Circular No. 855 outlines BSP's expectations on bank's credit risk management policies and processes in: a) establishing an appropriate credit risk environment; b) operating under a sound credit granting process; c) maintaining appropriate credit administration, measurement, monitoring and control processes over credit risk. Bank's guidelines must incorporate such factors as the major sources of credit risk exposures posed by assets, liabilities and off-balance sheet exposures. The Board is responsible for setting the credit risk appetite (including limits) and risk profile as well regularly reviewing management's ability to operate within these approved limits. For systemic banks, the Credit Oversight Committee is expected to oversee the credit risk management function in universal and commercial banks. It is noted that BSP does not have guidance in place to communicate its expectations to banks regarding the use and the approval process for the use of internal credit risk models.
EC2	The supervisor determines that a bank's Board approves, and regularly reviews, the credit risk management strategy and significant policies and processes for assuming,[46/] identifying, measuring, evaluating, monitoring, reporting and controlling or mitigating credit risk (including counterparty credit risk and associated potential future exposure) and that these are consistent with the risk appetite set by the Board. The supervisor also determines that senior management implements the credit risk strategy approved by the Board and develops the aforementioned policies and processes.
Description and findings re EC2	Circular No. 855 stipulates that the Board is ultimately responsible for a) ensuring that the bank's credit risk appetite, limits and overall credit risk management system (commensurate with size, complexity and scope of operations of a bank) provides for adequate policies, procedures and effective processes to identify, measure, monitor and control all credit risks inherent in a bank's products and activities, both at the individual and portfolio level on a consistent and continuing basis and b) that an independent assessment of the system is periodically performed, the results of which shall be reported to it or to a Board-level committee for appropriate action. Circular No. 855 stipulates that senior management of banks are responsible for: (a) ensuring that the credit risk-taking activities are aligned with the credit risk strategy approved by the Board; (b) developing and implementing a bank's credit policies and procedures; (c) ensuring that policies are adhered to by all levels of the organization. BSP's onsite examination framework annually reviews, on a risk based approach, whether a bank's credit risk management governance and credit process align with Board approved credit risk strategies, policies, risk limits as well as making a determination whether a bank can differentiate risks across individual/group credits, demonstrate adequate reporting up to the Board/Risk Oversight Committee and identify deteriorating credit exposures on a timely basis and act promptly to correct such deficiencies.
EC3	The supervisor requires, and regularly determines, that such policies and processes establish an appropriate and properly controlled credit risk environment, including: (a) a well-documented and effectively implemented strategy and sound policies and processes for assuming credit risk, without undue reliance on external credit assessments;

[46/] "Assuming" includes the assumption of all types of risk that give rise to credit risk, including credit risk or counterparty risk associated with various financial instruments.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	(b) well defined criteria and policies and processes for approving new exposures (including prudent underwriting standards) as well as for renewing and refinancing existing exposures, and identifying the appropriate approval authority for the size and complexity of the exposures; (c) effective credit administration policies and processes, including continued analysis of a borrower's ability and willingness to repay under the terms of the debt (including review of the performance of underlying assets in the case of securitization exposures); monitoring of documentation, legal covenants, contractual requirements, collateral and other forms of credit risk mitigation; and an appropriate asset grading or classification system; (d) effective information systems for accurate and timely identification, aggregation and reporting of credit risk exposures to the bank's Board and senior management on an ongoing basis; (e) prudent and appropriate credit limits, consistent with the bank's risk appetite, risk profile and capital strength, which are understood by, and regularly communicated to, relevant staff; (f) exception tracking and reporting processes that ensure prompt action at the appropriate level of the bank's senior management or Board where necessary; and, (g) effective controls (including in respect of the quality, reliability and relevancy of data and in respect of validation procedures) around the use of models to identify and measure credit risk and set limits.
Description and findings re EC3	Circular No. 855 stipulates that BSP requires (and assesses during its on-site annual examinations) a bank's adherence to the following: (a) Boards establish sound, comprehensive and clearly defined credit policies, processes and procedures adequate for the size, complexity and scope of the bank's operations; (b) approval process for new credits as well as the amendment, renewal and refinancing of existing credit exposures shall be aligned with credit risk management credit policies/pre-approved limits. Renewal, extensions or refinancing shall be granted upon the re-establishment of the creditworthiness of the obligor using the same credit-granting criteria and evaluation methods. (c) sound credit-granting criteria and underwriting standards where the obligor or counterparty's creditworthiness are assessed without undue reliance on external credit assessments. Examiners also focus on a bank's cash flow analysis, primary source/proof of income and overall indebtedness, together with integrity of obligor as well as legal capacity to assume the liability. Further, examiners review a bank's valuation of collateral including physical collateral or acceptability/enforceability of various forms of financial guarantees (legal covenants and contractual obligations). For more complex credit risk exposures (e.g., asset securitization, credit derivatives, credit-linked notes, etc.) banks should have a more sophisticated tool for identifying, measuring and continually controlling credit/country and transfer risk exposures. (d) + (e) assessing the strength of a bank's MIS including the ability to segment the tracking of the portfolio into diverse categories and reporting of credit risk exposures to the bank's

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	Board against pre-approved credit limits, including reporting and monitoring of large exposures, credit risk concentrations and RPTs. (f) exceptions or excesses in internal limits are monitored and escalated to higher authorities within the bank. (g) the reasonableness and effectiveness of the parameters of the credit scoring model/methodology is assessed. Validation of credit scoring models in measuring credit risk for pools of loans that are similar in purpose, risk characteristics (typically retails loans including housing loans, car or auto loans, etc.) is also assessed for consistent and meaningful results to ensure that the realized risk measures are within an expected range. Note that BSP will need to formalize its expectations and assessment methodology for credit model risk management purposes on a go forward basis. See BCP18 for more detail on BSP's requirement to strengthen credit risk model validation/approval with respect to expected loss provisioning methodology in accordance with PFRS accounting practices.
EC4	The supervisor determines that banks have policies and processes to monitor the total indebtedness of entities to which they extend credit and any risk factors that may result in default including significant unhedged foreign exchange risk.
Description and findings re EC4	S. 143 of the MORB requires banks to keep informed of the current financial condition of borrowers and entities. During on-site examinations, bank supervisors evaluate adequacy and appropriateness of factors considered and documented in approving credits which include, among others, sources of repayments, repayment history and current capacity to repay.
EC5	The supervisor requires that banks make credit decisions free of conflicts of interest and on an arm's length basis.
Description and findings re EC5	Circular No. 855 outlines BSP's requirements of banks to enter into all transactions with related parties free of conflicts of interest and on an arm's length basis. See BCP 20 for more detail.
EC6	The supervisor requires that the credit policy prescribes that major credit risk exposures exceeding a certain amount or percentage of the bank's capital are to be decided by the bank's Board or senior management. The same applies to credit risk exposures that are especially risky or otherwise not in line with the mainstream of the bank's activities.
Description and findings re EC6	Circular No. 855 outlines BSP's expectations of banks' credit policies regarding the underwriting and tracking of large exposures (measured on an individual single borrower limit and aggregate connected counterparty limit) and RPTs against Board approved limits. For larger banks, management's requirement to report to the Risk Oversight Committee of the Board provides the requirement for a risk management framework and governance for such large/risky credit exposures. See BCP 19 and 20 for more detail.
EC7	The supervisor has full access to information in the credit and investment portfolios and to the bank officers involved in assuming, managing, controlling and reporting on credit risk.
Description and findings re EC7	BSP's on-site annual examination of banks' credit risk management provides BSP with full access to information on a bank's credit and investment portfolios which include the opportunity to challenge bank officers who are directly involved in assuming, managing, controlling and reporting on credit risk. Assessors noted BSP's on-site examiners ability to require banks to make adjustments to certain credit exposures treatment if and when deficiencies were identified. This was noted in the ROE documents of D-SIBs.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC8	The supervisor requires banks to include their credit risk exposures into their stress testing programs for risk management purposes.
Description and findings re EC8	S.143 of the MORB stipulates BSP's requirement that banks conduct stress testing and scenario analysis of its credit portfolio, which include the assessment of impacts of off-balance sheet exposures both at the individual and group levels to assess the impact of market dislocations and changes in economic conditions or key factors on its profile, earnings and capital levels. Circular No. 989 provides BSP's guidelines on banks' conduct of stress testing exercises, which should be linked to a bank's risk appetite, business strategies, as well as capital and business continuality and liquidity plans as well as how these stress tests should link to the bank's ICAAP. Specifically, the stress testing requirements stipulate that banks must consider credit risk implications through the increase in default probabilities and worsening of credit spreads attributed to economic downturns and significant market shocks that will affect the entire classes of counterparties or credits. BSP also requires banks to conduct an annual REST for real estate exposures for universal, commercial and thrift banks on a solo and consolidated basis.
Assessment of Principle 17	Largely Compliant
Comment	BSP's current regulations pertaining to banks' credit risk management policies and processes and its on-site supervision framework appear to be adequate, except for the lack of guidance in respect of the management/use of internal models to measure credit risk. Given the pace of growth in certain sectors of the banking industry, it will be essential for the BSP to establish a concentrated area of technical credit expertise to keep pace with the potential increase in banks' use of more complicated credit facilities as well as the utilization of more sophisticated credit models (see BCP 18 for more details). Thematic/horizontal credit reviews across the larger banks focusing on credit practices will be important as BSP moves to a more risk based supervisory approach. Recommendations: • Develop guidance on the management/use of internal models to measure credit risk; • Establish a concentrated area of credit expertise; and • Conduct thematic/horizontal credit reviews across larger FIs focusing on bank's credit risk management practices.
Principle 18	**Problem assets, provisions and reserves.**[47/] The supervisor determines that banks have adequate policies and processes for the early identification and management of problem assets, and the maintenance of adequate provisions and reserves.[48/]
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to formulate policies and processes for identifying and managing problem assets. In addition, laws, regulations or the supervisor require regular review by banks of their problem assets (at an individual level or at a portfolio level for assets with homogenous characteristics) and asset classification, provisioning and write-offs.

[47/] Principle 17 covers the evaluation of assets in greater detail; Principle 18 covers the management of problem assets.

[48/] Reserves for the purposes of this Principle are "below the line" non-distributable appropriations of profit required by a supervisor in addition to provisions ("above the line" charges to profit).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Circular No. 855 sets out BSP's expectations of banks' regular review of loans and other credit accommodations at the individual and portfolio level. Banks are expected to implement an independent and objective credit review process to determine that credits are granted in accordance with the bank's policies; assess the overall asset quality, including appropriateness of classification and adequacy of loan-loss provisioning; determine trends; and identify problems (e.g., risk concentration, risk migration, deficiencies in credit administration and monitoring processes). BSP defines broadly the regulatory asset classification of pass, especially mention, substandard, doubtful and loss categories, and banks are permitted to use their own asset classification systems so long as there is a clear mapping back to the regulatory asset classification categories. S. 49 of the GBL gives the MB the powers to determine the specific period for purposes of classifying bad debts, fix the amount of reserves for bad debts, doubtful accounts or other contingencies and issues regulations on the writing off of loans, etc. BSP permits banks to assess loans on an individual basis (banks determine threshold for materiality for significant exposures) and on a portfolio basis (making use of credit risk assessment models or methodologies for estimating expected future cash flows including credit risk grading processes, which may combine several of the following: loan type, product type, market segment, estimated default probabilities or credit risk grading and classification, collateral type, geographical location and past-due status). Assessors noted that the SEC–Oversight Assurance Review body and the BSP plan to develop additional regulations and guidance pertaining to a bank's methodology/modelling of the impairment of expected credit losses.
EC2	The supervisor determines the adequacy of a bank's policies and processes for grading and classifying its assets and establishing appropriate and robust provisioning levels. The reviews supporting the supervisor's opinion may be conducted by external experts, with the supervisor reviewing the work of the external experts to determine the adequacy of the bank's policies and processes
Description and findings re EC2	Circular No. 1011 sets out BSP's expectations for banks to adopt the PFRS which are generally in line with IFRS 9 International Accounting Standard effective January 1, 2018. This regulation specifies that banks shall recognize adequate and timely allowance for credit losses at all times and that banks shall adopt the principles provided under the Enhanced Standards on Credit Risk Management under S. 178/4178Q/4197N of the MORB/MORNBFI. BSP however has required all banks to adopt PFRS (except smaller less sophisticated entities—see next paragraph), and in addition, BSP requires all banks to maintain a general allowance of 100bp to ensure a minimum floor for loan loss provisioning is maintained across the banking sector. Appendix 15/Q-10 of the MORB/MORNBFI stipulates that where the credit operations that may not economically justify a more sophisticated loan loss estimation methodology, broken down by unsecured loans (classification of loss at >90 days) versus secured loans where classification and provisioning levels vary depending on the type of collateral (e.g., "other classified collateral" and "real estate collateral" are recognized and therefore provisioning levels for greater than 90 days and up to 5 years allow for less than 100 percent (e.g., 91–120 days in arrears with provisioning levels of 25 percent/15 percent for "other classified collateral/secured by real estate; 121–360 days of

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	50 percent/25 percent and 361 days–5 years of 100 percent/50 percent provisioning levels accordingly). Assessors noted that this provisioning methodology does not align with PFRS and should be tweaked to provide greater levels of required provisioning after a prolonged "loss classification." Assessors acknowledged that the banks utilizing this provisioning methodology represent less than 3 percent of the total assets of the banking industry. BSP's on-site supervision framework includes a review of a bank's policies and processes for grading and classifying its assets as well as how banks establish appropriate and robust provisioning levels. Examiners sample both individual problem assets as well as review the strength of provisioning models and banks' own independent validation assessments. Further, the BSP places reliance on both the internal auditor's independent review of provisioning methodology/models as well as the work of the external auditors if the BSP has established sufficient basis to do so.
EC3	The supervisor determines that the bank's system for classification and provisioning takes into account off-balance sheet exposures.[49/]
Description and findings re EC3	S. 9 of Attachment 2 of Circular No. 1011 provides the rules on recognition and presentation of expected credit losses of off-balance sheet exposures in relation to the adoption of PFRS 9 Financial Instruments Impairment. BSP on-site examiners review banks to ensure that their system for classification and provisioning takes into account off-balance sheet exposures.
EC4	The supervisor determines that banks have appropriate policies and processes to ensure that provisions and write-offs are timely and reflect realistic repayment and recovery expectations, taking into account market and macroeconomic conditions.
Description and findings re EC4	Circular No. 855 requires banks to have policies and processes to ensure provisions are timely and that estimated credit losses shall reflect consideration of the bank's historical net charge-off rate of the groups, adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans in these groups as of the evaluation date, and applied consistently over time. Assessors noted that the BSP's regulations do not specify banks to have a maximum period for write-off of problem assets (i.e. so long as banks have 100 percent provisioning in place for such assets) and that there is no undue delay in implementing write-offs. Banks are, however, required to write-off problem credits, regardless of amount, against the collective allowance for credit losses or current operations within a reasonable period of as soon as problem credits are determined to be worthless as defined in the bank's written policies. However, problem credits to DOSRI shall be written off only upon prior approval of the MB. Timeliness of write-offs for smaller banks using the basic methodology should be re-assessed (see EC 2).
EC5	The supervisor determines that banks have appropriate policies and processes, and organizational resources for the early identification of deteriorating assets, for ongoing oversight of problem assets, and for collecting on past due obligations. For portfolios of credit exposures with homogeneous characteristics, the exposures are classified when payments are contractually in arrears for a minimum number of days (e.g., 30, 60, 90 days). The supervisor tests banks' treatment of assets with a view to identifying any material circumvention of the classification and provisioning standards (e.g., rescheduling, refinancing or reclassification of loans).

[49/] It is recognized that there are two different types of off-balance sheet exposures: those that can be unilaterally cancelled by the bank (based on contractual arrangements and therefore may not be subject to provisioning), and those that cannot be unilaterally cancelled.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	BSP's on-site supervision annually assesses a bank's policies and processes in conjunction with the adequacy of its organizational resources focused on problem loan workout, including the collection on past due obligations. Supervisors also assess a bank's treatment of asset classification, aging and provisioning levels to identify any material circumvention.
EC6	The supervisor obtains information on a regular basis, and in relevant detail, or has full access to information concerning the classification of assets and provisioning. The supervisor requires banks to have adequate documentation to support their classification and provisioning levels.
Description and findings re EC6	BSP's FRP requires banks to submit loan data on a quarterly basis that reflects the classification of assets, aging of arrears and provisioning on both a solo and consolidated basis. Supervisors assess the adequacy of banks' documentation during on-site examinations.
EC7	The supervisor assesses whether the classification of the assets and the provisioning is adequate for prudential purposes. If asset classifications are inaccurate or provisions are deemed to be inadequate for prudential purposes (e.g., if the supervisor considers existing or anticipated deterioration in asset quality to be of concern or if the provisions do not fully reflect losses expected to be incurred), the supervisor has the power to require the bank to adjust its classifications of individual assets, increase its levels of provisioning, reserves or capital and, if necessary, impose other remedial measures.
Description and findings re EC7	During on-site examinations, BSP flags banks on grading and provisioning issues and materially inadequate or understated provisioning. BSP has the power to require a bank to adjust its classifications on individual assets, increase its levels of provisioning, reserves or capital and, if necessary, impose other remedial measures such as issuing directives or letters of commitment or sanctions to address deficiencies (S. 49 of the GBL; Circular No. 855).
EC8	The supervisor requires banks to have appropriate mechanisms in place for regularly assessing the value of risk mitigants, including guarantees, credit derivatives and collateral. The valuation of collateral reflects the net realizable value, taking into account prevailing market conditions.
Description and findings re EC8	Circular No. 855 requires banks to have adequate policies regarding the acceptability of various forms of credit mitigants and appropriate collateral value limits; procedures for assessing the value of the physical collateral and availability of financial guarantees; and a process to ensure that these are, and continue to be, enforceable, realizable and marketable (net realizable value taking into consideration any factors affecting the diminished recoverability of the credit). In the case of guarantees, the level of coverage being provided in relation to the credit quality, financial and legal capacity of the guarantor must be evaluated. Such considerations are incorporated into the loan agreement.
EC9	Laws, regulations or the supervisor establish criteria for assets to be: (a) identified as a problem asset (e.g., a loan is identified as a problem asset when there is reason to believe that all amounts due, including principal and interest, will not be collected in accordance with the contractual terms of the loan agreement); and (b) reclassified as performing (e.g., a loan is reclassified as performing when all arrears have been cleared and the loan has been brought fully current, repayments have been made in a timely manner over a continuous repayment period and continued collection, in accordance with the contractual terms, is expected).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC9	Circular No. 855 outlines requirements to identify a problem asset(s), both by either making use of more sophisticated credit classification modeling systems or where the credit operations that may not economically justify a more sophisticated loan loss classification and estimation methodology (see EC 2 for more detail). Further, NPLs, investments, receivables or any financial asset (and/or any replacement loan) should remain classified as such until (a) there is sufficient evidence to support that full collection of principal and interests is probable and payments of interest and/or principal are received for at least six (6) months; or (b) written-off. Restructured loans should be considered non-performing unless prior to restructuring, the loans were categorized as performing. Moreover, loans, investments, receivables, or any financial asset should be considered non-performing, even without any missed contractual payments, when it is considered impaired under existing accounting standards, classified as doubtful or loss, in litigation, and/or there is evidence that full repayment of principal and interest is unlikely without foreclosure of collateral, if any. All other loans, even if not considered impaired, shall be considered non-performing if any principal and/or interest are unpaid for more than 90 days from contractual due date, or accrued interests for more than ninety (90) days have been capitalized, refinanced, or delayed by agreement. BSP would not permit reclassification of a loan as performing unless all arrears (both principle and interest) have been paid. Further, restructured loans may not be reclassified to performing until demonstrated by 6 months performing.
EC10	The supervisor determines that the bank's Board obtains timely and appropriate information on the condition of the bank's asset portfolio, including classification of assets, the level of provisions and reserves and major problem assets. The information includes, at a minimum, summary results of the latest asset review process, comparative trends in the overall quality of problem assets, and measurements of existing or anticipated deterioration in asset quality and losses expected to be incurred.
Description and findings re EC10	BSP assesses the strength of a bank's Board oversight with regards to the quality of asset classification and the level of provisioning and reserves on both major problem assets and groups of assets. S. 132 of the MORB specifies that universal, commercial and thrift banks have Risk Oversight Committees of the Board that are responsible for the development and oversight of the overall risk management program for the bank, including the problem asset management framework that should be appropriate for the size, complexity and scope of the operations of the bank. On-site examiners assess the strength of Board/Committee reporting, including the adequacy of a bank's reporting of existing or anticipated deterioration in asset quality and loses expected to be incurred as well as the proactive actions Boards should be taking to address these risks.
EC11	The supervisor requires that valuation, classification and provisioning, at least for significant exposures, are conducted on an individual item basis. For this purpose, supervisors require banks to set an appropriate threshold for the purpose of identifying significant exposures and to regularly review the level of the threshold.
Description and findings re EC11	Circular No. 855 requires a bank's policies on loan valuation, classification and provisioning requirements to establish and assess on-going relevance of materiality thresholds for significant credit exposures.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC12	The supervisor regularly assesses any trends and concentrations in risk and risk build-up across the banking sector in relation to banks' problem assets and takes into account any observed concentration in the risk mitigation strategies adopted by banks and the potential effect on the efficacy of the mitigant in reducing loss. The supervisor considers the adequacy of provisions and reserves at the bank and banking system level in the light of this assessment.
Description and findings re EC12	BSP regularly utilizes FRP data, including the data collected to run the REST uniform stress testing to monitor banking sector status of loan portfolios, NPLs, as well as the adequacy of reserves and impairment provisions. Specifically, the BSRA submitted by the SPRD to the MB on a quarterly basis makes use of this statistical information collected through the FRP, REST and the ICAAP and provides a good overview of BSP's ability to identifying emerging vulnerability and risks confronting the banking sector and their potential impact on the system's overall safety and soundness. The BSRA also highlights supervisory actions taken by the FSS as well as the mitigating measures undertaken by the banks concerned. The BRSA also recommends policy measures that will address emerging risks and vulnerabilities. Assessors noted that this type of report should be shared with the FSCC on a regular basis to facilitate a discussion amongst all domestic regulatory agencies on the current and emerging risks in the banking sector that could negatively impact the health of the overall Philippines financial system. It is important to note that the BSP has the authority to implement prudential requirements across all banks if macroeconomic conditions warrant such action.
Assessment of Principle 18	Compliant
Comments	BSP's regulations pertaining to banks' policies and processes for the early identification and management of problem assets and the requirement to maintain adequate provisions and reserves are considered adequate. Assessors noted the strength of BSP's on-site supervision framework in the assessment of a bank's adequacy in the management of problem assets. The BSP should consider changing its loan provisioning guidance for less sophisticated banks pertaining to secured loans (e.g., reconsider the adequacy of loan loss provisioning based on type of collateral and determination of acceptable write-off periods). Further, BSP should ensure its guidance pertaining to BSP's expectations on banks' methodology/modelling of the impairment of expected credit losses is in line with proposed SEC guidance. Recommendations: • Change loan loss provisioning guidance for less sophisticated banks pertaining to secured loans (collateral valuation, maximum write-off periods); and • Align BSP's expectations on banks' methodology/modelling of the impairment of expected credit losses with the SEC proposed guidance.
Principle 19	**Concentration risk and large exposure limits.** The supervisor determines that banks have adequate policies and processes to identify, measure, evaluate, monitor, report and control or mitigate concentrations of risk on a timely basis. Supervisors set prudential limits to restrict bank exposures to single counterparties or groups of connected counterparties.[50/]

[50/] Connected counterparties may include natural persons as well as a group of companies related financially or by common ownership, management or any combination thereof.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to have policies and processes that provide a comprehensive bank-wide view of significant sources of concentration risk.[51/] Exposures arising from off-balance sheet as well as on-balance sheet items and from contingent liabilities are captured.
Description and findings re EC1	S. 143 of the MORB sets out BSP's expectations regarding a bank's sound credit risk management practices, including credit limits, large exposures and credit risk concentrations. S. 143 of the MORB sets out the requirement for banks to: (a) identify, review, manage and report large exposures and concentration risks; (b) segment its portfolio by borrower/counterparties or loan category, group of connected borrowers/counterparties, individual industry sectors, geographic regions or countries, loan structure, collateral and tenor and various types of investments, including both on-balance sheet, as well as off-balance sheet transactions/exposures; c) define limit structures for each of the foregoing categories and d) monitor adherence and exceptions to bank threshold limits. S. 361–363 of the MORB defines large exposures (LEs) and connected counterparties (see EC5 and EC6 below for more detail). Current regulations however do not stipulate the requirement to calculate a single borrower's limit on a consolidated basis as well as an aggregate large exposure limit for a counterparty or group of connected counterparties on both solo and consolidated basis. See EC 6 for a description of BSP's draft exposure on the amendments to the prudential guidelines on large exposures that is expected to address this deficiency once finalized.
EC2	The supervisor determines that a bank's information systems identify and aggregate on a timely basis, and facilitate active management of, exposures creating risk concentrations and large exposure[52/] to single counterparties or groups of connected counterparties.
Description and findings re EC2	S. 144 of the MORB outlines BSP's expectations with respect to a bank's credit risk management information and reporting systems. S. 143 of the MORB states that banks are expected to render accurate, reliable and timely information and reports, including the timely identification and monitoring of credit risk concentrations, exposures approaching risk limits and exceptions and overrides to the limits, aggregate credit exposures and counterparties as well as to a group of accounts under common ownership or control. BSP's on-site examination framework annually examines the strength/robustness, accuracy and capacity of banks' MIS regarding the identification and aggregation of credit exposures. Smaller banks' MIS are generally less sophisticated and examined less frequently than the larger banks (see EC3 for more detail).

