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GUIDELINES ON THE ADOPTION OF THE PHILIPPINE FINANCIAL REPORTING STANDARD (PFRS) 9 - FINANCIAL INSTRUMENTS

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The Monetary Board in its Resolution No. 1226 dated 26 July 2018, approved the following guidelines governing the adoption of PFRS 9 - Financial Instruments.

Section 1. Subsection X191.3 of the Manual of Regulations for Banks (MORB), Subsection 4191Q.3 and Section 4161N of the Manual of Regulations for Non- Bank Financial Institutions (MORNBFI) are hereby amended to read as follows:

"Subsection X191.3/4191Q.3/Section 4161N Philipin Financial Reporting Standards (PFRS).

Statement of Policy. It is the thrust of the Bangko Sentral to align its financial reporting requirements with standards and practices that are widely accepted internationally to promote fairness, transparency, and accountability in the financial industry. In this light, the Bangko Sentral is issuing guidelines governing the adoption of the PFRS, aimed at ensuring consistency of application and comparability of financial reports across the industry.

a. *Adoption of PFRS.* BSP Supervised Financial Institutions (BSFIs) shall adopt PFRS in recording transactions and in the preparation of financial statements and reports to the Bangko Sentral. However, in cases where there are differences between Bangko Sentral regulations and PFRS as when more than one (1) option are allowed or certain maximum or minimum limits are prescribed by PFRS, the option or limit prescribed by the Bangko Sentral shall be adopted by BSFIs. These include the accounting treatment of "Government Grants".

Government grants extended in the form of loans bearing nil or below-market rate of interest shall be measured upon initial recognition at its fair value (i.e. the present value of the future cash flows of the financial instrument discounted using the market interest rate). The difference between the fair value and the net proceeds of the loan shall be recorded under "Unearned Income-Others", and shall be recognized as income on a systematic basis over the period of the loan necessary to match with the related cost for which the grants are intended to compensate.

b. Preparation of prudential reports. For prudential reporting, BSFIs shall adopt in all respect the PFRS except in the following cases:

(1) In preparing consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated with the financial statements of the parent bank on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Investments in financial/non-financial allied/non-allied associates and joint ventures shall be accounted for using the equity method in accordance with the provisions of Philippine Accounting Standards (PAS) 28 "Investments in Associates and Joint Ventures".

In preparing solo/separate financial statements, investments in financial/non-financial allied/non-allied subsidiaries/associates, including insurance subsidiaries/associates, shall be accounted for using the equity method as described in PAS 28.

The rules on the preparation of solo financial statements as provided in Appendix 77 shall apply to banks.

(2) BSFIs shall recognize adequate and timely allowance for credit losses at all times. In this respect, BSFIs shall adopt the principles provided under the Enhanced Standards on Credit Risk Management under Section X178/4178Q/4197N as well as the provisions of Appendix 97/Q-56/N-16 of the MORB/MORNBFIs in measuring credit losses.

c. *Preparation of Audited Financial Statements (AFS)*. AFS shall in all respect be PFRS compliant and shall be submitted to the Bangko Sentral in accordance with the provisions of Subsection X190.1/4190Q/4172N of the MORB/MORNBFIs.

BSFIs shall submit to the Bangko Sentral adjusting entries reconciling the balances in the financial statements for prudential reporting with those in the AFS.

d. *Guidelines on the adoption of PFRS 9 Financial Instruments*. BSFIs shall adopt, as part of the PFRS framework, PFRS 9: Financial Instruments upon its mandatory effectivity date of 01 January 2018.

For this purpose, BSFIs shall be governed by the following:

(1) Consistent with the duties and responsibilities of the board of directors provided under Subsection X143.1/4143Q.1 of the MORB/MORNBFIs, the board of directors or any equivalent governing body in the case of branches of foreign banks, shall ensure that the BSFI appropriately and consistently adopts PFRS 9 as part of its reporting governance process. In this respect, the board shall assess the impact of PFRS 9 on business strategies and risk

management systems and ensure availability of sufficient resources, including capacity building initiatives, in adopting the standard.

The board shall approve policies and guidelines relative to the adoption of PFRS 9, which shall cover responsibilities of the different units in the BSFI (e.g., Treasury, Risk Management, Financial Controllership) as well as the extent of participation or involvement of third parties in the adoption process. The board shall likewise ensure that adequate control measures are in place to ensure the integrity of reports.

(2) Management shall implement the policies set by the board related to the adoption of PFRS 9 and ensure that sound professional judgment is exercised in implementing the provisions of the standard. Management shall provide feedback to the board on the effectiveness of implementation of PFRS 9.

(3) BSFIs shall be guided by the provisions of Appendix 33/Appendix Q-20 on "Guidelines on the Adoption of Philippine Financial Reporting Standards 9 (PFRS 9) - Classification and Measurement" and Appendix 97/Appendix Q-56/Appendix N-16 on "Impairment" in implementing the provisions of PFRS 9.

e. Enforcement Actions. Consistent with Sec. X009/4009Q/4182N.6 of the MORB/MORNBF, the Bangko Sentral reserves the right to deploy its range of supervisory tools and enforcement actions to promote adherence with the requirements set out in this Subsection and bring about timely corrective actions to ensure appropriate and consistent adoption of PFRS. In this respect, the Bangko Sentral may issue directives or impose sanctions on the BSFI and/or its directors, officers and/or employees concerned for noted supervisory issues on the adoption of PFRS 9.

Prudential reports affected by non-adherence to the provisions of this Subsection shall be subject to penalties/sanctions provided under Subsection X184.3 / 4192Q.2 / 4162N.3 of the MORB/MORNBF.

f. Transitory Provisions. BSFIs shall observe the following transition rules:

(1) BSFIs shall apply PFRS 9, retrospectively, in accordance with the transition requirements and guidance provided under PFRS 9 and PAS 8 "Changes in Accounting Policies, Changes in Accounting Estimates and Errors". BSFIs shall be guided by the provisions of PAS 8 if the retrospective application is impracticable.

(2) A BSFI that applied the earlier versions of PFRS 9 (2009), PFRS 9 (2010) or PFRS 9 (2013) shall be allowed to reclassify its financial assets provided that the reclassification requirements under the standard are met.