BSP Imposes Specific Ceilings on Bank Lending to its Subsidiaries and Affiliates

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The Monetary Board (MB) approved on 11 January 2007 specific ceilings on a bank's/quasi-bank's lending to its subsidiaries and affiliates. Under the revised rules, loans, other credit accommodations and guarantees granted to each subsidiary or affiliate shall be limited to 10 percent of the net worth of the lending bank/quasi-bank, with a sub-limit of 5 percent of net worth if unsecured. Moreover, there will be a 20 percent of net worth aggregate limit on total loans, other credit accommodations and guarantees that may be granted to all subsidiaries and affiliates of the lending bank/quasi-bank. Furthermore, all unsecured loans, other credit accommodations and guarantees to subsidiaries and affiliates of banks/quasi-banks shall continue to be fully deducted from the capital accounts for purposes of calculating both the capital adequacy ratio (CAR) and net worth of bank/quasi-bank concerned for regulatory purposes.

In making the changes, the Monetary Board affirmed the basic principle that dealings of banks/quasi-banks with their subsidiaries and affiliates should be strictly limited and, when undertaken, these should be conducted in the regular course of business and upon terms not less favorable to the bank than those offered to others. Nonetheless, the Monetary Board recognized that it could be counter-productive to totally prohibit such lendings particularly since the country's capital market has yet to gain sufficient depth to adequately support corporate finance. The Monetary Board noted that other countries, e.g., the United States, Singapore, Hong Kong and Thailand, have similar regulations limiting banks' exposures to their subsidiaries and affiliates.

The initial effort to strengthen DOSRI regulations occurred in 15 March 2004 through the issuance of BSP Circular No. 423 as part of broad initiative to enhance corporate governance in banks which, for the first time, included in the definition of "related interest" the subsidiaries and affiliates of banks. However, this approach created complications in the implementation and was deemed vulnerable to legal challenge. For simplicity and clarity, the Monetary Board, therefore, decided to come out and directly specify ceilings on bank credit accommodations to their subsidiaries and affiliates while maintaining the general DOSRI limit rule.

The revised rules take effect on 10 April 2007 upon the expiration of the transition period provided for under BSP Circular No. 532.