[51/] This includes credit concentrations through exposure to: single counterparties and groups of connected counterparties both direct and indirect (such as through exposure to collateral or to credit protection provided by a single counterparty), counterparties in the same industry, economic sector or geographic region and counterparties whose financial performance is dependent on the same activity or commodity as well as off-balance sheet exposures (including guarantees and other commitments) and also market and other risk concentrations where a bank is overly exposed to particular asset classes, products, collateral, or currencies.

[52/] The measure of credit exposure, in the context of large exposures to single counterparties and groups of connected counterparties, should reflect the maximum possible loss from their failure (i.e., it should encompass actual claims and potential claims as well as contingent liabilities). The risk weighting concept adopted in the Basel capital standards should not be used in measuring credit exposure for this purpose as the relevant risk weights were devised as a measure of credit risk on a basket basis and their use for measuring credit concentrations could significantly underestimate potential losses (see "*Measuring and controlling large credit exposures*, January 1991).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	The supervisor determines that a bank's risk management policies and processes establish thresholds for acceptable concentrations of risk, reflecting the bank's risk appetite, risk profile and capital strength, which are understood by, and regularly communicated to, relevant staff. The supervisor also determines that the bank's policies and processes require all material concentrations to be regularly reviewed and reported to the bank's Board.
Description and findings re EC3	BSP's annual on-site examination conducts an assessment of banks' risk management framework, including a review of credit risk policies and procedures pertaining to concentrations and large exposures, strength of MIS (aggregation capability, tracking of/grouping counterparty exposures, reporting), and adequacy of stress testing procedures. BSP examiners assess a Board's regular review of acceptable thresholds established in conjunction with the bank's risk appetite framework and management's conduct in respecting these limits. Assessors noted strong challenge capabilities by supervisory examiners when issues with weaknesses in the framework were identified (e.g., BSP issuing directives to banks to improve tracking/reporting of large exposures of connected borrowers).
EC4	The supervisor regularly obtains information that enables concentrations within a bank's portfolio, including sectoral, geographical and currency exposures, to be reviewed.
Description and findings re EC4	BSP's FRP generally groups transactions into the different counterparties (both residents and non-residents), currencies (peso and foreign accounts) and geographic region/country classification. The supporting schedules to the FRP (Schedule 11—Loans and Receivables) collect data by industry, type of loan, and status of performing/provisioning and are provided on a quarterly basis. In addition, for the purposes of REST, BSP collects real estate exposure information on connected borrowers. Assessors noted this information is not necessarily utilized by the supervisors beyond REST purposes. See EC 7 for more detail. Note: S. 174 of the MORB requires banks to disclose significant credit exposures where concentrations to industry/economy sectors exceeds 30 percent of the total loan portfolio. (Note that there is an ongoing policy initiative to amend the regulations on the required disclosure which will extend the definition from 30 percent of the total loan portfolio or 10 percent of Tier 1 capital).[53/] When BSP conducts its annual on-site examination of D-SIBs/top largest 45 banks, it examines in detail the 50 largest exposures of the bank.
EC5	In respect of credit exposure to single counterparties or groups of connected counterparties, laws or regulations explicitly define, or the supervisor has the power to define, a "group of connected counterparties" to reflect actual risk exposure. The supervisor may exercise discretion in applying this definition on a case by case basis.
Description and findings re EC5	S. 361 of the MORB defines connected counterparties as 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 S. 362 of the MORB and specifies that the term "control of majority interest" shall be synonymous to "controlling interest" and exists when the parent owns directly or indirectly through subsidiaries more than one half of the voting power of an enterprise unless, in exceptional circumstance, it can be clearly demonstrated that such ownership does not constitute control. [53/] See Footnote 2.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	Further, control may exist even when the parent owns one-half or less of the voting power of an enterprise when there is: a) Power over more than one-half of the voting rights by virtue of an agreement with other investors; or b) Power to govern the financial and operating policies of the enterprise under a statute or an agreement; or c) Power to appoint or remove the majority members of the Board of directors or equivalent governing body; or d) Power to cast the majority votes at meetings of the Board of directors or equivalent governing body; or e) Any other arrangement similar to any of the above. "Economic Interdependence" is defined under S. 361 of the MORB as 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. On a case by case basis, the BSP may challenge how a bank defines connected counterparties and economic interdependence. Assessors noted actual cases where the BSP exercised such discretion. See EC6 for additional information regarding BSP's proposed amendments to the prudential standards on large exposures framework wherein the definition of economic interdependence will be expanded.
EC6	Laws, regulations or the supervisor set prudent and appropriate[54/] requirements to control and constrain large credit exposures to a single counterparty or a group of connected counterparties. "Exposures" for this purpose include all claims and transactions (including those giving rise to counterparty credit risk exposure), on-balance sheet as well as off-balance sheet. The supervisor determines that senior management monitors these limits and that they are not exceeded on a solo or consolidated basis.
Description and findings re EC6	S. 107 of the RA states that the MB may place an upper limit on the amount of loans and investments that banks may hold or may place a limit on the rate of increase of such assets within a specified period of time to prevent an expansion of bank credit. Such limits to the loans and investments may be an application to each bank or to specific categories. S. 361 of the MORB provides the definition of "large exposure" to include exposures to a counterparty or a group of connected counterparties equal or greater than 5 percent of the bank's qualifying capital. S. 362 of the MORB provides that the total amount of loans, credit accommodations and guarantees that may be extended by a bank to any person, partnership, association, corporation or other entity (SBL) shall at no time exceed 25 percent of the net worth of the bank. The basis for determining compliance with the SBL is the total credit commitment of the bank to or on behalf of the borrower. The limit or total amount of the loans, credit accommodations and guarantees <u>may be increased</u> if: (a) secured by trust receipts, etc. securing title of goods (10 percent); (b) if entities act as

[54/] Such requirements should, at least for internationally active banks, reflect the applicable Basel standards. As of September 2012, a new Basel standard on large exposures is still under consideration.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	value chain aggregators of the lending banks' clients (25 percent); (c) if loans support the Public-Private Partnership Program (25 percent); d) if loans are granted to finance oil importation, etc. (15 percent). Other prudential limits set by the BSP include a limit for wholesale lending activates of government banks (35 percent) to banks, credit limits for project finance exposures (25 percent of the net worth of the lending book). Current regulations however do not stipulate the requirement to calculate a single borrower limit on a consolidated basis as well as an aggregate large exposure limit for a counterparty or group of connected counterparties on both solo and consolidated basis. BSP also sets a range of other credit limits, including for example: (a) limit for wholesale lending activities of government banks (S. 362 of the MORB); (b) limits for project finance exposures (Circular No. 1001); and (c) ceilings on loans, other credit accommodations and granted to subsidiaries and/or affiliates (S. 342 of the MORB). BSP also outlines certain exposures that are exempted from such limits (as outlines in S. 362 of the MORB). BSP does not expect these limits to be exceeded (S. 362 of the MORB) and as a matter of practice, BSP expects banks to operate below the SBL and aggregate exposure limits. If a bank expects to breach any of the threshold limits, it is expected to contact the BSP. It is noted that violations of S. 362 of the MORB shall be subject to monetary penalties and other sanctions. As part of BSP's on-site examination framework, which examines annually the top 50 large exposures of banks to both single borrower limit plus loans to connected counterparties, examiners assess a bank's operations against threshold limits and will issue directives or other sanctions to banks when needed. Note: BSP's exposure draft on the proposed amendments to the prudential standards on the LE framework proposes to further align the existing regulations with the relevant and applicable aspects of the Basel LE framework.[55/] The proposed amendments, applicable to universal and commercial banks and their subsidiary banks/QBs, include the following main points: (1) revision of the definition of a LE to tighten the capital base of the large exposures from qualifying capital to Tier1 capital and at the same time change the ratio from 5 percent to 10 percent and to be captured both on a solo and on a consolidated basis; (2) adoption of a prudential limit on LEs i.e., 25 percent of Tier 1 capital; (3) setting out additional criteria in identifying economic interdependence to provide a more clear-cut guideline in aggregating exposures to a group of connected counterparties; (4) methodology for measuring and aggregating exposures, including guidelines in the measurement of on and off-balance sheet exposures as well as application of eligible credit risk mitigation techniques; (5) a more comprehensive limit as it will cover exposures from the trading book, derivatives, all traditional off-balance sheet assets, repo-style transactions, investment in securitization transactions and other structures with underlying assets, which are not covered under the existing SBL; and (6) reporting of large exposures both on a solo and on a consolidated basis. [55/] Basel Committee Banking Supervision Standards, *Supervisory framework for measuring and controlling large exposures*, April 2014.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC7	The supervisor requires banks to include the impact of significant risk concentrations into their stress testing programs for risk management purposes.
Description and findings re EC7	BSP requires banks to conduct various stress testing exercises which capture the exposure of concentrations of credit risks/exposures measured against the potential negative impact on banks' capital levels. A banks' ICAAP and the BSP's SRP provide insight into areas of credit concentration together with banks' proposed adequacy on capital levels. Beyond the ICAAP, banks are required to conduct their own stress testing against large exposures to single borrowers and groups of counterparties as part of their credit risk management processes. Further, BSP's REST conducts an annual assessment of banks' real estate exposures. The results of the REST were utilized as a macroprudential measure to address excessive concentrations of real estate exposures in the banking system resulting in the BSP setting prudential limits for real estate exposures (as defined in Memorandum No. M-2012-046: universal, commercial and thrift banks' exposures set at 6 percent of CET1 and 10 percent of risk-based CAR, on a solo and consolidated basis).
Assessment of Principle 19	Largely Compliant
Comments	BSP's on-site examination framework adequately assesses banks' adherence to the current large exposure (LE) framework. However, there are a number of weaknesses in the current LE framework. It does not capture the single borrower limit (SBL) on a consolidated basis; the definition of the capital base against which the SBL is calculated is not compliant with the applicable Basel standard; and clarification is required around the identification of economic interdependence to provide clearer guidance for aggregating exposures to a group of connected counterparties. These issues will be addressed once the proposed draft exposure on amending the current LE framework have been implemented. Recommendation: • Update regulations governing large exposures to ensure limits are calculated both on a solo and consolidated basis.
Principle 20	**Transactions with related parties**. In order to prevent abuses arising in transactions with related parties[56/] and to address the risk of conflict of interest, the supervisor requires banks to enter into any transactions with related parties[57/] on an arm's length basis; to monitor these transactions; to take appropriate steps to control or mitigate the risks; and to write off exposures to related parties in accordance with standard policies and processes.
Essential criteria	
EC1	Laws or regulations provide, or the supervisor has the power to prescribe, a comprehensive definition of "related parties". This considers the parties identified in the footnote to the Principle. The supervisor may exercise discretion in applying this definition on a case by case basis.

[56/] Related parties can include, among other things, the bank's subsidiaries, affiliates, and any party (including their subsidiaries, affiliates and special purpose entities) that the bank exerts control over or that exerts control over the bank, the bank's major shareholders, Board members, senior management and key staff, their direct and related interests, and their close family members, as well as corresponding persons in affiliated companies.

[57/] Related party transactions include on-balance sheet and off-balance sheet credit exposures and claims, as well as, dealings such as service contracts, asset purchases and sales, construction contracts, lease agreements, derivative transactions, borrowings, and write-offs. The term transaction should be interpreted broadly to incorporate not only transactions that are entered into with related parties but also situations in which an unrelated party (with whom a bank has an existing exposure) subsequently becomes a related party.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Circular 895 (S. 131 of the MORB) outlines BSP's definition of related parties which shall cover the bank's subsidiaries as well as affiliates and any party (including their subsidiaries, affiliates and special purpose entities) that the bank exerts direct/indirect control over or that exerts direct/indirect control over the bank; the bank's directors; officers; stockholders and related interests (DOSRI); and their close family members, as well as corresponding persons in affiliated companies. This shall also include such other person/juridical entity whose interests may pose potential conflict with the interest of the bank. S. 131 of the MORB also states that BSP can exercise discretion on a case to case basis. Assessors noted that BSP's definition of related parties is somewhat broader than the suggested Basel definition outlined in footnote 65 as BSP's definition includes "other persons or juridical entities whose interest may post potential conflict of interest with the bank." Further, the BSP regulation adopts a more stringent definition of control where ownership or holding, whether direct or indirect, of 20 percent or more of a class of voting shares of a company versus 50 percent as outlined in the Basel definition. Note that the threshold outlined in the regulations will be subject to review considering the recent amendment in the BSP charter that set the threshold of significant ownership at 10 percent.
EC2	Laws, regulations or the supervisor require that transactions with related parties are not undertaken on more favorable terms (e.g., in credit assessment, tenor, interest rates, fees, amortization schedules, requirement for collateral) than corresponding transactions with non-related counterparties.[58/]
Description and findings re EC2	Circular No. 895 outlines BSP's expectations that RPTs are conducted ensuring arm's length terms and that banks' policies have clear guidelines in ensuring that such transactions are conducted in the regular course of business and not undertaken on more favorable economic terms (e.g., price, commissions, interest rates, fees, tenor, collateral requirement) to such related parties than similar transactions with non-related parties under similar circumstances.
EC3	The supervisor requires that transactions with related parties and the write-off of related-party exposures exceeding specified amounts or otherwise posing special risks are subject to prior approval by the bank's Board. The supervisor requires that Board members with conflicts of interest are excluded from the approval process of granting and managing related party transactions.
Description and findings re EC3	Circular No. 895 outlines BSP's expectations for Boards on RPT to include banks to have guidelines in place on materiality thresholds (requiring Board approval) and excluded transactions. Banks' RPT guidelines should include the identification and prevention or management of a potential or actual conflict of interest. Members of the Board, stockholders and management must disclose to the Board whether they directly, indirectly or on behalf of a third party have a financial interest in any transaction or matter affecting the bank. Directors and officers with personal interest in the transaction must abstain from the discussions, approval and management of such transactions.
EC4	The supervisor determines that banks have policies and processes to prevent persons benefiting from the transaction and/or persons related to such a person from being part of the process of granting and managing the transaction.

[58/] An exception may be appropriate for beneficial terms that are part of overall remuneration packages (e.g., staff receiving credit at favorable rates).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	BSP's on-site examination framework annually assesses a bank's policies and processes surrounding RPTs with a focus on reviewing effective pricing mechanisms to ensure such transactions are at arm's length and in the best interest of the bank and its stakeholders. Examiners assess the strength of a bank's control functions to ensure related parties are not part of the process for granting and managing the RPT.
EC5	Laws or regulations set, or the supervisor has the power to set on a general or case by case basis, limits for exposures to related parties, to deduct such exposures from capital when assessing capital adequacy, or to require collateralization of such exposures. When limits are set on aggregate exposures to related parties, those are at least as strict as those for single counterparties or groups of connected counterparties.
Description and findings re EC5	Circular No. 895 states that a bank's RPT policies should provide internal limits for individual and aggregate exposures. Circular No. 914 outlines certain RPT/loans to be deducted from the net worth and CET1 of the bank, including: (a) outstanding unsecured loans to directors, officers, stockholders; (b) total outstanding unsecured loans granted to subsidiaries, and (c) RPTs that are not considered at arm's length by the BSP. Circular No. 914 provides that all outstanding loans, other credit accommodations and guarantees to all subsidiaries and affiliates shall be subject to the aggregate limits for RPTs. BSP's regulations pertaining to individual and aggregate ceiling limits for RPTs are stipulated in S. 344 of the MORB pertaining to DOSRI, S. 131 of the MORB pertaining to subsidiaries and affiliates and S. 131 of the MORB pertaining to other related parties.
EC6	The supervisor determines that banks have policies and processes to identify individual exposures to and transactions with related parties as well as the total amount of exposures, and to monitor and report on them through an independent credit review or audit process. The supervisor determines that exceptions to policies, processes and limits are reported to the appropriate level of the bank's senior management and, if necessary, to the Board, for timely action. The supervisor also determines that senior management monitors related party transactions on an ongoing basis, and that the Board also provides oversight of these transactions.
Description and findings re EC6	BSP's on site annual examination framework includes the effectiveness assessment of a bank's Board approved RPT policies and processes, the strength of the evaluation by a bank's RPT Committee of RPTs, Board's approval of material RPTs, banks' MIS to identify, aggregate and monitor RPTs and to continuously review and evaluate both new and existing relationships between and among businesses and counterparties. BSP examiners review materiality thresholds and excluded transactions as well as Board approved whistle blowing mechanisms and how a bank Board's deal with the restitution of losses and other remedies for abusive RPTs. Limits outlined in S. 361 and 363 of the MORB pertaining to large exposures and definition of aggregate connected borrowers also apply to RPTs.
EC7	The supervisor obtains and reviews information on aggregate exposures to related parties.
Description and findings re EC7	Circular No. 895 provides guidelines on disclosure and regulatory reporting for banks' RPTs. Further, banks must adequately disclose in their Annual Report, if applicable, the overarching policies and procedures for managing RPTs. Further, banks are required to submit a report to the BSP on material exposures to related parties, including material RPTs of their non-bank financial subsidiaries and affiliates based on a bank's own internal definition of materiality. BSP's off-site surveillance team reviews these reports however the on-site examination framework annually assesses the top 50 large exposures in greater detail. Last, BSP receives annual mapping of group structures of D-SIBs and conglomerates

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
	which assists with BSP's determination of a bank's adherence to RPT definitional requirements.
Assessment of Principle 20	Compliant
Comments	BSP's definition of related parties is broader than the suggested Basel definition, therefore current regulations appear adequate. BSP's on-site examination team adequately challenges banks' policies/procedures for managing related party transactions. As BSP adopts a more risk-based approach to its on-site examination framework, BSP's off-site surveillance and assessment of banks' RPT data will be key.
Principle 21	**Country and transfer risks**. The supervisor determines that banks have adequate policies and processes to identify, measure, evaluate, monitor, report and control or mitigate country risk[59/] and transfer risk[60/] in their international lending and investment activities on a timely basis.
Essential criteria	
EC1	The supervisor determines that a bank's policies and processes give due regard to the identification, measurement, evaluation, monitoring, reporting and control or mitigation of country risk and transfer risk. The supervisor also determines that the processes are consistent with the risk profile, systemic importance and risk appetite of the bank, take into account market and macroeconomic conditions and provide a comprehensive bank-wide view of country and transfer risk exposure. Exposures (including, where relevant, intra-group exposures) are identified, monitored and managed on a regional and an individual country basis (in addition to the end-borrower/end-counterparty basis). Banks are required to monitor and evaluate developments in country risk and in transfer risk and apply appropriate countermeasures.
Description and findings re EC1	S. 143 of the MORB outlines BSP's requirements for the management of country and transfer risk by banks with cross-border credit risk exposures. Banks are expected to have adequate internal capacity for identifying, measuring, monitoring and controlling country and transfer risks in their international lending and investment activities, without placing undue reliance on external ratings. Further, Circulars No. 855 and 971 outline BSP's expectations with respect to banks' processes for managing country and transfer risks are in accordance with the risk profile, risk appetite, systemic importance and takes a bank-wide view of the exposures including the consideration of market and macroeconomic conditions. For example, the BSP expects a more sophisticated tool to be used in more complex credit risk exposures (e.g. asset securitization, credit derivatives, credit-linked notes, etc.). It was noted that the existing regulations covering country and transfer risks are focused on the lending side of a bank's exposures. BSP's draft circular on Risk Management Guidelines on Investment Activities of banks, that has already been released for industry consultation, provides the additional guidance with respect to the investment activities for a bank's exposures.

[59/] Country risk is the risk of exposure to loss caused by events in a foreign country. The concept is broader than sovereign risk as all forms of lending or investment activity whether to/with individuals, corporate, banks or governments are covered.

[60/] Transfer risk is the risk that a borrower will not be able to convert local currency into foreign exchange and so will be unable to make debt service payments in foreign currency. The risk normally arises from exchange restrictions imposed by the government in the borrower's country (reference document: *IMF paper on External Debt Statistics—Guide for compilers and users*, 2003).

