

PROMPT CORRECTIVE ACTION FRAMEWORK

[Appendix to Section 003]

In carrying out its primary objective of maintaining price stability conducive to a balanced and sustainable growth of the economy¹, the Bangko Sentral must necessarily maintain stability of the financial system through preservation of confidence therein. While preservation of confidence in the financial system may call for closure of mismanaged banks and/or financial entities under its jurisdiction, such closure is not the only option available to the Bangko Sentral. When a bank's closure, for instance, is adjudged by the Monetary Board to have adverse systemic consequences, the State may act in accordance with law to avert potential financial system instability or economic disruption.²

It is recognized that the closure of a bank or its intervention can be a costly and painful exercise. For this reason, the Bangko Sentral, as supervisor, can enforce PCA³ as soon as a bank's condition indicates higher-than normal risk of failure.

PCA essentially involves the Bangko Sentral directing the board of directors of a bank, prior to an open outbreak of crisis, to institute strong measures to restore the entity to normal operating condition within a reasonable period, ideally within one (1) year. These measures may include any or all of the following components:

- (1) Implementation of a capital restoration plan;
- (2) Implementation of a business improvement plan; and
- (3) Implementation of corporate governance reforms.

Capital restoration plan - this component contains the schedule for building up a bank's capital base (primarily through an increase in Tier 1 capital) to a level commensurate to the underlying risk exposure and in full compliance with minimum capital adequacy requirement. In conjunction with this plan, the Bangko Sentral may also require any one (1), or a combination of the following:

1. Limit or curtail dividend payments to common stockholders;
2. Limit or curtail dividend payments to preferred stockholders; and
3. Limit or curtail fees and/or other payments to related parties.

Business improvement plan - this component contains the set of actions to be taken immediately to bring about an improvement in the entity's operating condition, including but not limited to any one (1), or a combination of the following:

1. Reduce risk exposures to manageable levels;
2. Strengthen risk management;

3. Curtail or limit the bank's scope of operations including those of its subsidiaries or affiliates where it exercises control;
4. Change or replace management officials;
5. Reduce expenses; and
6. Other measures to improve the quality of earnings.

Corporate governance reforms – this component contains the actions to be immediately taken to improve the composition and/or independence of the board of directors and to enhance the quality of its oversight over the management and operation of the entity. This also includes measures to minimize potential shareholder conflicts of interest detrimental to its creditors, particularly, depositors in a bank. This likewise lays down measures to provide an acceptable level of financial transparency to all stakeholders. Such actions could include, but are not limited to, any one (1), or a combination of the following:

1. A change in the composition of the board of directors or any of the mandatory committees (under the MORB);
2. An enhancement to the frequency and/or depth of reporting to the board of directors;
3. A reduction in exposures to and/or a termination or reduction of business relationships with affiliates that pose excessive risk or are inherently disadvantageous to the supervised financial institution; and
4. A change of external auditor.

A bank may be subject to PCA whenever any or all of the following conditions obtain:

- (1) When either of the Total Risk-Based Ratio⁴, Tier 1 Risk-Based Ratio, or Leverage Ratio⁵ falls below ten percent (10%), six percent (6%) and five percent (5%), 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 Sec. 121;
- (2) The 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 Monetary Board. Such concerns could include, but are not limited, to any one (1) or a combination of the following:
 - a. Finding of unsafe and unsound activities that could adversely affect the interest of depositors and/or creditors;
 - b. A finding of repeat violations of law or the continuing failure to comply with Monetary Board

- Directives; and
- c. Significant reporting errors that materially misrepresent the bank's financial condition.

The initiation of PCA shall be recommended by the Deputy Governor, SES to the Monetary Board for approval. Any initiation of PCA shall be reported to the PDIC for notation. Upon PCA initiation, the Bangko Sentral shall require the bank to enter into a MOU committing to the PCA plan. The MOU shall be subject to approval by the Deputy Governor, SES and confirmation by the Monetary Board.

In order to monitor compliance with the PCA, quarterly progress reports shall be made. The Bangko Sentral reserves the right to conduct periodic on-site visits outside of regular examination to validate compliance with the PCA plan.

Subject to Monetary Board approval, 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 of directors 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 Bangko Sentral credit facilities; and
- (5) restriction on declaration of dividends.

On the other hand, if the bank subject to PCA promptly implements a PCA plan and substantially complies with its conditions, it may continue to have access to Bangko Sentral credit facilities notwithstanding non-compliance with standard conditions of access to such facilities. The Deputy Governor, SES shall recommend such exemption to the Monetary Board for approval.

In cases where a bank's problems are deemed to be exceptionally serious from the outset, or when a bank is unwilling to submit to the PCA or unable to substantially comply with an agreed PCA plan, the Deputy Governor, SES may immediately recommend to the Monetary Board more drastic actions as prescribed under Section 29 (conservatorship) and Section 30 (receivership) of R.A. No. 7653.

Subject to Monetary Board approval, the PCA status of a bank may be lifted: Provided, That the bank fully complies with the terms and conditions of its MOU and: Provided, further, That the Deputy Governor, SES has determined that the financial and operating condition of the bank no longer presents a risk to itself or the financial system. Such improved assessment shall be immediately reported to the PDIC.

Footnotes

1. Section 3 of Republic Act No. 7653
2. Section 17 and 18 of Republic Act No. 3591, as amended
3. Section 4.6 of Republic Act No. 8791
4. Otherwise known as Capital Adequacy Ratio ("CAR")
5. Total Capital /Total Assets