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Although the cross-border exposures of Philippine banks are limited, BSP's on-site examination framework includes an annual assessment of banks' credit policies and procedures in the evaluation of country and transfer risks, including the adequacy of a bank's ability to identify, measure, monitor and control these risks and whether these risks are commensurate with the bank's risk profile, risk appetite and systemic importance. On-site examiners assess the bank's entire investment process, not just the lending side of its exposures.
EC2	The supervisor determines that banks' strategies, policies and processes for the management of country and transfer risks have been approved by the banks' Boards and that the Boards oversee management in a way that ensures that these policies and processes are implemented effectively and fully integrated into the banks' overall risk management process.
Description and findings re EC2	Circular 971 indicates that banks are required to have an appropriate risk governance framework capable of identifying, measuring mitigating and monitoring all risks, including country and transfer risks. It outlines a bank's Board's responsibilities to ensure that these policies and process are implemented and fully integrated into the bank's overall risk management process. BSP's on-site examination framework annually reviews the roles and responsibilities of Board and senior management, including making a determination of whether the Board has reviewed and approved the credit policies and that management is adhering to those policies.
EC3	The supervisor determines that banks have information systems, risk management systems and internal control systems that accurately aggregate, monitor and report country exposures on a timely basis; and ensure adherence to established country exposure limits.
Description and findings re EC3	S. 142 of the MORB requires a bank's risk governance framework to include a management information system that is able to provide dynamic, comprehensive and accurate risk reporting both at a disaggregated and aggregated level to allow for a bank-wide view of the risk exposures, including cross border exposures. BSP's on-site examination framework annually examines the adequacy of a bank's risk management, internal controls and information systems with respect to cross Boarder exposures, including the accuracy and reliability of the data. The examiners review credit risk management policies pertaining to country and transfer risks, Board-level reports as well as examining the adequacy of bank's capacity identify, measure, monitor and control the risk limits set by the Board.
EC4	There is supervisory oversight of the setting of appropriate provisions against country risk and transfer risk. There are different international practices that are all acceptable as long as they lead to risk-based results. These include: (a) The supervisor (or some other official authority) decides on appropriate minimum provisioning by regularly setting fixed percentages for exposures to each country taking into account prevailing conditions. The supervisor reviews minimum provisioning levels where appropriate. (b) The supervisor (or some other official authority) regularly sets percentage ranges for each country, taking into account prevailing conditions and the banks may decide,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC4	within these ranges, which provisioning to apply for the individual exposures. The supervisor reviews percentage ranges for provisioning purposes where appropriate. (c) The bank itself (or some other body such as the national bankers' association) sets percentages or guidelines or even decides for each individual loan on the appropriate provisioning. The adequacy of the provisioning will then be judged by the external auditor and/or by the supervisor.
Description and findings re EC4	S.143 of the MORB requires a bank to take into consideration the results of its country risk analysis when calculating the appropriate credit classification and allowance for probable losses of country exposures, including in the development of models for estimating expected losses. See BCP 18 for more details. The BSP on-site examination framework includes the assessment of the adequacy of bank's classification and provisioning for country exposures. In addition, BSP places reliance on the bank's external auditors for a third-party judgement on the adequacy of provisioning for losses.
EC5	The supervisor requires banks to include appropriate scenarios into their stress testing programs to reflect country and transfer risk analysis for risk management purposes.
Description and findings re EC5	Circular 989 outlines BSP's requirement that banks' stress testing scenarios demonstrate relevant risk factors including concentration risk in terms of exposures to individuals, group of related entities, industries, market sectors, countries or regions. Banks' stress tests are conducted at both consolidated and at material entities levels within the group.
EC6	The supervisor regularly obtains and reviews sufficient information on a timely basis on the country risk and transfer risk of banks. The supervisor also has the power to obtain additional information, as needed (e.g., in crisis situations).
Description and findings re EC6	Circular 850, report on cross-border financial positions of banks, is designed to measure and monitor the cross-border financial claims and liabilities of universal and commercial banks and their subsidiary thrift banks. Further, BSP's FRP collects data on a bank's foreign currency denominated financial claims and liabilities.
Assessment of Principle 21	Compliant
Comments	BSPs off-site surveillance of regulatory and supplementary data on banks' country exposures and its on-site examination framework is considered to be adequate. Assessors note that the BSP needs to finalize the draft Circular on Risk Management Guidelines on Investment Activities of banks to capture the investment side of country and transfer risks in the regulatory framework. In all other respects, the BSP's regulations and guidance on banks' country and transfer risk is considered to be acceptable. Recommendation: • Finalize the draft Circular on Risk Management Guidelines on Investment Activities of banks to capture the investment side of the country and transfer risks in the regulatory framework.[61/]
Principle 22	**Market risk**. The supervisor determines that banks have an adequate market risk management process that takes into account their risk appetite, risk profile, and market and macroeconomic conditions and the risk of a significant deterioration in market liquidity. This includes prudent policies and processes to identify, measure, evaluate, monitor, report and control or mitigate market risks on a timely basis.
Essential criteria	

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC1	Laws, regulations or the supervisor require banks to have appropriate market risk management processes that provide a comprehensive bank-wide view of market risk exposure. The supervisor determines that these processes are consistent with the risk appetite, risk profile, systemic importance and capital strength of the bank; take into account market and macroeconomic conditions and the risk of a significant deterioration in market liquidity; and clearly articulate the roles and responsibilities for identification, measuring, monitoring and control of market risk.
Description and findings re EC1	S. 144 and Appendix 70 of the MORB sets out the principles determining the adequacy and effectiveness of a bank's market risk management process, the level and trend of its market risk exposures and the adequacy of capital to be held relative to those exposures. Banks are required to define the individuals and/or committees responsible for managing market risk and to ensure that there is adequate separation of duties in key elements of the risk management process to avoid conflicts of interest. Appendix 42 of the MORB outlines the guidelines on the incorporation of market risk in the risk-based capital adequacy framework for commercial and universal banks. Derivative activities are governed by the provisions of S. 613 of the MORB. The two material market risks being run by Philippine banks are IRRBB and foreign exchange (FX) risk. Equity risk, credit spreads, and commodity risk are not material in the banking sector. Although the BSP's market risk regime focuses primarily on IRRBB and FX risk, the principles are applicable to all market risks [see BCP 23 for IRRBB]. The products used by banks for proprietary trading and hedging purposes are non-complex, comprising primarily forwards, swaps and options. Two foreign owned banks have approval to use internal models to calculate their market risk capital requirement. All other banks are on the standardized approach for market risk. Stand-alone thrift, rural and cooperative banks are subject to a simplified Basel 1.5 capital regime—see BCP 16 EC1. The BSP has a dedicated team of market risk experts to evaluate a bank's sensitivity to market risk as part of the CAMELS process. The assessment involves a review of both qualitative and quantitative data and management's ability to identify, monitor, measure and control market risk. Market risk examination procedures include: (a) a review of board and senior management minutes of meetings; (b) evaluation of market risk management policies and procedures, and compliance; (c) assessment of market risk measurement methodologies, limits structures, monitoring, and management information system, and (d) review of internal controls and audit. Market risk reviews are generally conducted as part of the regular examination of a bank, but the market risk team may, and has, conducted reviews between annual examination periods when market risk concerns have arisen. The market risk team is adequately resourced in terms of both numbers of staff and levels of expertise, given the non-complex nature of the market risk instruments currently employed by banks. As the banking sector develops and banks introduce more complex traded instruments, the BSP should continue to ensure it has sufficient relevant expertise to meet the challenge of greater market complexity.
EC2	The supervisor determines that banks' strategies, policies and processes for the management of market risk have been approved by the banks' Boards and that the Boards

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC2	oversee management in a way that ensures that these policies and processes are implemented effectively and fully integrated into the banks' overall risk management process.
Description and findings re EC2	See EC1. As part of the on-site examination process, market risk experts assess the adequacy and effectiveness of Board and senior management oversight over the market risk function in a bank. This forms a key consideration in the determination of the overall rating for the quality of market risk management under the CAMELS rating framework. There was evidence from reviews of bank examination reports of effective supervisory challenge.
EC3	The supervisor determines that the bank's policies and processes establish an appropriate and properly controlled market risk environment including: (a) effective information systems for accurate and timely identification, aggregation, monitoring and reporting of market risk exposure to the bank's Board and senior management; (b) appropriate market risk limits consistent with the bank's risk appetite, risk profile and capital strength, and with the management's ability to manage market risk and which are understood by, and regularly communicated to, relevant staff; (c) exception tracking and reporting processes that ensure prompt action at the appropriate level of the bank's senior management or Board, where necessary; (d) effective controls around the use of models to identify and measure market risk, and set limits; and, (e) sound policies and processes for allocation of exposures to the trading book.
Description and findings re EC3	Appendix 70 of the MORB recognizes that there are a number of methods/techniques for measuring market risk, ranging from simple marking-to-market or valuation techniques to highly sophisticated dynamic modeling techniques that reflect potential business activities. It requires banks to have market risk measurement systems that capture all material sources of market risk and assess the effect of changes in market risk factors in ways that are consistent with the scope of their activities. The appendix sets out the following specific requirements: (a) Banks should have an accurate, informative, and timely management information system to manage market risk exposures, both to inform management and to support compliance with policies. While the types of reports prepared for the management will vary dependent on a bank's market risk profile, the minimum information and reports include summaries of aggregate exposure; reports demonstrating compliance with policies and limits; summary of key assumptions; results of stress tests and summaries of the findings of reviews of market risk policies, procedures; and the adequacy of the market risk measurement systems, including any findings of internal and external auditors and retained consultants. Regardless of the measurement system used, banks are expected to ensure that input data are timely and correct, assumptions can be supported and are valid, the methodologies used produce accurate results, and the results can be easily understood and are regularly reported to senior management and the Board. (b) The Board and senior management should establish appropriate risk limits based on a bank's tolerance for market risk, taking into account the nature of its strategies and activities, past performance and management skills, as well as the sufficiency of earnings and capital to absorb losses. The level of detail of risk limits should reflect

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	the characteristics of the bank's holdings including the various sources of market risk to which it is exposed. (c) Positions that exceed pre-determined levels should receive prompt management action. Limit exceptions should be communicated to management without delay. Policies should include how management will be informed and what action should be taken by management in such cases. Particularly important is whether limits are absolute in the sense that they should never be exceeded or whether, under specific circumstances, breaches of limits can be tolerated for a short period of time. The circumstances leading to a tolerance of breaches should be clearly described. (d) To ensure the integrity of a bank's market risk management process, adequate internal controls should be an integral part of the bank's overall risk management system and should promote effective and efficient operations, reliable financial and regulatory reporting, and compliance with relevant laws, regulations, and institutional policies. The guidelines on market risk management in Appendix 70 of the MORB introduce an ambiguity around whether market risk should be viewed on a whole bank basis or whether the trading book and the accrual book should be treated separately. The BSP is proposing to issue an update to the risk management guidelines which will clarify this issue. The lack of clarity around the boundary between the two has been identified as a root cause of some inappropriate capital arbitrage practices between positions booked in the trading and banking books. Examiners are alert to the practice and, pending the issue of the revised guidance, have enforced the segregation between the trading and banking books, requiring banks to ensure that positions are subject to appropriate risk management processes. Banks' compliance with the guidelines and the effectiveness of internal policies, processes and infrastructure are validated during on-site examinations by the experts in the market risk team. Board meetings and packages are reviewed to identify the parameters used by the Board and senior management in setting market risk limits and to determine how limit exceptions are handled. Management information reports are evaluated to determine comprehensiveness, clarity and integrity of analysis and to establish whether reports accurately reflect the bank's level of market risk exposures. Independent reviews of the bank's market risk information system, which includes model validation, are assessed to ensure that such reviews include assessments of the assumptions and methodologies used.
EC4	The supervisor determines that there are systems and controls to ensure that banks' marked-to-market positions are revalued frequently. The supervisor also determines that all transactions are captured on a timely basis and that the valuation process uses consistent and prudent practices, and reliable market data verified by a function independent of the relevant risk-taking business units (or, in the absence of market prices, internal or industry-accepted models). To the extent that the bank relies on modeling for the purposes of valuation, the bank is required to ensure that the model is validated by a function independent of the relevant risk-taking businesses units. The supervisor requires banks to establish and maintain policies and processes for considering valuation adjustments for positions that otherwise cannot be prudently valued, including concentrated, less liquid, and stale positions.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	Appendix 70, S. 613 and Appendix 42 of the MORB require banks to adopt appropriate valuation procedures and an appropriate mark-to-market model methodology. In addition, there have been various Circulars issued providing guidance on the valuation of financial assets and liabilities, the most recent of which (Circular No.1021) amended the guidelines on the marking to market of financial instruments, aligning regulations with the provisions of PFRS 13 on fair value measurement. The BSP has not formally adopted the prudent valuation framework, but Appendix 59 of the MORB requires banks to submit documentation that describes the systems and controls for the prudent valuation of positions in the trading book, including valuation methodologies. These documents, and the approach adopted by banks to fair valuation methodologies, are reviewed during examinations. The BSP is proposing to issue revised risk management guidelines on investment activities, which will update the framework for the fair valuation of positions, placing emphasis on timely valuation and the need for the validation of models prior to use. The policy proposal is currently under exposure.
EC5	The supervisor determines that banks hold appropriate levels of capital against unexpected losses and make appropriate valuation adjustments for uncertainties in determining the fair value of assets and liabilities.
Description and findings re EC5 Description and findings re EC5	Appendix 42 of the MORB sets out the capital requirements for universal and commercial banks' market risk exposures. The guidelines are broadly consistent with the recommendations of the BCBS's document "Amendment to the Capital Accord to Incorporate Market Risks" issued in January 1996. Banks are allowed to use either the standardized approach or the internal models approach for the calculation of capital charges for specific and general market risks. Regulatory standards on market risk capital are under review following the Basel Committee's publication of the Minimum Capital Requirements for Market Risk standard in January 2016. As noted in EC4, appendix 59 of the MORB requires banks to submit documentation that describes the systems and controls for the prudent valuation of positions in the trading book, including valuation methodologies. Although there is no specific regulation or guideline that covers valuation adjustments for uncertainties in determining the fair value of a bank's assets and liabilities, the fair valuation methodologies employed by banks are reviewed during examinations. The reasonableness of any adjustments incorporated in valuing assets and liabilities under different stress conditions to account for uncertainties, and how these ultimately impact a banks' capital positions, are also assessed as part of the examination process.
EC6	The supervisor requires banks to include market risk exposure into their stress testing programs for risk management purposes.
Description and findings re EC6	Circular No. 989 provides guidelines on the conduct of stress testing exercises of universal and commercial banks. Rural, thrift and cooperative banks with simple operations are not required to conduct market risk stress tests given that such risk is not material to their operations. The guidelines set out the duties and responsibilities/roles and functions of the Board and senior management, the stress testing framework to be established, the supervisory expectations on the use of models for stress testing and independent review of stress testing, the applicability of the guidelines to the different types of banks, the

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	reporting requirements, and the supervisory enforcement actions, in case of non-compliance with the guidelines. Appendix 70 of the MORB requires universal and commercial banks to supplement their market risk measurement models with stress tests which would show how a portfolio or balance sheet might perform during extreme events or high volatile markets. It sets out possible stress scenarios, including abrupt changes in the general level of interest rates, changes in the relationships among key market rates, changes in the slope and the shape of the yield curve, changes in the liquidity of key financial markets, or changes in the volatility of market rates. The guidelines for performing stress testing are required to be detailed in a bank's risk management policy statement with periodic review of the design, assumptions of results of such stress tests. The market risk experts review banks' stress testing policies and procedures as part of the supervisory review of the ICAAP and when on site as part of an examination. Evidence from reviews of examination reports demonstrated effective supervisory challenge on banks' stress testing methodologies and assumptions.
Assessment of Principle 22	Largely Compliant
Comments	The regulatory framework and supervisory practice are appropriate for the complexity of market risk being run by banks, and the BSP is adequately resourced in terms of both numbers and levels of expertise to supervise banks' market risk functions effectively. The framework ensures that banks have adequate market risk management processes that take into account their risk appetite and risk profile, but there is a lack of clarity in the framework over the allocation of assets between trading and banking books, which creates capital arbitrage opportunities for banks. Proposals to update the BSP market risk framework, when implemented, will address this ambiguity and, more generally, will clarify the governance and capital treatment of market risk. Recommendation: • Issue the proposals on a revised market risk framework and on risk management guidelines on investment activities.[62/]
Principle 23	**Interest rate risk in the banking book**. The supervisor determines that banks have adequate systems to identify, measure, evaluate, monitor, report and control or mitigate interest rate risk[63/] in the banking book on a timely basis. These systems take into account the bank's risk appetite, risk profile and market and macroeconomic conditions.
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to have an appropriate interest rate risk strategy and interest rate risk management framework that provides a comprehensive bank-wide view of interest rate risk. This includes policies and processes to identify, measure, evaluate, monitor, report and control or mitigate material sources of interest rate risk. The supervisor determines that the bank's strategy, policies and processes are consistent with the risk appetite, risk profile and systemic importance of the bank, take into account market and macroeconomic conditions, and are regularly reviewed and appropriately adjusted, where necessary, with the bank's changing risk profile and market developments. ______________________ 62/ See footnote 2. 63/ Wherever "interest rate risk" is used in this Principle the term refers to interest rate risk in the banking book. Interest rate risk in the trading book is covered under Principle 22.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	S.144 and Appendix 70 of the MORB provide guidance on the definition and sources of IRRBB. They require banks to establish policies, processes and control procedures to ensure that the risk identification, aggregation, mitigation and monitoring capabilities of IRRBB are commensurate with the bank's size, complexity, risk profile, and systemic importance. IRRBB is defined as the risk that changes in market interest rates will reduce current or future earnings and/or the economic value of a bank. The sources of IRRBB are identified as re-pricing risk, basis risk, yield curve risk, and option risk, all of which are defined. S. 144 also sets out guidelines on how to measure the effects of IRRBB. A modified interest rate gap or earnings simulation model to forecast earnings over a running twelve-month time horizon under a variety of interest rate scenarios is used by many banks and is appropriate given that a large portion of their liabilities and assets re-price in less than one year. For those banks which hold assets, such as bonds and fixed rate loans, with extended terms beyond one year, an economic value model is considered more appropriate. Smaller banks with non-complex single currency balance sheets may use a single non-complex measurement methodology, such as re-pricing gap analysis to manage their interest rate risk. The BSP expects banks' economic value models to incorporate all significant classes of assets, liabilities and OBS. As with earnings at risk, the bank should incorporate a variety of interest rate scenarios to ensure that any strike prices, caps, limits, or "events" are breached in the simulation. Also, banks with significant levels of basis or yield curve risk are expected to add scenarios such as alternative correlations between interest rates and/or a flatter or steeper yield curve. The BSP has a specialist market risk team which undertakes the on-site examination of IRRBB risk run by universal and commercial banks. It is adequately resourced in terms of both numbers of staff and technical expertise. The review of IRRBB in thrift, rural and cooperative banks is performed by examiners responsible for the banks. This is appropriate given the non-complex nature of the risk being run. Market experts are engaged if a material interest rate risk is identified by the examination team. The evaluation of a bank's sensitivity to interest rate risk forms part of the CAMELS assessment, the guidelines for which are set out in SG 2009-21. The assessment considers both qualitative and quantitative data of a bank's interest rate risk by assessing its risk exposure, management's ability to identify, monitor, measure and control such risk and the implications for the bank's earnings and capital. Reviews of examination reports provided sufficient evidence that interest rate risk is evaluated appropriately by supervisors. The BSP has issued an exposure draft to industry that will update the BSP's existing IRRBB guidelines. It separates the regulations on IRRBB from the broader market risk guidelines and aligns the guidelines on the management of IRRBB more closely to the guidance issued by the BCBS in 2016. A simplified reporting approach as an alternative to the Basel standardized framework is to be adopted.
EC2	The supervisor determines that a bank's strategy, policies and processes for the management of interest rate risk have been approved, and are regularly reviewed, by the

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC2	bank's Board. The supervisor also determines that senior management ensures that the strategy, policies and processes are developed and implemented effectively.
Description and findings re EC2	Appendix 70 of the MORB sets out the requirements for appropriate Board and senior management oversight over a bank's risk management system and the roles and responsibilities of the Board and senior management in managing interest rate risk exposures. The on-site examination process conducted by market risk experts includes an assessment of the adequacy and effectiveness of Board and senior management oversight on IRRBB. Commentary in examination reports confirmed effective challenge in this area.
EC3 **EC3**	The supervisor determines that banks' policies and processes establish an appropriate and properly controlled interest rate risk environment including: (a) comprehensive and appropriate interest rate risk measurement systems; (b) regular review, and independent (internal or external) validation, of any models used by the functions tasked with managing interest rate risk (including review of key model assumptions); (c) appropriate limits, approved by the banks' Boards and senior management, that reflect the banks' risk appetite, risk profile and capital strength, and are understood by, and regularly communicated to, relevant staff; (d) effective exception tracking and reporting processes which ensure prompt action at the appropriate level of the banks' senior management or Boards where necessary; and, (e) effective information systems for accurate and timely identification, aggregation, monitoring and reporting of interest rate risk exposure to the banks' Boards and senior management.
Description and findings re EC3	See EC1. Appendix 70 of the MORB requires banks to: a) Establish appropriate risk measurement systems that capture all material sources of risk associated with its assets, liabilities and off-balance sheet positions. b) Ensure that models are validated by individuals who are neither directly involved in the development process nor responsible for providing inputs to the model, prior to the use of the said model. Such model validation includes the development of empirical support for the model's assumptions. A periodic review of methodologies and assumptions is also required. c) Establish appropriate risk limits, duly approved by the Board, to maintain the bank's exposure within set tolerances over a range of possible changes in interest rates. In setting limits, the Board and senior management are expected to consider the nature of the bank's strategies and activities, past performance and management skills, as well as the level of the bank's earnings and capital to ensure that both are sufficient to absorb losses equal to the set limits. d) Ensure that positions that exceed pre-determined levels receive prompt management action. Limit exceptions are expected to be communicated to management without delay.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	Policies should include how management will be informed and what action should be taken by management in such cases. The circumstances leading to a tolerance of breaches are also expected to be clearly described. e) Establish an accurate, informative, and timely management information system. Reports detailing the bank's interest rate risk exposure are expected to be review by the Board on a regular basis. As part of the examination process, supervisors assess banks' gap reports, use of interest rate scenarios and simulation models, and metrics used to capture IRRBB from both the earnings and economic value perspectives. Stress test methodologies and results are reviewed and the adequacy of management of model risk is ascertained. The exposure draft of updated guidelines on IRRBB will incorporate more detailed model risk governance principles, as well as an explicit requirement to adopt sound and reasonable assumptions on the repricing of products with behavioral optionalities in the computation of risk metrics.
EC4	The supervisor requires banks to include appropriate scenarios into their stress testing programs to measure their vulnerability to loss under adverse interest rate movements.
Description and findings re EC4	Appendix 70 of the MORB requires universal and commercial banks to supplement their interest rate risk measurement models with stress tests showing how a portfolio or the balance sheet might perform during extreme events or in highly volatile markets. The guidelines specify that the design of stress tests should be tailored to the specific risk characteristics of the bank and consider "worst case" scenarios in addition to more probable events. Circular 989 sets out the general requirements for universal and commercial banks to conduct stress tests. In respect of IRRBB, it specifically expects banks to consider risks arising from parallel or non-parallel shifts in the yield curve, and the increase in basis risk (i.e., changes in relationships between key market rates). Banks are expected to adopt systems that are capable of estimating changes to net interest income under a variety of interest rate scenarios. For example, non-complex banks with traditional business lines and balance sheets may limit their simulations to a single + 100 basis point parallel rate shock. Banks that hold significant levels of derivatives and structured products relative to capital are required to incorporate more severe rate movements (e.g., + 100, 200 and 300 basis points) to determine what happens if strike prices are breached or "events" are triggered. The market risk experts evaluate the adequacy of universal and commercial banks' stress testing programs during on-site examinations. The examination involves an assessment of whether the stress test involves plausible forward-looking scenarios and takes into account scenarios along a spectrum of severity levels. There were numerous examples of constructive challenge by supervisors on stress testing issues in bank examination reports. There are currently no requirements for rural, thrift or cooperative banks to conduct stress tests of their interest rate risk, but the exposure draft that will update existing IRRBB guidelines, includes such a requirement. It will also introduce further enhancements to banks' stress testing exercises, covering the determination of currency-specific interest rate movements; the setting of assumptions on how rates shall change under identified stress

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	scenarios; and the adoption of forward-looking scenarios that incorporate changes in portfolio composition due to internal and external factors, new products, new market information and emerging risks.
Assessment of Principle 23	Largely Compliant
Comments	The legal and supervisory framework for ensuring banks have adequate systems that identify, measure, evaluate, monitor, report and control IRRBB is appropriate for the complexity of the risk being run by such banks. The framework does not, however, set IRR stress test requirements for smaller banks. A revised set of IRRBB guidelines has been exposed to industry for comment which, when implemented, will introduce further enhancements to banks' stress testing exercises and, more generally, align the BSP framework with the applicable Basel standard. Recommendation: • Implement the proposals on a revised set of IRRBB guidelines.[64/]
Principle 24 **Principle 24**	**Liquidity risk**. The supervisor sets prudent and appropriate liquidity requirements (which can include either quantitative or qualitative requirements or both) for banks that reflect the liquidity needs of the bank. The supervisor determines that banks have a strategy that enables prudent management of liquidity risk and compliance with liquidity requirements. The strategy takes into account the bank's risk profile as well as market and macroeconomic conditions and includes prudent policies and processes, consistent with the bank's risk appetite, to identify, measure, evaluate, monitor, report and control or mitigate liquidity risk over an appropriate set of time horizons. At least for internationally active banks, liquidity requirements are not lower than the applicable Basel standards.
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to consistently observe prescribed liquidity requirements including thresholds by reference to which a bank is subject to supervisory action. At least for internationally active banks, the prescribed requirements are not lower than, and the supervisor uses a range of liquidity monitoring tools no less extensive than, those prescribed in the applicable Basel standards.
Description and findings re EC1	The BSP has set three liquidity requirements for its banks. Universal and commercial banks and their subsidiary banks and QBs are required to comply with LCR and NSFR frameworks, and stand-alone rural, thrift and cooperative banks are required to meet an MLR framework. <u>Liquidity Coverage Ratio</u> Appendix 72 of the MORB sets out the requirements and components of the numerator and denominator of the LCR. The calculation of the LCR is based on the Basel III framework, but the BSP has exercised certain discretions in respect of deposit run-off rates which are more conservative than the Basel standard. The framework took effect from January 1, 2019, since when universal and commercial banks have been required to maintain an LCR of 100 percent on a daily basis. To monitor compliance with the minimum LCR requirements, banks are required to submit monthly and quarterly calculations of their LCR to demonstrate compliance with the 100 percent minimum requirement. ______________________ [64/] See footnote 2.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	The BSP also receives additional monitoring reports to assess the liquidity risk of a bank. In line with the recommendations of the BCBS, a contractual maturity mismatch report is submitted on a monthly basis by banks. The BCBS LCR standard suggests time buckets of overnight, 7 days, 14 days and one month out to 5 years. The BSP, however, does not require banks to report contractual maturity mismatches in the shorter time buckets from overnight out to 14 days. As such, the reporting does not capture any potential daily liquidity mismatches in the period out to one month. The BSP should review its current reporting requirements and introduce additional time buckets, including overnight, in its contractual maturity mismatch report to align with the applicable Basel standard. Information related to a bank's LCR is also required to be disclosed in the bank's quarterly published balance sheet, and on the bank's website. its other published financial reports or publicly available regulatory reports. Upon receipt of the monthly LCR report, off-site supervisors assess any shortfall in a bank's LCR. This will not necessarily result in supervisory or enforcement action but, at a minimum, will entail heightened supervisory monitoring. The assessment will consider the extent of the liquidity deficit and whether non-compliance with the LCR will be temporary, is part of a regular pattern or practice, or is caused by an unusual event. In the event that the LCR remains below the minimum requirement for a prolonged period of time or if the BSP has determined that the bank is otherwise materially non-compliant with the LCR, and the reported shortfall in the LCR is caused by a firm-specific stress situation, the BSP will require an effective and timely remedial action from the bank to address the deficiency in its liquidity position within a committed timeline. When a bank fails to restore its liquidity position within the committed timeline, or is unable to substantially comply with the remedial measures directed, sanctions may be imposed on the bank subject to MB approval. <u>Net Stable Funding Ratio</u> Circular 1007 sets out the requirements of the NSFR. It aims to promote the long-term resilience of a bank by maintaining a stable funding profile in relation to the composition of its assets and off-balance sheet activities. The NSFR applies to all universal and commercial banks and their subsidiary banks and QBs, on both a solo and consolidated basis. The NSFR took effect from 1 January 2019, from which date covered banks are required to maintain at least 100 percent NSFR on a daily basis. The BSP monitors banks' compliance with the requirement through quarterly reports. Similar to the LCR requirements, a shortfall will not necessarily result in supervisory or enforcement action; at a minimum, it will entail heightened supervisory monitoring. The BSP will require effective and timely remedial action from the bank to address any deficiency in its liquidity position within a committed timeline. When a bank fails to restore its liquidity position within the committed timeline, the BSP may deploy more stringent enforcement actions. <u>Minimum Liquidity Ratio</u>

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Circular 996 sets out the MLR requirements for stand-alone rural, thrift and cooperative banks. The objective of the MLR is to promote short-term resilience to liquidity shocks of the covered banks. The MLR is expressed as a percentage of a bank's eligible stock of liquid assets to its total qualifying liabilities. The MLR definition of stock of liquid assets is not consistent with the definition of HQLA in the LCR, but the liquid assets must be readily liquefiable and free from encumbrances. The qualifying liabilities are defined in Circular 996 and include irrevocable obligations under off-balance sheet items (e.g., guarantees, committed credit lines). Banks are required to maintain an MLR of 20 percent on a daily basis, absent a period of financial stress. The 20 percent ratio was based on empirical historical loss/bank failure data. The MLR came into effect on 1 January 2019. Covered banks are required to submit a monthly report on their compliance with the MLR ratio, on a solo basis in peso-equivalent terms using a prescribed form within 15 business days after the end of the reference period. As with the other two frameworks, a shortfall will not necessarily result in supervisory or enforcement action but, at a minimum, it will entail heightened supervisory monitoring. <u>Other minimum liquidity requirements</u> Circular 996 and S. 73 of the Manual of Regulations on Foreign Exchange Transactions (MORFXT) require depository banks under the foreign currency deposit and expanded foreign currency deposit systems (FCDU/EFCDU) to maintain at all times a 100 percent cover for their foreign currency liabilities, except for USD-denominated repurchase agreement with the BSP. S. 75 of the MORFXT prescribes that FCDUs/EFCDUs of universal and commercial banks as well as FCDUs of rural, thrift and cooperative banks maintain the foreign currency cover in any foreign currency acceptable with the BSP. Supervisors ensure compliance with the above liquidity requirements, including their policies and processes, as part of the on-site examination process. The adequacy of a bank's liquidity and funding profile is assessed under the CAMELS framework.
EC2	The prescribed liquidity requirements reflect the liquidity risk profile of banks (including on- and off-balance sheet risks) in the context of the markets and macroeconomic conditions in which they operate.
Description and findings re EC2	The BSP has exercised discretions in its implementation of the LCR framework in respect of run off rates, which are more conservative than the Basel standard. These reflect local circumstances. More generally, however, the LCR, MLR and NSFR frameworks are not risk-based. The minimum requirements apply uniformly to each bank subject to each framework and are not tailored to the liquidity risk profile of individual banks. The BSP does not require its universal and commercial banks to produce an ILAAP and does not factor liquidity risks that are not captured in the LCR calculation (e.g., intraday liquidity risk) into banks' liquidity requirements.
EC3	The supervisor determines that banks have a robust liquidity management framework that requires the banks to maintain sufficient liquidity to withstand a range of stress events, and includes appropriate policies and processes for managing liquidity risk that have been approved by the banks' Boards. The supervisor also determines that these policies and processes provide a comprehensive bank-wide view of liquidity risk and are consistent with the banks' risk profile and systemic importance

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	Circular 981 sets out the liquidity risk management guidelines that banks should follow. It specifies that a bank's liquidity risk management framework should reflect the size, nature and complexity of its activities; it should be able to identify, measure, monitor, and control its exposures to liquidity risk in a timely and comprehensive manner; and maintain a structurally sound funding and liquidity profile. Specifically, the guidelines require banks to maintain a level of liquidity sufficient to readily meet both expected and unexpected cash flows and collateral needs without adversely affecting daily operations and the bank's financial condition. The management of cash flows considers the bank's funding capacity for both short- and long-term time horizons, including intraday, and the currencies in which it has significant activities or exposures. Systems and controls are required to be in place to oversee and manage liquidity positions on an intragroup basis, including those arising from cross-border transactions, taking into consideration the differing liquidity risk profiles of each entity and the transferability of funds within the group. A bank should also ensure that it is able to withstand a series of stress events with varying severities under different time horizons. Banks' compliance with the liquidity risk management regulations are evaluated during on-site examinations. Guidelines on intraday liquidity reporting have been issued but reporting requirements have yet to be implemented. Under these guidelines, universal and commercial banks are required to submit monthly reports on intraday liquidity to the BSP. This will enable the BSP to monitor banks' intraday liquidity positions, their sources of intraday liquidity, and their ability to meet payment and settlement obligations on a timely basis under both normal and stressed conditions.
EC4	The supervisor determines that banks' liquidity strategy, policies and processes establish an appropriate and properly controlled liquidity risk environment including: (a) clear articulation of an overall liquidity risk appetite that is appropriate for the banks' business and their role in the financial system and that is approved by the banks' Boards; (b) sound day-to-day, and where appropriate intraday, liquidity risk management practices; (c) effective information systems to enable active identification, aggregation, monitoring and control of liquidity risk exposures and funding needs (including active management of collateral positions) bank-wide; (d) adequate oversight by the banks' Boards in ensuring that management effectively implements policies and processes for the management of liquidity risk in a manner consistent with the banks' liquidity risk appetite; and, (e) regular review by the banks' Boards (at least annually) and appropriate adjustment of the banks' strategy, policies and processes for the management of liquidity risk in the light of the banks' changing risk profile and external developments in the markets and macroeconomic conditions in which they operate.
Description and findings re EC4	See EC3.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC5	The supervisor requires banks to establish, and regularly review, funding strategies and policies and processes for the ongoing measurement and monitoring of funding requirements and the effective management of funding risk. The policies and processes include consideration of how other risks (e.g. credit, market, operational and reputation risk) may impact the bank's overall liquidity strategy, and include: (a) an analysis of funding requirements under alternative scenarios; (b) the maintenance of a cushion of high quality, unencumbered, liquid assets that can be used, without impediment, to obtain funding in times of stress; (c) diversification in the sources (including counterparties, instruments, currencies and markets) and tenor of funding, and regular review of concentration limits; (d) regular efforts to establish and maintain relationships with liability holders; and, (e) regular assessment of the capacity to sell assets.
Description and findings re EC5	Circular 981 requires senior management to develop a funding strategy that provides for the effective diversification of funding sources and maturities taking into account market conditions and the bank's ability to access funds from different sources. It requires a bank to diversify available funding sources in the short, medium and long-term and for diversification targets to be part of the medium to long-term funding plan. The targets should be aligned with the bank's budgeting and business planning process. The funding strategy should be formally documented and regularly reviewed in light of any changes in the market environment or key assumptions. In doing so, management should have an adequate understanding of how the bank's liquidity risk profile is affected by other risks such as credit, market, operational and reputational risks. The regulations list factors for banks to consider in developing a funding strategy. These include access to alternative sources of funding in different situations and the management of any potential concentration in particular funding markets and sources (including maturities, credit profiles of liabilities, specific instruments or products, geographical locations and currencies). Banks are also required to regularly test their contingency funding plans by verifying the ability to sell a certain volume of assets. As part of ensuring access to alternative sources of funding, banks are expected to establish and maintain relationships with liability holders. Banks' funding strategies are reviewed as part of the on-site examination process. Evidence of effective challenge by supervisors was cited in examination reports.
EC6	The supervisor determines that banks have robust liquidity contingency funding plans to handle liquidity problems. The supervisor determines that the bank's contingency funding plan is formally articulated, adequately documented and sets out the bank's strategy for addressing liquidity shortfalls in a range of stress environments without placing reliance on lender of last resort support. The supervisor also determines that the bank's contingency funding plan establishes clear lines of responsibility, includes clear communication plans (including communication with the supervisor) and is regularly tested and updated to ensure it is operationally robust. The supervisor assesses whether, in the light of the bank's risk profile and systemic importance, the bank's contingency funding plan is feasible and requires the bank to address any deficiencies.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	Circular 981 requires banks to have formal contingency funding plans (CFPs) that clearly set out strategies for addressing liquidity shortfalls, including those estimated from stress tests that apply a range of scenarios. The CFP is expected to be able to address liquidity issues over a range of time horizons; reflect the relevance of the central bank lending facility as a secondary source of liquidity; clearly delineate the roles and responsibilities and internal procedures for crisis management; include a communication plan to deliver clear and consistent information on a timely basis to internal and external counterparties, including the BSP; and be subject to regular testing to ensure effectiveness and operational feasibility. Supervisors assess the adequacy and viability of a bank's CFP in light of its risk profile and systemic importance as part of the examination process. Any deficiencies noted are cited in reports of examination, and the bank's compliance with directives to address the same is duly monitored. Evidence of such challenge was seen in examination reports.
EC7	The supervisor requires banks to include a variety of short-term and protracted bank-specific and market-wide liquidity stress scenarios (individually and in combination), using conservative and regularly reviewed assumptions, into their stress testing programmes for risk management purposes. The supervisor determines that the results of the stress tests are used by the bank to adjust its liquidity risk management strategies, policies and positions and to develop effective contingency funding plans.
Description and findings re EC7	Circular 981 requires universal and commercial banks to conduct stress tests on a regular basis for a variety of short-term and protracted stress scenarios. At a minimum, the bank should consider (1) an institution-specific crisis scenario, (2) a market-wide crisis scenario, and (3) a combination of both. The scenarios are subject to regular review and approval by the Board and senior management to ensure that their nature and severity remain appropriate and relevant. The results of the stress tests are expected to be linked to the overall asset and liability management and liquidity risk management processes of the bank. The results should be integrated into the bank's strategic business planning process, liquidity risk management strategies and practices, setting of internal liquidity risk limits, and the assessment of potential funding shortfalls in the CFP. The Board and senior management should discuss the results and consider the need for remedial or mitigating actions. Stand-alone thrift, rural, and cooperative banks are required to conduct simple sensitivity analysis covering credit, liquidity, and operational risks. Supervisors assess the sufficiency of banks' policies and procedures in the conduct of liquidity stress tests, evaluating the validity of the applied assumptions as well as the actions taken on the results, during on-site examinations. Evidence from examination reports demonstrated effective challenge of stress testing assumptions by supervisors.
EC8	The supervisor identifies those banks carrying out significant foreign currency liquidity transformation. Where a bank's foreign currency business is significant, or the bank has significant exposure in a given currency, the supervisor requires the bank to undertake separate analysis of its strategy and monitor its liquidity needs separately for each such significant currency. This includes the use of stress testing to determine the appropriateness of mismatches in that currency and, where appropriate, the setting and regular review of limits on the size of its cash flow mismatches for foreign currencies in aggregate and for each significant currency individually. In such cases, the supervisor also

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC8	monitors the bank's liquidity needs in each significant currency and evaluates the bank's ability to transfer liquidity from one currency to another across jurisdictions and legal entities.
Description and findings re EC8 Description and findings re EC8	Circular 981 clarifies that liquidity risk management principles also apply to the management of any foreign currency in which a bank maintains a significant exposure. (A currency is considered "significant" if the aggregate liabilities denominated in that currency amount to 5 percent or more of a bank's total liabilities.) Banks are required to formulate liquidity strategies and policies for the major currencies in which they have significant activity or exposure, and to assess their aggregate foreign currency liquidity needs under both normal and stressed conditions and control currency mismatches within acceptable levels. Banks are required also to assess the likely convertibility of foreign currencies and access to foreign exchange markets for switching funding from one currency to another. Banks are required to set, and review regularly, limits on the size of any funding gaps for each significant individual currency and in aggregate over particular time bands. In setting limits, management should consider the bank's ability to raise funds in foreign exchange markets and to transfer surplus liquidity from one currency to another, across jurisdictions and legal entities. LCR, MLR, and NSFR regulations require banks to measure and monitor applicable liquidity ratios by significant currency. The MORFXT also limits the allowable open FX position of banks to USD 50 million or its equivalent, or 20 percent of unimpaired capital, whichever is the lower. This limit includes off-balance sheet items such as foreign currency forwards. Banks are required to regularly submit reports demonstrating compliance with this limit. Supervisors assess banks' FX liquidity management practices during on-site examinations. Off-site supervisors also monitor banks' foreign currency liquidity needs through monthly significant currency LCR reports. The supervisory assessment of banks' liquidity risk exposures is informed by an understanding of potential impediments to the transfer of liquidity from one currency to another across jurisdictions or legal entities.
Assessment of Principle 24	Largely compliant
Comments	An appropriate regulatory framework is in place to ensure minimum requirements for liquidity and funding for universal and commercial banks, but the cashflow mismatch monitoring tools for the LCR should be reviewed and aligned more closely with applicable Basel standards. The BSP has issued guidelines on a monitoring regime for intraday liquidity but has yet to introduce a reporting regime for intraday liquidity. The BSP does not set individual liquidity and funding requirements for its banks above the statutory minimum that reflect the liquidity and funding profiles of those banks. Recommendations: • Review the monitoring tools for the LCR to align them more closely with applicable Basel standards, including introduction of a more granular cashflow mismatch report. • Introduce an ILAAP framework to enable the BSP to set individual liquidity and funding requirements for banks above the statutory minimum to reflect the particular liquidity and funding profiles of those banks. • Implement an intraday liquidity reporting regime.[65/] [65/] See footnote 2.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Principle 25	**Operational risk**. The supervisor determines that banks have an adequate operational risk management framework that takes into account their risk appetite, risk profile and market and macroeconomic conditions. This includes prudent policies and processes to identify, assess, evaluate, monitor, report and control or mitigate operational risk[66/] on a timely basis.
Essential criteria	
EC1	Law, regulations or the supervisor require banks to have appropriate operational risk management strategies, policies and processes to identify, assess, evaluate, monitor, report and control or mitigate operational risk. The supervisor determines that the bank's strategy, policies and processes are consistent with the bank's risk profile, systemic importance, risk appetite and capital strength, take into account market and macroeconomic conditions, and address all major aspects of operational risk prevalent in the businesses of the bank on a bank-wide basis (including periods when operational risk could increase).
Description and findings re EC1	S. 146 and 148 of the MORB outline BSP's expectations on banks' minimum requirements on operational risk management, IT risk management as well as application sections of the MORB specifying the BSP's expectations with respect to a bank's internal control framework pertaining to operational risk (S. 162 and 163 of the MORB) and business continuity management (Circular No. 951). A bank's Board approved policies and processes are expected to be in place and to demonstrate the ability and capacity to adequately identify, assess, evaluate, monitor, report and control or at least mitigate operational risk. Circular No. 958 sets out the standards on customer authentication dealing with cyber related attacks involving fund transfers, payments and other transactions via on-line channels and information security requirements. BSP's onsite annual supervisory examinations review the adequacy of Board approved policies and procedures governing operational risk management practices by reviewing minutes of the Board, incident reporting, risk event database to evaluate how these tools are being utilized. Further, the examiners review the risk control self-assessment conducted by management and how the results are feed into the strategic and capital planning processes to address operational risk. This assessment also takes into consideration factors that could impact the overall operations of the bank, including an assessment of macroeconomic impacts.
EC2	The supervisor requires banks' strategies, policies and processes for the management of operational risk (including the banks' risk appetite for operational risk) to be approved and regularly reviewed by the banks' Boards. The supervisor also requires that the Board oversees management in ensuring that these policies and processes are implemented effectively.
Description and findings re EC2	S. 146 of the MORB outlines BSP's expectations with respect to a Board's duties and responsibilities regarding the effective management of risk on an enterprise-wide basis, including receiving adequate and timely information on material developments in the operational risk profile of the bank together with current and on-going emerging operational risk exposures and vulnerabilities that could negatively impact the bank.

[66/] The Committee has defined operational risk as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. The definition includes legal risk but excludes strategic and reputational risk.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	The supervisor determines that the approved strategy and significant policies and processes for the management of operational risk are implemented effectively by management and fully integrated into the bank's overall risk management process.
Description and findings re EC3	S. 146 of the MORB provides that Boards shall ensure that senior management implement appropriate policies, processes underlying the operational risk management framework and provide a feedback reporting mechanism where employees are able to raise concerns without negative consequences. BSP's on-site annual examination process reviews banks' effectiveness and reliability of operational risk identification and assessment tools and how these tools, together with the information flow, are integrated into the bank's overall risk management framework.
EC4	The supervisor reviews the quality and comprehensiveness of the bank's disaster recovery and business continuity plans to assess their feasibility in scenarios of severe business disruption which might plausibly affect the bank. In so doing, the supervisor determines that the bank is able to operate as a going concern and minimize losses, including those that may arise from disturbances to payment and settlement systems, in the event of severe business disruption.
Description and findings re EC4	S. 128 and Appendix 111 of the MORB provide guidance to D-SIB's with respect to the preparation of recovery plans. Circular No. 951 provides guidelines on business continuity management (BCM) frameworks which are to include: business impact analysis and risk assessment; strategy formulation, plan develop, plan testing and personnel training and plan maintenance. Adequacy and comprehensiveness of the BCM are assessed during on-site examination. This includes a review of the minutes of meetings of committees tasked with BCM oversight and the related policies and procedures. The adequacy of BCP strategies and back-up of critical systems are also assessed through the review of BCP strategies and business impact analysis, as well as ocular visit of the primary site, business recovery center and disaster recovery site. Review of the BCP/DR test results are also conducted for materiality regarding severe business disruption (such as the potential failure of the payment and settlement system (large banks).
EC5	The supervisor determines that banks have established appropriate information technology policies and processes to identify, assess, monitor and manage technology risks. The supervisor also determines that banks have appropriate and sound information technology infrastructure to meet their current and projected business requirements (under normal circumstances and in periods of stress), which ensures data and system integrity, security and availability and supports integrated and comprehensive risk management.
Description and findings re EC5	S. 148 of the MORB sets out BSP's expectations of a bank's IT risk management that recognizes the need for banks to keep abreast of the aggressive and widespread adoption of technology in the financial service industry through the establishment of a robust IT risk management system covering IT governance, risk identification and assessment, IT controls implementation and risk measurement and monitoring. The Core IT Specialist Group of the BSP, now Technology Risk and Innovation Supervision Department, assesses the inherent IT risk of banks based on the IT Profile Scoring Methodology, and classifies them as either "Complex", "Moderate" or "Simple", as provided in the regulations. During on-site examination, examiners evaluate the IT risk management

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	of banks, taking into account their IT profile, and rate them accordingly using the IT rating system. For complex banks, BSP's on-site annual examination includes an effectiveness assessment of whether banks' control practices satisfactorily address the overall IT risk mitigation strategy pertaining to information security, project management/development and acquisition and change management; IT operations, IT outsourcing/vendor management and electronic banking.
EC6	The supervisor determines that banks have appropriate and effective information systems to: (a) monitor operational risk; (b) compile and analyze operational risk data; and, (c) facilitate appropriate reporting mechanisms at the banks' Boards, senior management and business line levels that support proactive management of operational risk.
Description and findings re EC6 Description and findings re EC6	Assessment of the adequacy and effectiveness of a bank's operational risk management framework in relation to the strategies, complexity of operations and risk profile is generally conducted by BSP supervisors during on-site examination. This includes a review of the minutes of meetings, policies, procedures, processes, systems and reports relative to operational risk management. The effectiveness and reliability of operational risk monitoring tools compile and analyze operational risk data are also evaluated and how these tools are appreciated by the Board of directors, senior management and business units through walkthroughs and interviews.
EC7	The supervisor requires that banks have appropriate reporting mechanisms to keep the supervisor apprised of developments affecting operational risk at banks in their jurisdictions.
Description and findings re EC7	S. 146 of the MORB requires banks to notify the appropriate supervising department of the BSP within 10 calendar days from the date of discovery of any operational risk event. S. 173 of the MORB requires banks to report crimes, whether consummated, greater than Php 20,000 and incidents involving material loss, destruction or damage to the bank's property (Php100,000). Circular No. 1019 amends the technology and cyber-risk reporting and notification requirements for banks to include reportable major incidents within 2 hours from discovery with reporting of the nature of the incident and specific system or business function involved (together with additional on-going reporting requirements to the BSP.
EC8	The supervisor determines that banks have established appropriate policies and processes to assess, manage and monitor outsourced activities. The outsourcing risk management program covers: (a) conducting appropriate due diligence for selecting potential service providers; (b) structuring the outsourcing arrangement; (c) managing and monitoring the risks associated with the outsourcing arrangement; (d) ensuring an effective control environment; and, (e) establishing viable contingency planning. Outsourcing policies and processes require the bank to have comprehensive contracts and/or service level agreements with a clear allocation of responsibilities between the outsourcing provider and the bank.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC8	S. 112 of the MORB as amended by Circular No. 899 outlines the BSP's expectations of banks' management of outsourcing risk. Adequacy of banks' outsourcing framework, governance and risk management relative to outsourcing activities are assessed during BSP's on-site examination. This includes a review of the minutes of meetings, service level agreements, policies and procedures, audit reports and monitoring reports relative to outsourcing activities. The examination also evaluates the selection criteria and performance review of the service provider/s, as well as the business continuity and contingency plans in case the service provider is not able to deliver the required services. In the past, Assessors noted that the BSP has raised issues on the adequacy of governance/oversight of outsourcing activities, criteria to select the "best" service provider, business continuity and contingency plans, and performance evaluation of the service provider.
Assessment of Principle 25	Compliant
Comments	BSP's regulatory requirements pertaining to banks' operational risk management framework appear to be adequate. Assessors noted BSP's plans to augment IT technical expertise relating to developments in financial technology and cyber related risk.
Principle 26	**Internal control and audit**. The supervisor determines that banks have adequate internal control frameworks to establish and maintain a properly controlled operating environment for the conduct of their business taking into account their risk profile. These include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding the bank's assets; and appropriate independent[67/] internal audit and compliance functions to test adherence to these controls as well as applicable laws and regulations.
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to have internal control frameworks that are adequate to establish a properly controlled operating environment for the conduct of their business, taking into account their risk profile. These controls are the responsibility of the bank's Board and/or senior management and deal with organizational structure, accounting policies and processes, checks and balances, and the safeguarding of assets and investments (including measures for the prevention and early detection and reporting of misuse such as fraud, embezzlement, unauthorized trading and computer intrusion). More specifically, these controls address: (a) organizational structure: definitions of duties and responsibilities, including clear delegation of authority (e.g., clear loan approval limits), decision-making policies and processes, separation of critical functions (e.g., business origination, payments, reconciliation, risk management, accounting, audit and compliance); (b) accounting policies and processes: reconciliation of accounts, control lists, information for management; (c) checks and balances (or "four eyes principle"): segregation of duties, cross-checking, dual control of assets, double signatures; and (d) safeguarding assets and investments: including physical control and computer access. [67/] In assessing independence, supervisors give due regard to the control systems designed to avoid conflicts of interest in the performance measurement of staff in the compliance, control and internal audit functions. For example, the remuneration of such staff should be determined independently of the business lines that they oversee.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Circular No. 871 outlines BSP's expectation of banks regarding internal control and internal audits specifying that banks should have an adequate and effective internal control framework, risk recognition and assessment, control activities, information and communication; and monitoring activities and correcting deficiencies. There is no "one size fits all" internal control framework, therefore the internal control framework should be proportional to the size, risk profile and complexity of operations of the financial institution. Specifically, banks are required (S. 162 of the MORB) to: (a) maintain an organizational structure that clearly assigns responsibility, authority and reporting relationships; ensure that delegated responsibilities are effectively carried out; (b) have adequate accounting policies, records and processes; (c) have control activities to include the segregation of conflicting functions; (d) have control activities to include robust physical and environmental controls to tangible assets and access controls to information assets.
EC2	The supervisor determines that there is an appropriate balance in the skills and resources of the back office, control functions and operational management relative to the business origination units. The supervisor also determines that the staff of the back office and control functions have sufficient expertise and authority within the organization (and, where appropriate, in the case of control functions, sufficient access to the bank's Board) to be an effective check and balance to the business origination units.
Description and findings re EC2	Circular 871 provides that senior management of banks are to implement internal control policies and ensure that activities are to be conducted by qualified personnel with the necessary experience and competence. Management shall ensure that bank personnel undertake continuing professional development and that there is an appropriate balance in the skills and resources of the front office, back office, and control functions. In addition, management are required to promptly inform the internal audit function of the significant changes in the bank's risk management systems, policies and processes. BSP's annual on-site examination reviews the adequacy of banks' internal control policies and determines if a bank's staff have sufficient expertise, segregation of duties and that the control functions have the ability/access to inform senior management and the Board of relevant issues.
EC3	The supervisor determines that banks have an adequately staffed, permanent and independent compliance function[68/] that assists senior management in managing effectively the compliance risks faced by the bank. The supervisor determines that staff within the compliance function are suitably trained, have relevant experience and have sufficient authority within the bank to perform their role effectively. The supervisor determines that the bank's Board exercises oversight of the management of the compliance function.
Description and findings re EC3	S. 161 of the MORB outlines BSP's expectations regarding banks' establishment of compliance functions. ____________________ [68/] The term "compliance function" does not necessarily denote an organizational unit. Compliance staff may reside in operating business units or local subsidiaries and report up to operating business line management or local management, provided such staff also have a reporting line through to the head of compliance who should be independent from business lines.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC3	Adequacy and effectiveness of the compliance function is assessed during BSP's on-site examinations. This includes a review of the charter, organizational structure, reporting lines and minutes of Board or Board-level committee meetings to assess authority and independence of the compliance function. The examination also reviews the compliance manual, plan and reports. Adequacy and competency of personnel assigned in the compliance function is also evaluated through the review of the table of organization, biographical or personnel data, trainings and continuous professional development. Accomplishments vis-à-vis plans/targets is also reviewed to determine adequacy of personnel as well as the review of the compliance reports also gives an indication on the competency of personnel assigned in the compliance function.
EC4	The supervisor determines that banks have an independent, permanent and effective internal audit function[69/] charged with: (a) assessing whether existing policies, processes and internal controls (including risk management, compliance and corporate governance processes) are effective, appropriate and remain sufficient for the bank's business; and, (b) ensuring that policies and processes are complied with.
Description and findings re EC4	In general, banks may outsource internal audit activities except for areas covered by existing statutes on deposit secrecy, to have access to certain areas of expertise or to address resource constraints. Considering the size and risk profile of non-complex thrift, rural and cooperative banks, they are allowed to outsource internal audit activities covering all areas of bank operations except for areas covered by existing statutes on deposit secrecy, provided that the audit committee shall take on additional responsibilities such as, among others, developing an audit plan. The independence, permanency and effectiveness of the IA function is assessed during BSP's on-site examination through the review of the charter, organizational structure, reporting lines and minutes of Board or Board-level committee (i.e., Audit Committee). To assess whether existing polices, processes and internal controls are effective and complied with, the examination reviews the internal audit manual, methodologies, risk rating system, audit plan, audit reports and monitoring/tracking of open audit issues.
EC5	The supervisor determines that the internal audit function: (a) has sufficient resources, and staff that are suitably trained and have relevant experience to understand and evaluate the business they are auditing; (b) has appropriate independence with reporting lines to the bank's Board or to an audit committee of the Board, and has status within the bank to ensure that senior management reacts to and acts upon its recommendations; (c) is kept informed in a timely manner of any material changes made to the bank's risk management strategy, policies or processes; (d) has full access to and communication with any member of staff as well as full access to records, files or data of the bank and its affiliates, whenever relevant to the performance of its duties;

[69/] The term "internal audit function" does not necessarily denote an organizational unit. Some countries allow small banks to implement a system of independent reviews, e.g., conducted by external experts, of key internal controls as an alternative.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC5	(e) employs a methodology that identifies the material risks run by the bank; (f) prepares an audit plan, which is reviewed regularly, based on its own risk assessment and allocates its resources accordingly; and, (g) has the authority to assess any outsourced functions.
Description and findings re EC5	BSP's on-site annual examination determines the effectiveness of the IA function by assessing: (a) the education/experience/training and understanding of IA personnel's understanding of the risk exposures of the bank and whether the overall audit function possesses sufficient resources; (b) the degree of independence by determining if IA is free to report audit results directly to the Board or audit committee and its ability to examine any activity or entity of the bank, including direct access to key staff; (c) IA's ability to be kept closely informed of material changes in a bank's business strategy through contact with the compliance function and EA on operational risk matters; (d) IA's ability to communicate directly to staff, including access to critical data, records, files whenever relevant to the exercise of its assignment; (e) + (f) IA's ability to develop an audit plan based on robust risk assessment inputs from the Board, audit committee and senior management to ensure the plan is comprehensive and adequately covers regulatory matters; and, (f) IA's ability to access any outsources services, including all processes, and activities.
Assessment of Principle 26	Compliant
Comments	BSP's regulatory framework and annual on-site examination processes provide supervisors with an adequate view of the effectiveness of a bank's internal control frameworks and IA function. BSP has updated its requirements pertaining to a bank's compliance function and updated its supervisory assessment approach to address prior BCP assessment findings.
Principle 27	**Financial reporting and external audit**. The supervisor determines that banks and banking groups maintain adequate and reliable records, prepare financial statements in accordance with accounting policies and practices that are widely accepted internationally and annually publish information that fairly reflects their financial condition and performance and bears an independent external auditor's opinion. The supervisor also determines that banks and parent companies of banking groups have adequate governance and oversight of the external audit function.
Essential criteria	
EC1	The supervisor[70/] holds the bank's Board and management responsible for ensuring that financial statements are prepared in accordance with accounting policies and practices that are widely accepted internationally and that these are supported by recordkeeping systems in order to produce adequate and reliable data.

[70/] In this Essential Criterion, the supervisor is not necessarily limited to the banking supervisor. The responsibility for ensuring that financial statements are prepared in accordance with accounting policies and practices may also be vested with securities and market supervisors.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	Appendix 39 of S. 164 of the MORB states that financial statements filed with the BSP are primarily the responsibility of the management of the reporting institution. S. 172 of the MORB requires banks to adopt PFRS and PAS. A 2017 ROSC concluded that the Philippines has a comprehensive accounting and auditing framework, established standards, and mature institutions to support its sophisticated capital market structure and well-developed financial sector. National accounting and auditing standards are substantially equivalent to international principles and many elements of international good practice are in place to foster reliable and efficient corporate financial reporting. S. 162 of the MORB sets out guidelines which specifically require banks to maintain adequate financial policies, records and processes to ensure the integrity of reported data and balances as well as minimum internal controls to ensure independent balancing, separation of recording and physical handling of transactions, joint custody over important records and resources as well as dual control over certain accounts/transactions. This is supported by Circular 963, which requires the Board and senior management to implement an effective reporting system to generate complete, accurate, consistent, reliable and timely reports. Banks are required to ensure that IT systems provide an effective reporting system that is appropriate for their size and complexity of operations. The integrity of a bank's financial data and reporting systems is assessed during on-site examination through validation and verification of reports against supporting documents/schedules, analytical review or trending analysis, reasonableness tests of balances, and review of the process on preparation of bank reports.
EC2	The supervisor holds the bank's Board and management responsible for ensuring that the financial statements issued annually to the public bear an independent external auditor's opinion as a result of an audit conducted in accordance with internationally accepted auditing practices and standards.
Description and findings re EC2	S. 174 of the MORB requires a bank to undertake an annual financial audit conducted in line with PAS on its financial statements by an external auditor acceptable to the BSP, not later than 30 calendar days after the close of its calendar/fiscal year. The report should be submitted to the Board and to the BSP not later than 120 calendar days after the close of its calendar/fiscal year. The report should be accompanied by: (1) Certification by the external auditor on the: (1) dates of start and termination of audit; (2) date of submission of the financial audit report and certification under oath stating that no material weakness or breach in the internal control and risk management systems was noted in the course of the audit of the bank to the Board of directors or country head; and (3) the absence of any direct or indirect financial interest and other circumstances that may impair the independence of the external auditor; (2) A Reconciliation Statement between the Annual Financial Statement and the balance sheet and income statement including copies of adjusting entries on the reconciling items; and, (3) Other information that may be required by the BSP.
EC3	The supervisor determines that banks use valuation practices consistent with accounting standards widely accepted internationally. The supervisor also determines that the

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	framework, structure and processes for fair value estimation are subject to independent verification and validation, and that banks document any significant differences between the valuations used for financial reporting purposes and for regulatory purposes.
Description and findings re EC3	Appendix 27 under S. 172 of the MORB aligns local financial accounting standards with international accounting standards and Circular 1021 sets out guidelines on the marking-to-market of financial instruments to align existing regulations with the provisions of PFRS 13 on Fair Value Measurement. Circular 1011 provides guidelines on the adoption of PFRS 9 on expected credit losses. It states that banks should adopt PFRS in recording transactions and in the preparation of financial statements and reports to the BSP. Where there are differences between BSP regulations and PFRS and when there is more than one option allowed or certain maximum or minimum limits are prescribed by PFRS, the option or limit prescribed by the BSP should be adopted by banks. When adopting the new impairment requirements under PFRS 9, the BSP has maintained a 1.0 percent minimum provision on all on-balance sheet loans as a regulatory backstop to ensure that banks maintain adequate allowances for credit losses. Banks are required to provide an annual reconciliation to the BSP of any differences between their financial accounting and regulatory reporting frameworks. Memorandum M-2014-011 requires the external auditor to evaluate whether the methodologies, assumptions and valuation practices, including provisioning for loan losses, are appropriate and consistent with the applicable financial reporting framework. While the provisioning requirements under the prescribed financial reporting framework and BSP rules and regulations may differ, external auditors are expected to look into the soundness of the assumptions and methodologies used under both regimes. In addition, external auditors should also look into the adequacy and propriety of documentation of significant differences between the valuations used for financial reporting purposes and for regulatory purposes.
EC4	Laws or regulations set, or the supervisor has the power to establish the scope of external audits of banks and the standards to be followed in performing such audits. These require the use of a risk and materiality-based approach in planning and performing the external audit.
Description and findings re EC4	The Auditing Assurance Standards Council (AASC) is the body authorized to establish and promulgate generally accepted auditing standards in the Philippines. It is the stated policy of the AASC to make International Standards and Practice Statements issued by the IAASB the applicable standards and practice statements in the Philippines. As noted in EC1, a 2017 ROSC on the accounting and auditing environment in the Philippines found that national accounting and auditing standards are substantially equivalent to international principles and many elements of international good practice are in place to foster reliable and efficient corporate financial reporting. The one notable exception is in the underlying legal framework necessary to enable an independent system of oversight over the quality of audits. The specific standards applicable to the conduct of external audits include: (i) Philippine Standards on Auditing (PSAs); and, (ii) Philippine Standards on Review Engagement.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC4	PSA 300 on planning an audit of financial statements requires an auditor to develop a plan that shall include a description of: • The nature, timing and extent of planned risk assessment procedures, as determined under PSA 315, "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment." PSA 315 states that the objective of the auditor is to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels, through understanding the entity and its environment, including the entity's internal control, thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement. • The auditor shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. The risk assessment procedures include inquiries of management and other concerned officers, analytical procedures, observation and inspection. • The nature, timing and extent of planned further audit procedures at the assertion level, as determined under PSA 330, "The Auditor's Responses to Assessed Risks." • The auditor shall design and perform further audit procedures whose nature, timing, and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. • Other planned audit procedures that are required to be carried out so that the engagement complies with PSAs. PSA 320 requires the application of the concept of materiality in planning and performing an audit. In planning the audit, the auditor makes judgments about the size of misstatements that will be considered material. These judgments provide a basis for: 1. Determining the nature, timing and extent of risk assessment procedures; 2. Identifying and assessing the risks of material misstatement; and 3. Determining the nature, timing and extent of further audit procedures.
EC5	Supervisory guidelines or local auditing standards determine that audits cover areas such as the loan portfolio, loan loss provisions, non-performing assets, asset valuations, trading and other securities activities, derivatives, asset securitizations, consolidation of and other involvement with off-balance sheet vehicles and the adequacy of internal controls over financial reporting.
Description and findings re EC5	S. 174 of the MORB requires audits to be conducted in accordance with established quality assurance procedures covering the following areas of operation: 1. asset quality, 2. adequacy of risk-based capital, 3. risk management systems, and, 4. corporate governance framework of banks/quasi-banks. It also requires banks to submit a report on its annual financial audit, accompanied by a certification under oath by the external auditor stating that there are no material weakness or breach in the internal control and risk management systems noted in the course of the audit of the bank.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	Memorandum 2014-011 cites examples of key audit areas and exposures that merit special audit consideration for a bank. These include, but are not limited to, impairment and loan loss provisioning, financial instruments measured at fair value, liabilities, related party transactions and disclosures. In addition, Appendix 39 of the MORB requires the external auditor's work program to be submitted to the BSP, evidencing the audited institution's compliance with BSP rules and regulations, including the following: 1. capital adequacy ratio, as currently prescribed by the BSP; 2. AMLA framework; 3. risk management system, particularly liquidity and market risks; and, 4. loans and other risk assets review and classification, as currently prescribed by BSP rules and regulations. Banks' annual financial reports are reviewed by supervisors in accordance with SG Nos. 2008-019 and 2009-27. These SGs serve as a guide for off-site supervisors in undertaking an evaluation of the audited financial statements. Evidence from files confirmed that the BSP evaluates the quality and coverage of a bank's external audit.
EC6	The supervisor has the power to reject and rescind the appointment of an external auditor who is deemed to have inadequate expertise or independence, or is not subject to or does not adhere to established professional standards.
Description and findings re EC6	S. 164 and Appendix 39 of the MORB govern the selection and delisting by the BSP of external auditors and auditing firms. The following qualification requirements, among others, are required to be met by the individual external auditor and the auditing firm at the time of application and on continuing basis: a. Accredited by the Board of Accountancy; b. At least five years of audit experience; c. Independent; and, d. Must have established adequate quality assurance procedures to ensure full compliance with accounting and regulatory requirements. The following are the grounds for delisting and suspension: a. Failure to submit required reports; b. Continuous conduct of audit despite loss of independence, c. Willful misrepresentation to the BSP; d. Commission of an act that is discreditable to the profession as determined by the Board of Auditors, after due notice and hearing; e. Commission of a crime that is declared by a competent court involving moral turpitude, fraud or liability for violation of laws, rules and regulations; f. Refusal, for no valid reason, to submit documents in connection with an ongoing investigation; g. Gross negligence in the conduct of audit which would result to non-compliance with generally accepted auditing standards or issuance of an unqualified opinion that is not supported by full compliance by the auditee of generally accepted accounting principles; h. Failure to comply with PASs and Philippine Auditing Practice Statements; and,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC6	i. Conduct of non-audit services without undertaking safeguards to reduce threat to his independence. The accreditation of external auditors for a bank is currently handled by the External Auditor Selection Team in the BSP but, from June 2019, a single accreditation framework across different regulatory agencies (i.e., SEC, BSP, IC and PDIC) is to be implemented. As the designated central agency to accept applications, the SEC will set out the accreditation/selection process that include minimum documentary requirements. The BSP has issued regulations on the adoption of the revised appointment framework. The single accreditation framework has been introduced to reduce the burden on industry, which currently has to apply for accreditation to each of the domestic regulators. The 'one-stop' shop will remove this duplication. The BSP retains a veto on the accreditation of an external auditor in the new system, should it not approve an individual or firm. The selection of external auditors and/or auditing firm is valid for a period of five years. Supervisors are required to make an annual assessment of the performance of external auditors and/or auditing firm and may recommend deletion from the list even prior to the three-year renewal period if the external auditors' report did not comply with the BSP requirements. Evidence was cited of the BSP delisting an audit firm for failing to meet the required standards.
EC7	The supervisor determines that banks rotate their external auditors (either the firm or individuals within the firm) from time to time.
Description and findings re EC7	Appendix 39 of the MORB requires the external auditor and/or auditing firm to be changed, or the lead partner shall be rotated every five years or earlier, provided further that the rotation of the lead partner shall have an interval of at least two years. The rotation policy is reviewed by the BSP as part of its routine supervisory process.
EC8	The supervisor meets periodically with external audit firms to discuss issues of common interest relating to bank operations.
Description and findings re EC8	Routine meetings with external auditors do not form part of the supervisory process, but meetings are convened between the two parties on an ad hoc basis, generally to discuss issues around the accounting treatment of certain financial transactions and less so to discuss specific supervisory concerns. Such meetings are held without any representation from the bank concerned. Memorandum M-2014-011 sets out the following principles which frame the relationship: a. The complementary role of the BSP and the external auditors are ingrained in existing statutes. b. The external auditors reporting on adverse findings as prescribed under existing BSP regulations is useful to the ongoing monitoring of BSP on financial condition and risk profile of financial institutions. c. The BSP engages external auditors in discussion involving accounting issues, to arrive at a consensus regarding the treatment of certain banking transactions. d. In many respects, the BSP and the external auditor have complementary concerns regarding the same matters, though the focus of their concerns is different.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC8	e. The external auditor can benefit from the work of the BSP. Significant supervisory issues raised by the BSP could inform the scope of the audit in assessing the going concern assumption used by financial institutions. The Memorandum also provides the external auditor with authority to have read-access to the BSP's ROE on a bank when conducting its audit. Any concerns identified in the ROE may inform the scope of the audit. A decision of the MB prevents supervisors from discussing any supervisory concerns it has with an external auditor due to legal prohibitions and limitations set out in S. 27 and 28 of the NCBA. The constraints imposed on sharing supervisory information with external auditors inhibits effective dialogue between the two parties. A review into establishing more effective working arrangements with external auditors on the sharing of information in the ROE has been initiated by the MB. Formal information sharing arrangements should be established between the two parties to facilitate such dialogue. The BSP may wish also to consider introducing routine meetings (at least on an annual basis) with the external audit firms of banks as part of the supervisory process.
EC9	The supervisor requires the external auditor, directly or through the bank, to report to the supervisor matters of material significance, for example failure to comply with the licensing criteria or breaches of banking or other laws, significant deficiencies and control weaknesses in the bank's financial reporting process or other matters that they believe are likely to be of material significance to the functions of the supervisor. Laws or regulations provide that auditors who make any such reports in good faith cannot be held liable for breach of a duty of confidentiality.
Description and findings re EC9	Circular 1040 requires external auditors to report to the BSP any matter affecting the soundness or condition of a bank/quasi-bank, such as, but not limited to the following: 1. Within 15 calendar days after discovery— (i) Any material finding involving fraud or error; (ii) Actual or potential losses, the aggregate of which amounts to at least ten percent (10%) of the consolidated total assets of the BSFI; (iii) Significant doubt as to the ability of the BSFI to continue as a going concern; (iv) Material breach of laws or BSP rules and regulations such as but not limited to prescribed capital and liquidity ratios, significant deficiency in allowance for credit losses, material weaknesses in fair value measurement methodology, and significant vulnerabilities to money laundering and combating the financing of terrorism; (v) Material internal control weaknesses which may lead to financial reporting problems; and (vi) Findings on matters of corporate governance that may require urgent action by the BSP. The 15 calendar-day period provides time for the external auditor to investigate the issue and to establish whether there is substance to it. In practice, material concerns would be reported immediately. Appendix 39 of the MORB prescribes that the audit engagement contract between the audit firm and the bank should include a provision that states

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC9	disclosures by the external auditor to the BSP should be allowed. Bank management is required to be present during discussions or at least be informed of the adverse findings in order to preserve the concerns of the supervisory authority and external auditors regarding the confidentiality of information, except in cases where the external auditor believes that the entity's management is engaged in fraudulent conduct. Section 174 of the MORB provides that the disclosure of an external auditor's adverse findings to the BSP should not be a ground for civil, criminal or disciplinary proceeding against the audit firm. In practice there have been very few occasions when auditors have contacted the BSP to report matters of material significance.
Assessment of Principle 27	Largely compliant
Comments	Banks' financial reporting requirements are in accordance with international standards. The BSP does not engage with external auditors on a regular basis as part of the routine supervisory process. Although external auditors have access to the BSP's Reports of Examination, there are constraints imposed on supervisors sharing information on a bank with external auditors as part of an ongoing dialogue. A review into establishing more effective working arrangements with external auditors on the sharing of information has been initiated by the MB. Recommendations: • Remove any constraints on information sharing between BSP supervisors and external auditors • Introduce routine meetings between BSP supervisors and external auditors as part of the supervisory process.
Principle 28	**Disclosure and transparency**. The supervisor determines that banks and banking groups regularly publish information on a consolidated and, where appropriate, solo basis that is easily accessible and fairly reflects their financial condition, performance, risk exposures, risk management strategies and corporate governance policies and processes.
Essential criteria	
EC1	Laws, regulations or the supervisor require periodic public disclosures[71/] of information by banks on a consolidated and, where appropriate, solo basis that adequately reflect the bank's true financial condition and performance, and adhere to standards promoting comparability, relevance, reliability and timeliness of the information disclosed.
Description and findings re EC1	S. 61 of the GBL requires banks to publish a statement of their financial condition, including those of their subsidiaries and affiliates, at least once every quarter, in a newspaper of general circulation in the city or province where the bank's principal office is located. S. 175 of the MORB implements S. 61 of the GBL. Banks with resources of P1 billion and above are required to publish their solo and consolidated balance sheets, where applicable, in a newspaper of general circulation. Banks with resources of less than P1 billion may either publish their financial reports in a newspaper of general circulation or in their bank [71/] For the purposes of this Essential Criterion, the disclosure requirement may be found in applicable accounting, stock exchange listing, or other similar rules, instead of or in addition to directives issued by the supervisor.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	premises. S. 174 of the MORB requires similar disclosure requirements for foreign bank branches in all their banking offices in the Philippines. To promote consistency and comparability between banks, Circular 956 provides guidelines on the scope of the disclosures in annual reports and the sanctions to be imposed for non-disclosure of relevant information. The disclosures should cover, inter alia, the bank's financial condition, performance, ownership, the risk management framework, and governance.
EC2	The supervisor determines that the required disclosures include both qualitative and quantitative information on a bank's financial performance, financial position, risk management strategies and practices, risk exposures, aggregate exposures to related parties, transactions with related parties, accounting policies, and basic business, management, governance and remuneration. The scope and content of information provided, and the level of disaggregation and detail is commensurate with the risk profile and systemic importance of the bank.
Description and findings re EC2	S. 175 of the MORB sets out the minimum disclosure requirements for banks. These cover the bank's corporate policy; a detailed financial summary of its profitability, capital, performance and balance sheet data/ratios; its financial condition and results of operations; the risk management framework; the corporate governance framework, including policies on related party transactions; and corporate information on the structure and shareholdings of the group. In addition, S. 174 of the MORB requires all banks to disclose the following additional information in their notes to audited financial statements: a. Basic quantitative indicators of financial performance such as return on average equity, return on average assets and net interest margin; b. Risk-based capital adequacy ratio; c. Concentration of credit as to industry/economic sector; d. Breakdown of total loans as to secured and unsecured and breakdown of secured loans as to type of security; e. Total outstanding loans to bank's DOSRI, percent of DOSRI loans to total loan portfolio, percent of unsecured DOSRI loans to total DOSRI loans, percent of past due DOSRI loans to total DOSRI loans and percent of non- performing DOSRI loans to total DOSRI loans; f. Nature and amount of contingencies and commitments arising from off- balance sheet items [include direct credit substitutes (e.g., export LCs confirmed, underwritten accounts unsold), transaction-related contingencies (e.g., performance bonds, bid bonds, standby LCs), short- term self-liquidating trade-related contingencies arising from the movement of goods (e.g., sight/ usance domestic LCs, sight/usance import LCs), sale and repurchase agreements not recognized in the balance sheet; interest and foreign exchange rate related items; and other commitments; g. Provisions and allowances for losses and how these are determined; h. Aggregate amount of secured liabilities and assets pledged as security; and, i. Accounting policies which shall include, but shall not be limited to, general accounting principles, changes in accounting policies/practices, principles of consolidation, policies and methods for determining when assets are impaired, recognizing income on impaired assets and losses on non-performing credits, income recognition, valuation

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC2	policies and accounting policies on securitizations, foreign currency translations, loan fees, premiums and discounts, repurchase agreements, premises/fixed assets, income taxes and derivatives. Pillar 3 requirements apply to all banks, but the disclosure requirements for stand-alone thrift, rural and cooperative banks are less onerous for universal and commercial banks. The requirements are set out Part IX of Appendix 59 of the MORB. They are not compliant with the latest Basel III Pillar 3 requirements, which set out a detailed set of quantitative and qualitative disclosures covering the composition of a bank's capital, leverage and liquidity data, credit risk, counterparty credit risk, market risk, IRRBB, and remuneration. The existing disclosure requirements for universal and commercial banks cover elements of the Pillar 3 disclosure regime, but the coverage is not as comprehensive. The BSP is, however, revising its disclosure regime to align the requirements with the applicable BCBS standard.
EC3	Laws, regulations or the supervisor require banks to disclose all material entities in the group structure.
Description and findings re EC3	S. 5 (O) (ii) in Annex A-1 of Circular 965 requires all universal and commercial banks that are part of conglomerates to disclose in their annual report all entities in the group's wider conglomerate structure. The report on a bank's conglomerate structure is required to be submitted to the BSP within thirty calendar days after the end of every calendar year. Banks are also required to disclose in their Consolidated Balance Sheet a list of all financial allied subsidiaries and their policies and procedures for managing RPTs, including managing of conflicts of interest or potential conflicts of interest; responsibility of the RPT Committee; nature, terms and conditions, as well as original and outstanding individual and aggregate balances, including off-balance sheet commitments, of material RPTs.
EC4	The supervisor or another government agency effectively reviews and enforces compliance with disclosure standards.
Description and findings re EC4	Circular 956 and Memorandum No. M-2017-011 set out a detailed checklist of the disclosures that banks are required to include in their annual financial report and the sanctions to be imposed for non-disclosure. SGs 2008-019 and 2009-27 specify the form of detailed evaluation undertaken by the BSP staff to ensure compliance by banks with the disclosure standards. Information provided by banks in their published balance sheet/consolidated balance sheet is validated automatically against information provided in other prudential reports.
EC5	The supervisor or other relevant bodies regularly publishes information on the banking system in aggregate to facilitate public understanding of the banking system and the exercise of market discipline. Such information includes aggregate data on balance sheet indicators and statistical parameters that reflect the principal aspects of banks' operations (balance sheet structure, capital ratios, income earning capacity, and risk profiles).
Description and findings re EC5	The BSP publishes regular information on the banking system on its website. Such information includes aggregate statistical data on the following: 1. Balance sheet data, 2. Income statement data, 3. Selected performance indicators, such as asset quality, liquidity, profitability and capital adequacy ratios, 4. Trust and other fiduciary business and other management activities,

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	5. Mandated credit, and, 6. Selected information on loan accounts, deposit accounts and physical network. The BSP also regularly publishes the following reports: 1. A semi-annual Report on the Philippine Financial System; and 2. A factbook on the Philippine Banking System, which is a compilation of various information and statistical data of the BSP supervised financial institutions such as the Physical Network and Directory, Aggregated Balance Sheet and Income Statement, Regional Distribution of Selected Accounts, individual Published Balance Sheet of Universal/Commercial/Thrift Banks and Summary Report on Compliance with Agri-Agra and MSME. The FSCC also prepares and publishes an FSR on an annual basis. This report details developments and risks to the banking system. The first FSR was published in June 2018.
Assessment of Principle 28	Largely compliant
Comments	The BSP prescribes detailed public disclosure requirements for banks on both a consolidated and solo basis and verifies that these requirements are met. The disclosure regime is not as comprehensive as the current BCBS Pillar 3 framework in terms of the scope and detail of coverage required across a number of risk elements (e.g. for NSFR, market risk, IRRBB and remuneration). The BSP is, however, revising its disclosure regime to align the requirements with the applicable BCBS standard. Recommendation: • Issue proposals on a revised Pillar 3 framework.
Principle 29	**Abuse of financial services**. The supervisor determines that banks have adequate policies and processes, including strict customer due diligence (CDD) rules to promote high ethical and professional standards in the financial sector and prevent the bank from being used, intentionally or unintentionally, for criminal activities.[72/]
Essential criteria	
EC1	Laws or regulations establish the duties, responsibilities and powers of the supervisor related to the supervision of banks' internal controls and enforcement of the relevant laws and regulations regarding criminal activities.
Description and findings re EC1	S. 4 of the GBL outlines BSP's general supervisory powers over banks. The anti-money laundering legislation in the Philippines is RA No. 9160, otherwise known as the "Anti-Money Laundering Act of 2001" (AMLA), as amended, provides the criminalization of money laundering and the preventive measures, such as customer identification and verification, record keeping and reporting of covered and suspicious transactions, that must be complied by covered persons or reporting entities. The AMLA __________ [72/] The Committee is aware that, in some jurisdictions, other authorities, such as a financial intelligence unit (FIU), rather than a banking supervisor, may have primary responsibility for assessing compliance with laws and regulations regarding criminal activities in banks, such as fraud, money laundering and the financing of terrorism. Thus, in the context of this Principle, "the supervisor" might refer to such other authorities, in particular in Essential Criteria 7, 8 and 10. In such jurisdictions, the banking supervisor cooperates with such authorities to achieve adherence with the criteria mentioned in this Principle.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	has been amended several times to conform with international standards set by the Financial Action Task Force (FATF). The Implementing Rules and Regulations (IRR) of the AMLA which provide more details on regulations for the effective implementation of the law was issued in 2001. The IRR was further revised in 2003, 2012 and 2016 in light of the amendment to the AMLA. The 2016 IRR was updated in 2018 through the promulgation of the 2018 Implementing Rules and Regulations (IRR) of the AMLA known as the "2018 AMLA IRR". RA No. 10168 or The Terrorism Financing Prevention and Suppression Act of 2012 and s. 7 of the AMLA authorizes the Anti-Money Laundering Council (AMLC), among other things, to investigate financing of terrorism, enlist the assistance of any branch, department, bureau, office, agency or instrumentality of the government, in undertaking measures to counter terrorism financing such as the freezing and forfeiture of properties or funds. The BSP oversee the compliance of all AML/CFT requirements for the operations: of banks, quasi-banking and non-banking entities, money service businesses (MSBs), credit granting businesses and payment system operators. (See paragraphs below that outline BSP's authority to ensure bank's compliance with AML/CFT requirements) Circular No 706, otherwise known as the "Updated AML Rules and Regulations (UARR)" was implemented in 2011 by the BSP to ensure banks fully complied with the provisions of the AMLA, as amended and its IRR. Circular No. 950 was issued in 2017 by the BSP to strengthen both its risk-based regulations and to align its rules with international standards. Circular No. 706 and No. 950 are incorporated into the MORB (Part 9, 2017). However, with the promulgation of the 2018 AMLA IRR, the UARR, as amended, was further updated by Circular No. 1022 in 2018 (which will be incorporated into the MORB when next updated). The Customer Due Diligence (CDD) and Know-your-customer (KYC) requirements, as provided in S. 3, Rule 18, Chapter VI of the 2018 AMLA IRR are embedded in BSP's Circular No. 706 as amended outlining expectations of banks to meet these requirements. S. 7(1) of the AMLA stipulates the authority of the AMLC to require and receive covered transactions reports or suspicious transaction reports (CTRs/STRs) from covered persons. Several pertinent sections and rules of the AMLA define suspicious transactions (S. 3(b-1); Rule 2, 22) wherein banks are required to report CTRs/STRs directly to the AMLC on a timely basis. BSP's AML/CFT risk-based supervisory framework and on-site examination program consists of the following: (a) establishment of a dedicated unit for AML examination, entitled the Financial System Integrity Department under FSS (Currently 51 (approved 79) AML specialists with the requisite qualifications/robust continuing education program) which focuses on the compliance of banks to AML/CFT requirements. Note the non-banking supervision group will oversee the implementation of BSP's AML/CFT requirements pertaining to money

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC1	service businesses, credit granting businesses and payment system operators (banking AML experts will provide training but not carry out the supervisory review/oversight function). (b) on-site examination framework that in general assesses the adequacy of banks' controls and systems to prevent, identify and report potential abuses of financial services, including ML and FT. Although the AML risk assessment (AML Risk Rating System (ARRS) is separate and distinct from the overall risk assessment of a bank's risk profile, the AML section of the ROE provides an overview of AML assessment, nature of AML weaknesses/findings are distinctively noted with corresponding directives/remedial actions. BSP applies a risk-based approach in the examination of banks, MSBs and trust entities including a determination to carry out a full scope AML/CFT examination or a focused examination. Banks rated "4" (assessed as having sound ML/TF risk management and prevention framework) will be subject to an on-site examination every three years whereas banks rated 3 on-site examinations to be conducted every two years versus higher risk banks will have more attention. AML specialists provide technical assistance to front line examiners of smaller banks in order to ensure broadly that they are in compliance with BSP's AML/CFT regulatory requirements. BSP's AML experts are encouraged to conduct thematic reviews on a consistent basis in order to increase its understanding of sector and cross sector risks which would assist bank supervisors of potential risk impact on the BSP supervised entities. BSP AML experts would benefit from views/inputs from other regulatory authorities, including the AMLC. Although the BSP makes adequate use of its supervisors to oversee the AML/CFT supervisory framework for smaller banks, the total number of AML experts needs to be reexamined in light of its additional AML/CFT supervisory oversight of new entities.
EC2	The supervisor determines that banks have adequate policies and processes that promote high ethical and professional standards and prevent the bank from being used, intentionally or unintentionally, for criminal activities. This includes the prevention and detection of criminal activity, and reporting of such suspected activities to the appropriate authorities.
Description and findings re EC2	S. 911 of the MORB, as amended by Circular Nos. 706 and 950, requires BSP covered institutions to adopt a comprehensive and risk-based Money Laundering and Terrorist Financing Prevention Program (MTPP per Circular No. 1022, previously referred to as MLPP) geared toward the promotion of high ethical and professional standards and the prevention of the bank being used, intentionally or unintentionally, for ML/TF. S. 911 of the MORB states that the MTPP shall include policies, controls and procedures to enable covered persons to manage the risks that have been identified in their risk assessment, including taking enhanced measures for those classified as posing higher risks. BSP's AML on-site examiners review the adequacy of banks' policies and processes that should promote high ethical and professional standards as well as assessing the strength of a bank's ability to prevent, detect criminal activity and report on suspicious transactions.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC3	In addition to reporting to the financial intelligence unit or other designated authorities, banks report to the banking supervisor suspicious activities and incidents of fraud when such activities/incidents are material to the safety, soundness or reputation of the bank.[73/]
Description and findings re EC3	All suspicious activities under the AMLA are reported by banks to the AMLC. Banks are duty-bound to submit reports or advise BSP of certain suspicious/illegal activity or incident of fraud (Php 20,000 and no threshold level if an insider crime) that could have a material impact to its safety, soundness and reputation so that appropriate supervisory attention may be given. Further S. 173 of the MORB requires banks to report on crimes/losses regarding incidents of banking fraud (e.g. incidents involving material loss, destruction or damage to the bank's property/facilities, other than arising from a crime, when the amount involved per incident is Php 100,000 or more).
EC4	If the supervisor becomes aware of any additional suspicious transactions, it informs the financial intelligence unit and, if applicable, other designated authority of such transactions. In addition, the supervisor, directly or indirectly, shares information related to suspected or actual criminal activities with relevant authorities.
Description and findings re EC4	The AMLC serves as the Philippine's central anti-money laundering/counter-terrorism financing authority and financial intelligence unit (FIU) and its dealings with the BSP are governed by the 2019 Memorandum of Understanding with the AMLC (MB Approved dated 7 March 2019). This MoU provides extensive guidelines on the sharing of information both from the AMLC to the BSP and vice versa (e.g. BSP provides copies of AML/CFT on-site examination reports for ARRS rated 1 and allows AMLC to utilize this information as part of its administrative proceedings whereas AMLC makes BSP aware of all legal proceedings pertaining to STRs/CTRs, etc.). BSP is prohibited from sharing CDD information held by banks (e.g. if other designated authorities required this information), due to the restrictions in the banking secrecy legislation. BSP may request the information by demonstrating probable cause and it cannot share this information without the consent of the MB.
EC5	The supervisor determines that banks establish CDD policies and processes that are well documented and communicated to all relevant staff. The supervisor also determines that such policies and processes are integrated into the bank's overall risk management and there are appropriate steps to identify, assess, monitor, manage and mitigate risks of money laundering and the financing of terrorism with respect to customers, countries and regions, as well as to products, services, transactions and delivery channels on an ongoing basis. The CDD management program, on a group-wide basis, has as its essential elements: (a) a customer acceptance policy that identifies business relationships that the bank will not accept based on identified risks; (b) a customer identification, verification and due diligence programme on an ongoing basis; this encompasses verification of beneficial ownership, understanding the purpose and nature of the business relationship, and risk-based reviews to ensure that records are updated and relevant; __________ [73/] Consistent with international standards, banks are to report suspicious activities involving cases of potential money laundering and the financing of terrorism to the relevant national centre, established either as an independent governmental authority or within an existing authority or authorities that serves as an FIU.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC5	(c) policies and processes to monitor and recognize unusual or potentially suspicious transactions; (d) enhanced due diligence on high-risk accounts (e.g. escalation to the bank's senior management level of decisions on entering into business relationships with these accounts or maintaining such relationships when an existing relationship becomes high-risk); (e) enhanced due diligence on politically exposed persons (including, among other things, escalation to the bank's senior management level of decisions on entering into business relationships with these persons); and (f) clear rules on what records must be kept on CDD and individual transactions and their retention period. Such records have at least a five-year retention period.
Description and findings re EC5	BSP's AML on-site examination framework assesses the strength of banks' CDD policies and processes, that such processes are integrated into a bank's overall risk management processes including the identification, assessment and reporting on AML/CFT related requirements (S. 921 of the MORB). Examiners assess banks' compliance with: (a) customer assessment policy that provides the type of business relationships that will not be accepted or prohibited, including prohibition on anonymous accounts, accounts under fictitious names, numbered checking accounts, etc. (b) CDD program which includes the verification of customer's and beneficial owner's identities based on official documents. Where the customer, or the owner of the controlling interest is a company listed in a stock exchange and subject to disclosure requirements (either by stock exchange rules or through law or enforceable means) or is a majority-owned subsidiary of such a company, the covered person/bank is not required to verify the identity of any shareholder or beneficial owner of such companies. The relevant identification data may be obtained from a public register, from the customer or from other reliable sources to ensure adequate transparency of beneficial ownership. (c) policies and processes are in place to monitor and recognize unusual or potentially suspicious transactions to include, on the basis of materiality and risk, ensuring that pertinent identification information and documents collected under the CDD process are kept up-to-date and relevant, by undertaking reviews of existing records, particularly for higher risk categories of customers. It was noted that the required timeframe for filing of STRs should be improved.[74/] (e) enhanced due diligence is effectively carried out for higher-risk accounts, including escalation to the bank's senior management level of decisions on entering into business relationships with these accounts or maintaining such relationships when an existing relationship becomes high-risk. ______________________ [74/] Recommendation 20.1 of the Asia/Pacific Group on Money Laundering's Mutual Evaluation of the Philippines (MER) 2019 noted that s. 9(c) of the AMLA allows STRs to the AMLC to be filled within five working days, which is not considered to have met the requirement for "prompt" reporting.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC5	(e) effective due diligence on politically exposed persons (PEPs) and immediate family members (including escalation to the Board) for both domestic and foreign PEPs to determine whether a customer or the beneficial owner is a PEP, obtain senior management approval before continuing with such a relationship or adopt measures to obtain source of wealth or funds information and to conduct enhanced ongoing monitoring of such relationships. (f) assess adequacy of banks' rules on what records must be kept on consumer identification and individual transactions, including the retention period (S. 924 of the MORB stipulates minimum 5 years retention) as well as a bank's ability to undertake the necessary adequate security measures to ensure the confidentiality of such information, including all information shared by the group-wide compliance function.
EC6	The supervisor determines that banks have in addition to normal due diligence, specific policies and processes regarding correspondent banking. Such policies and processes include: (a) gathering sufficient information about their respondent banks to understand fully the nature of their business and customer base, and how they are supervised; and (b) not establishing or continuing correspondent relationships with those that do not have adequate controls against criminal activities or that are not effectively supervised by the relevant authorities, or with those banks that are considered to be shell banks.
Description and findings re EC6	Rule 19 S. 3 of the 2018 AMLA-RIRR and S. 923 of the MORB as amended by Circular Nos. 706 and 950 requires covered persons to adopt policies and procedures to prevent correspondent banking activities from being utilized for money laundering activities and designate an officer responsible in ensuring compliance with these policies and procedures. As part of its AML on-site examination, BSP assesses whether banks/covered persons, in relation to correspondent banking, are required to: (a) gather sufficient information about the respondent institution to understand fully the nature of the respondent's business, and to determine from publicly available information the reputation of the institution and the quality of supervision, including whether it has been subject to a ML/TF investigation or regulatory action; assess the respondent institution's AML/CFT controls; obtain approval from senior management before establishing new correspondent relationships; and clearly understand the respective AML/CFT responsibilities of each institution. (b) S. 923 of the MORB (and Circular No 1022 which strengthened the provisions) provides the guidelines on fund/wire transfers. In view of the risk associated with dealing with fund/wire transfers, where a covered person may unknowingly transmit proceeds of unlawful activities or funds intended to finance terrorist activities, it should establish policies and procedures designed to prevent or discontinue it from being utilized for that purpose.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
EC7	The supervisor determines that banks have sufficient controls and systems to prevent, identify and report potential abuses of financial services, including money laundering and the financing of terrorism.
Description and findings re EC7	BSP's AML risk-based supervisory framework and on-site examination program assesses the adequacy of a bank's controls and systems to prevent, identify and report potential abuses of financial services, including ML and FT. AML examiners review banks' AML audit programs, compliance testing, ST reports, conduct random sampling of covered TRs, review newly opened accounts and bank/companywide closed banks as well as assess a bank's effectiveness of its methodology/controls over risk profiling, risk triggers/escalation process as well as assessing the strength of a bank's due diligence practices on existing clients (see EC 2 for more detailed information on BSP's AML on-site examination framework).
EC8	The supervisor has adequate powers to take action against a bank that does not comply with its obligations related to relevant laws and regulations regarding criminal activities.
Description and findings re EC8	S. 37 of the RA gives the BSP MB the authority to impose upon any bank or quasi-bank, their directors and/or officers, for any willful violation of BSP charter/by-laws, willful delay in the submission of reports or publications thereof as required by law, rules and regulations; any refusal to permit examination into the affairs of the institution; any willful making of a false or misleading statement to the Board or the appropriate supervising and examining department or its examiners; any willful failure or refusal to comply with, or violation of, any banking law or any order, instruction or regulation issued by the MB, or any order, instruction or ruling by the Governor; or any commission of irregularities, and/or conducting business in an unsafe or unsound manner as may be determined by the MB. BSP also has the authority to utilize a range of administrative sanctions and monetary penalties to be imposed on banks for non-compliance with AML/CFT requirements (S. 941 of the MORB and S. 4811Q of the MOR-NBFI). Further, BSP may utilize a range of enforcement actions can be imposed against Board members, senior management or line officers (written reprimand, restriction of certain licenses/products, suspension or removal from office and disqualifications from holding any position with a bank). In addition, the AMLC may also undertake enforcement and legal action to institute civil and criminal proceedings and other remedial proceedings through the Office of the Solicitor General (s. 7 of the AMLA). In cases of heighted supervisory concern (AML composite risk rating reflecting high risk) enforcement actions may be utilized include corrective action, sanction, and/or additional supervisory enforcement action (e.g. ranging from issuing a letter of commitment from a bank's Board to revocation of the BSP's issued license or registration) consistent with S. 002 of the MORB. Assessors note that at times the BSP has made use of these range of both administrative sanctions and enforcement actions (including issuing a monetary penalty) in the past where AML/CFT deficiencies have been noted at banks. Although BSP makes use of its enforcement tools (issuing directives, letters of commitment, etc.), it needs to ensure it is effectively utilizing its monetary penalty regime for AML/CFT non-compliance issues on a consistent basis.
EC9	The supervisor determines that banks have:

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)

EC9	(a) requirements for internal audit and/or external experts[75/] to independently evaluate the relevant risk management policies, processes and controls. The supervisor has access to their reports; (b) established policies and processes to designate compliance officers at the banks' management level, and appoint a relevant dedicated officer to whom potential abuses of the banks' financial services (including suspicious transactions) are reported; (c) adequate screening policies and processes to ensure high ethical and professional standards when hiring staff; or when entering into an agency or outsourcing relationship; and (d) ongoing training programs for their staff, including on CDD and methods to monitor and detect criminal and suspicious activities.
Description and findings re EC9	While conducting AML on-site examinations, BSP assesses banks compliance with (S. 911 of the MORB): (a) A bank's IA functions pertaining to ML/TF demonstrate that they have qualified personnel, conduct periodic and independent evaluation for CDD, CT and ST reporting, efficiency of the electronic AML/CFT transaction monitoring and reporting system and that results are reported to the Board and deficiencies tracked and dealt with by the compliance function. (b) Compliance function adequately conduct periodic testing, ensure infractions are reported, communicate broadly with staff on AML/CFT requirements. (c) adequate screening and recruitment processes that ensure qualified persons with no criminal records assume sensitive banking functions. (d) establishing effective and continuous training programs for staff, including CDD, CT and ST reporting and understanding of internal reporting processes.
EC10	The supervisor determines that banks have and follow clear policies and processes for staff to report any problems related to the abuse of the banks' financial services to either local management or the relevant dedicated officer or to both. The supervisor also determines that banks have and utilize adequate management information systems to provide the banks' Boards, management and the dedicated officers with timely and appropriate information on such activities.
Description and findings re EC10	S. 911 of the MORB, as amended by Circular Nos. 706 and 950 on the adoption of MTPP, requires covered persons to adopt a comprehensive and risk-based MTPP that includes, among others, a detailed procedures related suspicious transaction reporting including the adoption of a system, electronic or manual, of flagging, monitoring and reporting of transactions that qualify as suspicious transactions, regardless of amount or that will raise a "red flag" for purposes of conducting further verification or investigation, or transactions involving amounts below the threshold to facilitate the process of aggregating them for [75/] These could be external auditors or other qualified parties, commissioned with an appropriate mandate, and subject to appropriate confidentiality restrictions.

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)

Description and findings re EC10	purposes of future reporting of such transactions to the AMLC when their aggregated amounts breach the threshold. The ST reporting shall include a reporting chain under which an ST will be processed and the designation of a Board-level or approved committee who will ultimately decide whether or not the covered person should file a report to the AMLC. If the resources of the covered person do not permit the designation of a committee, it may designate the compliance officer to perform this function instead provided that the Board of directors is informed of his decision. S. 911 of the MORB, as amended by Circular Nos. 706 and 950 on monitoring and reporting tools, requires banks/covered persons to adopt an AML/CFT monitoring system that is appropriate for their risk-profile and business complexity. The system should be capable of generating timely, accurate and complete reports to lessen the likelihood of any reputational and compliance risks, and to regularly apprise the Board and senior management on AML/CFT compliance. S. 132 of the MORB provides that the audit committee shall establish and maintain mechanisms by which officers and staff shall, in confidence, raise concerns about possible improprieties or malpractices in matters of financial reporting, internal control, auditing or other issues to persons or entities that have the power to take corrective action. Circular No. 969 strengthened BSP's corporate governance requirements of banks' Boards to oversee the integrity, independence and effectiveness of a bank's policies and procedures for whistleblowing. It shall allow employees to communicate, with protection from reprisal, legitimate concerns about illegal, unethical or questionable practices directly to the Board or to any independent unit. Policies shall likewise be set on how such concerns shall be investigated and addressed, for example, by an internal control function, an objective external party, senior management and/or the Board itself. Officers and staff shall, in confidence, raise concerns about possible improprieties or malpractices in matters of financial reporting, internal control, auditing or other issues to persons or entities that have the power to take corrective action. It shall ensure that arrangements are in place for the independent investigation, appropriate follow-up action, and subsequent resolution of complaints. BSP's AML on-site examination framework assesses the adequacy of bank's policies and procedures pertaining to staff's ability to raise issues pertaining to the abuse of bank's financial services, the effectiveness of MIS systems for reporting, monitoring and dealing with issues raised. BSP's AML specialists join the on-site examination team for most large universal and commercial banks and foreign banks and overseas branches of universal banks. Most rural and cooperative banks, when examined, have an AML component to the on-site examination.
EC11	Laws provide that a member of a bank's staff who reports suspicious activity in good faith either internally or directly to the relevant authority cannot be held liable.
Description and findings re EC11	S. 922 of the MORB pertaining to the Exemption from Bank Secrecy Laws stipulates that when reporting covered or suspicious transactions to the AMLC, covered persons and their officers and employees shall not be deemed to have violated RA No. 1405, as amended, RA No. 6426, as amended, RA No. 8791 and other similar laws, but are prohibited from communicating, directly or indirectly, in any manner or by any means, to any person, the

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (continued)	
Description and findings re EC11	fact that a covered or suspicious transaction report was made, the contents thereof, or any other information in relation thereto. In case of violation thereof, the concerned officer and employee of the covered person shall be criminally liable in accordance with the provisions of the AMLA, as amended. S. 9 of the AMLA and S. 922 pertaining to Exemption from Bank Secrecy Laws regarding the Safe Harbor Provision stipulates that no administrative, criminal or civil proceedings, shall lie against any person for having made a CTR or an STR in the regular performance of his duties in good faith, whether or not such reporting results in any criminal prosecution under the AMLA, as amended, its RIRR or any other law.
EC12	The supervisor, directly or indirectly, cooperates with the relevant domestic and foreign financial sector supervisory authorities or shares with them information related to suspected or actual criminal activities where this information is for supervisory purposes.
Description and findings re EC12	As stated in EC11, there is an exemption from the bank secrecy laws pertaining to the reporting of suspicious transactions to the AMLC, however, the BSP is not permitted to share information pertaining to suspicious activities to other relevant domestic and foreign financial sector supervisory authorities for supervisory purposes unless authorized by the Monetary Board. The AMLC has the authority to receive and take action in respect of, any request from foreign states for assistance in their own anti-money laundering operations. The BSP can refer the case of a foreign counterpart to AMLC for investigation or bank inquiry. The results of AMLC’s investigation or bank inquiry may, then, be referred to the BSP for transmittal to the requesting foreign counterpart of the BSP based on the 2019 MoU with the AMLC (MB Approved dated 7 March 2019). This MoU provides extensive guidelines on the sharing of information both from the AMLC to the BSP and vice versa (e.g. BSP provides copies of AML/CFT on-site examination reports for ARRS rated 1 and allows AMLC to utilize this information as part of its administrative proceedings.
EC13	Unless done by another authority, the supervisor has in-house resources with specialist expertise for addressing criminal activities. In this case, the supervisor regularly provides information on risks of money laundering and the financing of terrorism to the banks.
Description and findings re EC13	The BSP has issued many regulations/Circulars and public advisories (Circular-Letters, Memorandum to banks, media releases, primers) to help prevent financial abuse and mitigate ML/TF risk, make banks and the public fully aware of those fraudulent schemes or illegal activities, and to provide guidance on the proper actions to be taken. BSP requires FIs to be vigilant in processing account openings and monitoring of transactions, and in complying with AML/CFT requirements and their reporting obligations for covered and suspicious transactions to the AMLC. In addition, the BSP required banks to take into account, as part of their own AML/CFT risk assessment processes, the results of the 2017 National Risk Assessment. S. 50 of the NCBA gives BSP the authority to conduct investigations into criminal activities.
Assessment of Principle 29	Largely Compliant

Table 2. Philippines: Supervisory Powers, Responsibilities and Functions (concluded)	
Comments Comments	The AML/ATF legislative framework as it pertains to banks covered in BSP's mandate appear to be effective. Further, BSP's AML risk assessment framework and on-site examination coverage of entities appear robust. The MoU between the AMLC and BSP, originally established in 2007 was updated in March 2019 and clearly outlines the coordination and collaboration between these two regulatory agencies as well as the robust sharing of necessary information between the two organizations. While the BSP makes use of its front-line supervisors to carry out AML on-site examinations for a) smaller financial institutions (526 thrift, rural and co-operatives), and b) non-banking entities such as money service businesses, credit granting businesses and payment system operators (1162 entities), the contingent of AML technical experts (51 experts (up from 34 one year ago) with a total of 79 approved positions) may need to be reassessed. Although BSP makes use of its enforcement tools (issuing directives, letters of commitment, etc.), it needs to ensure it is effectively utilizing its monetary penalty regime for AML/CFT non-compliance issues on a consistent basis. Recommendations: • Increase contingent of AML risk specialists to ensure the effectiveness of its AML/CFT supervision program; • Ensure consistent use of the monetary penalty regime when banks are found in non-compliance with AML and CFT requirements.

SUMMARY COMPLIANCE WITH THE BASEL CORE PRINCIPLES

Table 3. Philippines: Summary Compliance with the Basel Core Principles		
Core Principle	**Grade**	**Comments**
1. Responsibilities, objectives and powers	MNC	A significant weakness in the legislative and regulatory framework arises from the bank secrecy laws, which constrain the ability of the BSP to conduct effective ongoing supervision of banks. The laws state that all bank deposits with banking institutions in the Philippines are considered to be of an absolutely confidential nature and may not be examined, inquired or looked into by any person, including the BSP, except in defined circumstances. BSP should be granted unimpaired access to information on depositors and given the ability, without constraints, to employ and share depositor information for any prudential purpose (e.g., funding concentrations from related parties, intra-group dependencies, cash flow analysis, relationship to RPT and off-site AML data and analysis) in order to fulfill its supervisory mandate to address safety and soundness concerns. The BSP does not have the power to review and examine the parent or other affiliate companies of BSP supervised firms, although recently passed legislation provides it with authority to obtain data from such entities for 'statistical and policy development purposes in relation to the proper discharge of its functions and responsibilities. However, the BSP has not had cause to use this authority to date, and the stated scope of the new authority for 'statistical and policy development purposes' is limited. It does not provide the BSP with full powers to review the activities of parent companies and of companies affiliated with parent companies. Current legislation does not delineate clearly the respective responsibilities and objectives of the BSP, as primary supervisor of banks, and the PDIC, which also has supervisory and enforcement roles over banks in certain situations. The two authorities have signed a MOA which sets out their respective responsibilities and information sharing arrangements, but it is not a public document. The BSP and CDA do not have a formalized coordination and data-sharing agreement.

Core Principle	Grade	Comments
2. Independence, accountability, resourcing and legal protection for supervisors	LC	The BSP has full discretion to take any supervisory actions or decisions on banks and banking groups under its supervision and is adequately resourced to carry out those duties. Although there is no evidence of any past political interference in supervisory decisions taken by the MB, the operational independence of the BSP is compromised by the attendance of a member of the Cabinet on the MB.
3. Cooperation and collaboration	C	Existing regulations and practical arrangements between the BSP and domestic and foreign regulators provide an effective framework for cooperation and collaboration. The MOAs signed between the respective regulators adequately reflect the need to protect confidential information.
4. Permissible activities	C	BSP laws and regulations clearly establish the permissible activities of supervised banks, and naming conventions are controlled. Taking of deposits is restricted to identified BSP authorized institutions. A list of licensed banks is publicly available.
5. Licensing criteria	LC	BSP possesses adequate authority to set criteria and reject applications for banking licenses. The licensing process involves assessments of ownership structure and governance of the banking group. Prior consent of foreign authorities is obtained in order to license entry of a foreign banking organization. Licensing regulations and standards do not clearly identify grounds for revocation (especially when based upon false information), do not mandate a review of the suitability of ultimate beneficial owners, and apply standards that are not consistently employing standards related to ongoing supervision, especially governance, internal controls and risk management standards, ensuring such are 'in place' upon entry into the banking system. A system to ensure prompt monitoring of new entrants is lacking.
6. Transfer of significant ownership	MC	The recently enacted NCBA in S. 25-A could operate to restrict BSP's authority to pre-approve transfers of ownership to those transactions involving transfers of voting shares.

Core Principle	Grade	Comments
6. Transfer of significant ownership	MNC	The NCBA grant of BSP prior approval authority does not extend to ownership of significant controlling interests, held directly or indirectly. In addition, existing regulations lack clarity in the definition of 'control' or 'significant controlling interest,' do not set forth a definition of beneficial ownership and are tied to ownership or control of voting shares. And, BSP laws or regulations, or supervisory requirements, do not explicitly require notification to BSP of material negative information affecting suitability of parties that have direct or indirect controlling interests. Given the conglomerate ownership of multiple significant D-SIBs in the Philippines, where bank ownership chains cascade up through intermediate corporate structures to ultimate beneficial owners, the application of S. 25-A, the lack of regulatory clarity regarding the definition of 'control' or 'significant controlling interest' to include ultimate beneficial ownership, or indirect control of voting shares, could impair BSP's ability to review and approve transfers of significant controlling interests and assess suitability of ultimate beneficial owners.
7. Major acquisitions	C	BSP possesses adequate powers to approve or reject and impose prudential conditions upon acquisition or investments by a bank. BSP laws and regulations set forth clear expressions of permitted investments and thresholds, and establishes criteria for approvals, including investments by, or in, foreign operations. BSP reviews and assesses major acquisitions and applies reasonable prudential standards. It should be noted, however, that BSP does not possess the power to approve major acquisitions by a bank's parent or the parent's affiliate; and as a result, significant non-banking risks may be added to a conglomerate group without notice, review or approval of BSP.
8. Supervisory approach	LC	BSP maintains an effective system of banking supervision that is evolving to enhance current abilities to develop a more forward-looking and risk-based approach to oversight of banks, bank groups and systemically important firms. BSP reviews and assesses risks to the banking system as a whole and imports such analysis into its oversight of individual banks.

Core Principle	Grade	Comments
8. Supervisory approach	LC	At present, there is no resolvability assessment process in place, in conjunction with PDIC, with respect to BSP supervised firms, including its D-SIBs. BSP's framework for early intervention and its approach to assessing resolvability of firms and promptly resolving banks, especially D-SIBs, in an orderly fashion is not fully developed.
9. Supervisory techniques and tools	C	BSP employs an effective range of examination techniques and tools to support its supervisory processes and approach in relation to BSP regulated financial institutions. On-site and off-site monitoring has been integrated into supervisory departments assigned a range of financial institutions, and multiple bank-specific and macro-economic analyses are taken into consideration in scoping and conducting examinations. The integration of examination activities was implemented at the beginning of 2019, with advance preparatory steps being taken, and will take time to fully complete and assess performance under the new structure. Examinations incorporate a comprehensive review of financial statement and accounts, business model analysis and horizontal peer reviews, and incorporate stress testing results. Findings are communicated to the bank via the ROE in an adequate timely fashion, with clear directives setting forth supervisory expectations. Mandated corrective actions are monitored and followed in monthly and quarterly updates and reviewed in depth during on-site examinations. The scope and intensity of examinations reflect the size, complexity and risk profile of the bank, employing bank-level and banking system analysis, including peer reviews.
10. Supervisory reporting	C	BSP has an effective set of reporting requirements to view and analyze prudential reports on a solo and consolidated basis. BSP has adequate power to require and receives reports from supervised firms regarding financial condition, performance and risks. BSP regulations require banks to demonstrate effective governance and internal controls, including valuations, and has effectively review banks'

Core Principle	Grade	Comments
10. Supervisory reporting	C	governance and internal control processes, acting in relevant instances to challenge banks' valuation methodologies and assumptions. BSP has been inhibited from requiring submission of all relevant information from the wider banking group, given the restrictions on its supervisory remit. BSP has employed its available bank reporting requirements and information sources in order to gain a view regarding materiality of group activities in relation to the bank and banking group and it should continue to enhance its methodology and approaches to assessing risks posed by the wider group, including obtaining necessary information to support resolution planning and resolvability analysis.
11. Corrective and sanctioning powers of supervisors	LC	While BSP has an appropriate set of supervisory tools, including an ability to revoke the banking license, the timeframes within which the remediation of identified supervisory issues is concluded or resolved can be extensive. Banks placed into PCA can linger in such status for prolonged periods (years), during which time the banks can remain capital deficient. The PCA framework does not effectively operate to require firms to be placed into resolution at an early stage, and before equity has been exhausted. Escalation of PCA enforcement actions is not tied to stages of decline in regulatory capital levels, and resolution/receivership is not imposed even where bank owners have demonstrated an inability or unwillingness to recapitalize the firm unless grounds under Sec. 30 of the NCBA, as amended, exist.
11. Corrective and sanctioning powers of supervisors	LC	The PCA and BRes frameworks have resulted in unhealthy and poorly managed banks remaining licensed and active for prolonged periods. The ability to fully protect the bank from the actions of parent companies and affiliates is impaired because such entities fall outside of its regulatory perimeter, and direct action against non-regulated entities within the conglomerate group cannot be taken. The available information on conglomerate structure is only updated periodically, and there is no requirement that the bank or banking group provide a comprehensive and current view of the group-wide risk concentrations and inter-dependencies.

Core Principle	Grade	Comments
11. Corrective and sanctioning powers of supervisors	LC	In addition, BSP does not conduct a comprehensive resolvability assessment and resolution plans are not developed. These weaknesses result in BSP not possessing a comprehensive view of the protective actions that would be necessary or appropriate to 'ring-fence' the bank while ensuring that critical economic functions of systemic importance to the financial system are maintained. Adequate information on inter-connections and dependencies between the bank and the wider group entities is important to inform BSP decision-making regarding 'ring-fence' actions that may be practical and effective, avoid interruption to critical functions, and mitigate potential systemic impacts.
12. Consolidated supervision	LC	The BSP's supervisory regime adequately assesses the adequacy of a consolidated banking groups' capital and liquidity positions and ensures that RPTs are conducted on an arms-length basis. Concentration risk is not currently captured adequately because the single borrower limit is not applied at the consolidated group level, but proposed revisions to the LE framework will address this issue. The majority of BSP designated D-SIBs are incorporated within a conglomerate structure that includes non-regulated parent companies and affiliates engaged in non-banking activities, but the wider group of companies is not captured within BSP's regulatory perimeter.
12. Consolidated supervision	LC	All BSP regulated entities are included in consolidated banking groups, but not all financial institutions under the supervision of IC and the SEC are part of those consolidated banking groups. As noted in BCP1, the BSP does not have the power to review and examine the parent or other affiliate companies of BSP supervised firms.
13. Home-host relationships	C	The overseas activities of Philippine banks are not material to their overall operations, but the BSP has established MOAs and less formal information sharing arrangements with relevant host countries. As noted in BCP3, the MOA with BaFin should be reviewed as supervisory responsibility for the relevant bank has transferred to the SSM.
14. Corporate governance	C	BSP's Corporate Governance regulations and guidelines are comprehensive, with appropriate and clearly articulated requirements for Boards and senior management. BSP's on-site examination framework adequately reviews banks' compliance with BSP's regulations.

Core Principle	Grade	Comments
15. Risk management process 15. Risk management process	LC	Overall, BSP's regulatory framework on risk management governance appears to be adequate for the currently defined risk areas (credit, IRRB, market, operational, etc.). However, given the increasing trends among banks towards greater use of quantitative analysis and models in decision making processes, it is important that BSP finalize the draft exposures pertaining to model risk management. Further, the finalization of the draft exposures on reputational risk as well as updating the regulations to reflect the requirement to publicly disclose the dismissal or replacement of a bank's CEO, CRO, Chief Compliance Officer and Internal Audit Executives is also needed. BSP's current guidance used to assess bank's internal capital (ICAAP) needs to be updated to reflect current practices. In addition, recovery plans should be separated out of ICAAP and shared with PDIC as it would be beneficial to include the views of the resolution authority in the assessment of the robustness of the plans. In addition, although the FSCC has approved a Financial Crisis Management and Resolution Framework for the domestic regulatory agencies to work towards crisis operational preparedness in dealing with a material problem of a major bank, each agency is still working on developing and finalizing their individual crisis management plans. Assessors note that the agreed contingency arrangements amongst the regulatory agencies who sit on the FSCC are very preliminary in nature. Much more work is required to fully develop adequate contingency planning arrangements for the recovery and/failure of a systemic bank.
16. Capital adequacy	LC	An appropriate capital framework is in place for the major banks in the Philippine banking sector, with minimum capital ratios and a leverage ratio set at more conservative levels than applicable Basel standards. The capital framework for stand-alone rural, thrift and cooperative banks is in the process of being revised to align more closely with Basel III. The BSP does not directly vary individual banks' capital requirements to reflect their risk profile but has adjusted certain asset risk weights and has introduced a higher capital regime for D-SIBs.

Core Principle	Grade	Comments
17. Credit risk	LC	BSP's current regulations pertaining to banks' credit risk management policies and processes and its on-site supervision framework appear to be adequate, except for the lack of guidance in respect of the management/use of internal models to measure credit risk. Given the pace of growth in certain sectors of the banking industry, it will be essential for the BSP to establish a concentrated area of technical credit expertise to keep pace with the potential increase in banks' use of more complicated credit facilities as well as the utilization of more sophisticated credit models (see BCP 18 for more details). Thematic/horizontal credit reviews across the larger banks focusing on credit practices will be important as BSP moves to a more risk based supervisory approach.
18. Problem assets, provisions, and reserves	C	BSP's regulations pertaining to banks' policies and processes for the early identification and management of problem assets and the requirement to maintain adequate provisions and reserves are considered adequate. Assessors noted the strength of BSP's on-site supervision framework in the assessment of a bank's adequacy in the management of problem assets. The BSP should consider changing its loan provisioning guidance for less sophisticated banks pertaining to secured loans (e.g. reconsider the adequacy of loan loss provisioning based on type of collateral and determination of acceptable write-off periods). Further, BSP should ensure its guidance pertaining to BSP's expectations on banks' methodology/modelling of the impairment of expected credit losses is in line with proposed SEC guidance.
19. Concentration risk and large exposure limits	LC	BSP's on-site examination framework adequately assesses banks' adherence to the current large exposure (LE) framework. However, there are a number of weaknesses in the current LE framework. It does not capture the single borrower limit (SBL) on a consolidated basis; the definition of the capital base against which the SBL is calculated is not compliant with the applicable Basel standard; and clarification is required around the identification of economic interdependence to provide clearer guidance for aggregating exposures to a group of connected counterparties.

Core Principle	Grade	Comments
19. Concentration risk and large exposure limits	LC	These issues will be addressed when the proposals in the BSP's exposure draft amending the current LE framework have been implemented.
20. Transactions with related parties	C	BSP's definition of related parties is broader than the suggested Basel definition, therefore current regulations appear adequate. BSP's on-site examination team adequately challenges banks' policies/procedures for managing related party transactions. As BSP adopts a more risk-based approach to its on-site examination framework, BSP's off-site surveillance and assessment of banks' RPT data will be key.
21. Country and transfer risks	C	BSPs off-site surveillance of regulatory and supplementary data on banks' country exposures and its on-site examination framework is considered to be adequate. Assessors note that the BSP needs to finalize the draft Circular on Risk Management Guidelines on Investment Activities of banks to capture the investment side of country and transfer risks in the regulatory framework. In all other respects, the BSP's regulations and guidance on banks' country and transfer risk is considered to be acceptable.
22. Market risk	LC	The regulatory framework and supervisory practice are appropriate for the complexity of market risk being run by banks, and the BSP is adequately resourced in terms of both numbers and levels of expertise to supervise banks' market risk functions effectively. The framework ensures that banks have adequate market risk management processes that take into account their risk appetite and risk profile, but there is a lack of clarity in the framework over the allocation of assets between trading and banking books, which creates capital arbitrage opportunities for banks. Proposals to update the BSP market risk framework, when implemented, will address this ambiguity and, more generally, will clarify the governance and capital treatment of market risk.
23. Interest rate risk in the banking book	LC	The legal and supervisory framework for ensuring banks have adequate systems that identify, measure, evaluate, monitor, report and control IRRBB is appropriate for the complexity of the risk being run by such banks. The framework does not,

Core Principle	Grade	Comments
23. Interest rate risk in the banking book	LC	however, set IRR stress test requirements for smaller banks. A revised set of IRRBB guidelines has been exposed to industry for comment which, when implemented, will introduce further enhancements to banks' stress testing exercises and, more generally, align the BSP framework with the applicable Basel standard.
24. Liquidity risk	LC	An appropriate regulatory framework is in place to ensure minimum requirements for liquidity and funding for universal and commercial banks, but the cashflow mismatch monitoring tools for the LCR should be reviewed and aligned more closely with applicable Basel standards. The BSP has issued guidelines on a monitoring regime for intraday liquidity but has yet to introduce a reporting regime for intraday liquidity. The BSP does not set individual liquidity and funding requirements for its banks above the statutory minimum that reflect the liquidity and funding profiles of those banks. The liquidity regime for smaller banks is generally appropriate for such institutions.
25. Operational risk	C	BSP's regulatory requirements pertaining to banks' operational risk management framework appear to be adequate. Assessors noted BSP's plans to augment IT technical expertise relating to developments in financial technology and cyber related risk.
26. Internal control and audit	C	BSP's regulatory framework and annual on-site examination processes provide supervisors with an adequate view of the effectiveness of a bank's internal control frameworks and IA function. BSP has updated its requirements pertaining to a bank's compliance function and updated its supervisory assessment approach to address prior BCP assessment findings.
27. Financial reporting and external audit	LC	Banks' financial reporting requirements are in accordance with international standards. The BSP does not engage with external auditors on a regular basis as part of the routine supervisory process. Although external auditors have access to the BSP's Reports of Examination, there are constraints imposed on supervisors sharing information on a bank with external auditors as part of an ongoing dialogue. A review into establishing more effective working arrangements with external auditors on the sharing of information has been initiated by the MB.

Core Principle	Grade	Comments
28. Disclosure and transparency	LC	The BSP prescribes detailed public disclosure requirements for banks on both a consolidated and solo basis and verifies that these requirements are met. The disclosure regime is not as comprehensive as the current BCBS Pillar 3 framework in terms of the scope and detail of coverage required across a number of risk elements (e.g. for LCR, NSFR, leverage, market risk, IRRBB and remuneration). The BSP is, however, revising its disclosure regime to align the requirements with the applicable BCBS standard.
29. Abuse of financial services	LC	The AML/ATF legislative framework as it pertains to the banks covered in BSP's mandate generally appear to be effective. Further, BSP's AML risk assessment framework and on-site examination coverage of entities appear robust. Further, the MoU between the AMLC and BSP, originally established in 2007 was updated in March 2019, clearly outlines the coordination and collaboration between these two regulatory agencies as well as the robust sharing of necessary information between the two organizations. While the BSP makes use of its front-line supervisors to carry out AML on-site examinations for a) smaller financial institutions (526 thrift, rural and cooperative banks), and b) non-banking entities such as money service businesses, credit granting businesses and payment system operators (1162 entities), the contingent of AML technical experts (51 experts (up from 34 one year ago) with a total of 79 approved positions) may need to be reassessed. Although BSP makes use of its enforcement tools (issuing directives, letters of commitment, etc.), it needs to ensure it is effectively utilizing its monetary penalty regime for AML/CFT non-compliance issues on a consistent basis.

RECOMMENDED ACTIONS AND AUTHORITIES' COMMENTS

A. Recommended Actions

Table 4. Philippines: Recommended Actions to Improve Compliance with the Basel Core Principles and the Effectiveness of Regulatory and Supervisory Frameworks

Reference Principle	Recommended Action
Principle (1)	• Amend the bank secrecy laws to grant BSP full access to banks' deposit and other data; • Provide BSP with the legal authority to review the activities of a bank's parent companies and of companies affiliated with parent companies' activities to determine their impact on the safety and soundness of the bank and the banking group; • Make the MOA between the BSP and PDIC public to provide greater transparency around the responsibilities of the two authorities; • Establish a bilateral agreement between the BSP and CDA to formalize co-ordination and data-sharing arrangements between the two authorities.
Principle (2)	• Amend the Charter of the BSP to revisit the position of the Cabinet Member as a voting member of the MB; • Amend the NCBA to require public disclosure of the reason(s) for dismissal of the Head of the MB.
Principle (3)	• Negotiate a MOA with the SSM to replace the existing MOA with BaFin; • Negotiate a formal MOA between the BSP and CDA; • Establish formal college of supervisor arrangements for sharing information between domestic supervisory bodies.[1/]
Principle (5)	• Clarify in regulations or supervisory guidance the grounds supporting revocation (beyond the grounds supporting appointment of PDIC as receiver), including the ability to revoke when applications are determined to be submitted based upon false information. • Amend licensing criteria to ensure a review of the suitability of ultimate beneficial owners, where applicable, and specify that there must be a demonstration of financial strength of incorporators or subscribers adequate to provide additional financial support beyond the initial subscription level. [1/] See footnote 19.

Reference Principle	Recommended Action
Principle (5)	• Amend licensing criteria to set objective criteria for licensing of new banks, foreign banks, and to grant licenses for additional authorities to apply standards consistent with ongoing supervision equally across applicants, including, importantly, ensuring that applicants have adequate governance, internal controls and risk management systems 'in place' upon commencing operations. • Clarify licensing guidelines or procedures to mandate more frequent review of newly licensed banks upon entry into the banking system. • Ensure that ongoing supervision incorporates a review of relevant banks' compliance with applicable local tax, licensing or other supervisory requirements. • Continue close coordination with local government units to coordinate regarding licensing and permitting processes.
Principle (6)	• Review and amend the legal and regulatory framework related to transfer of significant controlling interests to include the definition of ultimate beneficial owner or direct and indirect significant controlling interest; • Ensure BSP has the power to review, reject and impose prudential conditions upon the transfer of controlling interest or significant ownership, including beneficial ownership, of a bank held indirectly; • Ensure BSP has the power to review and enforce the suitability of beneficial owners and obtain timely information regarding material changes to their suitability.
Principle (8)	• Develop and implement, in conjunction with PDIC, policies and standards to assess resolvability of firms and promptly resolving banks, especially D-SIBs, in an orderly fashion. • Develop and implement policies and standards requiring regulated financial institutions to support a resolvability assessment, which would include consideration of inter-connectedness, structure and operations within the wider group and adopt measures to address impediments to resolvability.
Principle (11)	• Continue ongoing revisions to the PCA framework and implement policies and procedures that will operate to ensure that firms placed into PCA status are addressed in a timely fashion and place firms into resolution in a prompt and timely fashion. • Continue to work with PDIC to establish effective coordination mechanisms to ensure that, where appropriate grounds exist, firms are placed into resolution in a prompt and timely fashion. • Conclude efforts to develop and implement policies and standards regarding the supervisory approach to ring-fence the bank from the actions of parent companies, subsidiaries, and other related

Reference Principle	Recommended Action
Principle (11)	companies in matters that could impair the safety and soundness of the bank.
Principle (12)	• Bring financial institutions in conglomerate structures which are outside the BSP consolidated banking group and which are regulated by other domestic regulators into the consolidated banking group to enable the BSP to capture the risks they pose to the banking group. • Require BSP regulated banks within conglomerate structures to specifically identify all risks arising from companies within their wider group structure in their ICAAP and describe fully the internal controls for reporting and managing such risks.
Principle (15)	• Finalize draft exposures on model risk management, reputational and public disclosure of dismissal of CRO, CO and IA executives. • Develop and operationalize BSP's crisis preparedness involving a systemic financial institution, including working with other regulatory agencies within the FSCC (e.g. sharing D-SIB recovery plans with the PDIC) in order to strengthen and formalize needed contingency arrangements pertaining to the recovery or resolution of a major bank failure. • Update guidance on ICAAP to reflect current practices.
Principle (16)	• Set individual capital ratios for banks based on their risk profile as part of the SRP process. • Introduce a simplified ICAAP for the rural, thrift and cooperative banks.
Principle (17)	• Develop guidance on the management/use of internal models to measure credit risk. • Establish a concentrated area of credit expertise. • Conduct thematic/horizontal credit reviews across larger FIs focusing on bank's credit risk management practices.
Principle (18)	• Change loan loss provisioning guidance for less sophisticated banks pertaining to secured loans (collateral valuation, maximum write-off periods) • Align BSP's expectations on banks' methodology/modelling of the impairment of expected credit losses with the SEC proposed guidance.
Principle (19)	• Update regulations governing large exposures to ensure limits are calculated both on a solo and consolidated basis.
Principle (21)	• Finalize the draft Circular on Risk Management Guidelines on Investment Activities of banks to capture the investment side of the country and transfer risks in the regulatory framework.[2/]

Reference Principle	Recommended Action
Principle (22)	• Implement the proposals on a revised market risk framework and on risk management guidelines on investment activities.[3/]
Principle (23)	• Implement the proposals on a revised set of IRRBB guidelines.[4/]
Principle (24)	• Review the monitoring tools for the LCR to align them more closely with applicable Basel standards, including introduction of a more granular cashflow mismatch report. • Introduce an ILAAP framework to enable the BSP to set individual liquidity and funding requirements for banks above the statutory minimum to reflect the particular liquidity and funding profiles of those banks. • Implement an intraday liquidity reporting regime.[5/]
Principle (27)	• Remove any constraints on information sharing between BSP supervisors and external auditors • Introduce routine meetings between BSP supervisors and external auditors as part of the supervisory process.
Principle (28)	• Issue proposals on a revised Pillar 3 framework.
Principle (29)	• Increase contingent of AML risk specialists to ensure the effectiveness of its AML/CFT supervision program. • Ensure consistent use of the monetary penalty regime when banks are found in non-compliance with AML and CFT requirements.

[2]/ See footnote 2.

[3/] See footnote 2.

[4/] See footnote 2.

[5/] See footnote 2.

B. Authorities' Response to the Assessment

56. The Bangko Sentral ng Pilipinas (BSP) would like to thank the joint IMF and World Bank BCP assessment mission team for conducting a comprehensive assessment of the BSP's compliance with the Basel Core Principles (BCP) for Effective Banking Supervision. The BSP recognizes the importance of this mission as it allows the organization to benchmark the reforms it has instituted with globally recognized standards. This exercise likewise provided a valuable opportunity to the BSP supervision team to learn from the exchange of insights and views with the members of the mission team and benefit from experts' views on how to further strengthen the BSP's supervision tools and practices.

57. Since the 2009 FSAP mission, significant developments in the legal and regulatory frameworks were put in place that enabled the BSP to effectively supervise banks contributing to the sustained resilience of the Philippine financial system. These include the passage of critical laws such as the amendments to the BSP Charter, and implementation of a critical regulatory reform agenda that covers the adoption of the Basel III framework and internationally recognized standards and best practices on corporate governance and risk management system, among others. The reform agenda is complemented by an institutionalized capacity building program for supervisors, and strong stakeholder collaboration.

58. The BSP appreciates the recognition and positive assessment of the BCP assessment mission team on the initiatives implemented over the years. The BSP also welcomes the recommendations of the mission team as these are valuable inputs in crafting the strategy roadmap for the financial sector.

59. In particular, the BSP echoes the views of the mission team on the importance of lifting the bank deposit secrecy laws. The amendment of the bank deposit secrecy laws will enable the BSP and other financial sector regulators to fully and effectively discharge their supervisory mandates to promote the safety and soundness of the financial sector and protect the depositing public. The BSP also recognizes that allowing financial sector regulators unrestricted access to bank records, including depositor information, should be subject to strong professional confidentiality arrangements.

60. The BSP would like to reiterate its views in the following areas to provide some context and highlight the practices and circumstances that should be considered in the assessment:

- **The independence of the BSP is not compromised even with the appointment of a cabinet member in the Monetary Board.** It should be noted that the cabinet member represents only one (1) vote while a majority vote of the seven-man team is needed in order to approve a resolution. We would also like to stress that the membership of the Finance Secretary in the Monetary Board enhances coordination with the National Government, particularly on matters relating to financial stability.

The BSP has displayed operational independence since its establishment in July 1993. There has been no case nor instance when the seat of the cabinet member was used to influence the decisions of the Monetary Board. Moreover, majority of the members of the Monetary Board are from the private sector.

- **The recent amendments to the New Central Bank Act (NCBA) provide the BSP with the power to disapprove the transfer of shares to parties who are not fit and proper to hold or own shares of stock of banks.** Although existing regulations do not explicitly include the language 'ultimate beneficial ownership' in the definition of 'control' or 'significant controlling interest', the BSP does not consider this as a constraint in assessing the fitness and propriety of the ultimate beneficial owners. The BSP has rejected applications for transfer of shares of stock of banks to parties who are not considered as fit and proper to hold said shares.

- **On the chartering of domestic and foreign bank applicants, the BSP applies common criteria which focus mainly on the suitability/fitness of shareholders and management, and financial strength of the applicants.** Aside from this, foreign banks are expected to comply with additional selection criteria as provided in the law which fully liberalized the entry of foreign banks in the Philippines. The suitability of bank owners is passed upon by the BSP not only at the initial stage of the chartering process but also during the corporate life of a bank. The determination of financial strength of shareholders is not limited to the evaluation of their capacity to pay the subscribed shares of stock. It extends to the assessment of their capability to infuse additional capital should the need arise in the future.

- **The BSP consistently endeavors to implement timely and effective remediation of significant supervisory issues.** It should be noted that the BSP issues directives even before the finalization of the Report of Examination (ROE), particularly if such involve the issuance of restrictions or cease and desist orders on unsafe and unsound practices, or capital call for banks with deficient capital, among others. Moreover, banks are already expected to address key issues upon the close of the on-site examination. Nonetheless, the BSP remains committed to continue improving the effectiveness of its processes and resolution timelines particularly for banks under the prompt corrective action (PCA) and banks for resolution (BRes) frameworks.

- **The BSP adheres to the principles of proportionality by issuing simplified guidelines without compromising regulatory objectives of safeguarding the safety and soundness of the banking system.** The submission of Internal Capital Adequacy Assessment Process (ICAAP) document is not imposed on thrift, rural and cooperative banks due to their simple operations and risk profiles. But said banks are required to conduct capital planning exercise and this is being validated during onsite examination.

- **The BSP has embarked on a four-phase program to further strengthen the liquidity position of the banking system. This includes the enhancement of foundational liquidity risk management guidelines, adoption of the Liquidity Coverage Ratio (LCR) and Net**

Stable Funding Ratio (NSFR) frameworks and issuance of Intraday Liquidity Reporting guidelines. While the BSP does not require banks to develop an Internal Liquidity Adequacy Assessment Process (ILAAP), the existing liquidity risk management framework already requires bank to adopt appropriate risk measurement and internal risk limits covering all significant sources of liquidity risk. Banks' compliance with these requirements are assessed during regular examination. Nonetheless, the BSP will await further guidance from the Basel Committee on Banking Supervision (BCBS) on ILAAP to ensure consistency of domestic regulations with international standards.

61. Finally, the BSP will continue to pursue proportionate and responsive regulatory reforms considering the developments and challenges in the business environment.