



BANGKO SENTRAL NG PILIPINAS

OFFICE OF THE GOVERNOR

CIRCULAR NO. 1085

Series of 2020

Subject : Sustainable Finance Framework

The Monetary Board, in its Resolution No. 415 dated 19 March 2020, approved the sustainable finance policy framework that sets out the expectations of the Bangko Sentral on the integration of sustainability principles, including those covering environmental and social (E&S) risk areas, in the corporate governance and risk management frameworks as well as in the strategic objectives and operations of banks.

Section 1. Section 153 of the Manual of Regulations for Banks (MORB) on Sustainable Finance Framework is hereby added to read, as follows:

Section 153 SUSTAINABLE FINANCE FRAMEWORK

Policy Statement. The Bangko Sentral is cognizant that climate change and other environmental and social risks could pose financial stability concerns considering their significant and protracted implications on the bank's operations and financial interest. In particular, physical and transition risks arising from climate change could result in significant societal, economic and financial risks affecting the banks and their stakeholders. The Bangko Sentral likewise recognizes the critical role of the financial industry in pursuing sustainable and resilient growth by enabling environmentally and socially responsible business decisions consistent with the aspirations set out for the Filipinos under the Philippine Development Plan.

Towards this end, the Bangko Sentral expects banks to embed sustainability principles, including those covering environmental and social risk areas, in their corporate governance framework, risk management systems, and strategic objectives consistent with their size, risk profile and complexity of operations.

Scope of Application. This Framework shall apply to all banks. Branches of foreign banks may adopt the relevant policies and strategies of their Head Office that are consistent with applicable provisions in this Section.

Definition of Terms. For purposes of this Framework, the following definitions shall apply:

- a. **Sustainable Finance.** This refers to any form of financial product or service which integrates environmental, social and governance criteria into business decisions that supports economic growth and provides lasting benefit for both clients and society while reducing pressures on the environment.

This also covers green finance which is designed to facilitate the flow of funds towards green economic activities and climate change mitigation and adaptation projects.

- b. ***Environmental and Social (E&S) Risk.*** This refers to potential financial, legal, and/or reputational negative effect of environmental and social issues on the bank. E&S issues include environmental pollution, climate risk (both physical and transition risks), hazards to human health, safety and security, and threats to community, biodiversity and cultural heritage, among others.
- c. ***Physical Risk.*** This refers to the potential loss or damage to tangible assets arising from climate change and/or other weather-related conditions such as floods, typhoons, droughts, earthquakes, extreme weather variability and rising sea levels.
- d. ***Transition Risk.*** This refers to the potential economic adjustment cost resulting from policy, legal, technology and market changes to meet climate change mitigation and adaptation requirements.
- e. ***Environmental and Social Risk Management System (ESRMS).*** This refers to policies, procedures and tools to identify, assess, monitor and mitigate exposures to E&S risks.

Duties and Responsibilities of the Board of Directors and Senior Management.

Board of Directors. Consistent with the expectations set out under Sec. 132 to promote the long-term financial interest of the bank and ensure that it has beneficial influence on the economy, the board of directors (or equivalent management committee in the case of foreign bank branches) shall:

- a. Institutionalize the adoption of sustainability principles, including those covering E&S risk areas in the bank, by incorporating the same in the corporate governance and risk management frameworks as well as in the bank's strategic objectives and operations taking into account the bank's risk appetite and ability to manage risk;
- b. Promote a culture that fosters environmentally and socially responsible business decisions. The board of directors shall ensure that sustainability implications are considered in the overall decision-making process;
- c. Approve the bank's ESRMS that is commensurate with the bank's size, nature, and complexity of operations and oversee its implementation. The board of directors shall ensure that the ESRMS is aligned with internationally recognized principles, standards and global practices and forms part of the enterprise-wide risk management (ERM) system;
- d. Ensure that sustainability objectives and policies are clearly communicated across the institution, and to its investors, clients, and other stakeholders;

- e. Adopt an effective organizational structure to ensure attainment and continuing relevance of the bank's sustainability objectives. The board of directors or the designated board-level or management committee shall monitor the bank's progress in attaining sustainability objectives;
- f. Ensure that adequate resources are available to attain the bank's sustainability objectives. The board of directors shall ensure that the members of the board, senior management and personnel are regularly apprised of the developments on sustainability standards and practices; and
- g. Ensure that the sustainability agenda is integrated in the bank's performance appraisal system.

Senior Management. The senior management shall be responsible for the overall implementation of the board-approved strategies and policies in relation to the sustainability objectives of the bank. It shall:

- a. Assess on a periodic basis the continuing relevance of said policies considering the developments in the business environment;
- b. Facilitate the identification, assessment, monitoring and mitigation of E&S risks. The senior management shall ensure that the bank takes a holistic approach in managing these risks aligned with the strategic objectives set by the board of directors;
- c. Assess consistency of operations and performance of personnel with the bank's sustainability objectives; and
- d. Apprise the board of directors on a regular basis on the bank's exposure to E&S risks which shall include potential issues associated with both internal and external activities of the bank and the activities of its clients that may have material impact on the bank's portfolio or reputation. Moreover, the senior management shall report its progress in implementing the bank's sustainability policies and ESRMS.

Environmental and Social Risk Management System (ESRMS). The ESRMS shall be articulated in a separate document solely relating to the management of E&S risk or embedded in existing documents related to the management of specific risk areas, (e.g., credit risk management system). At the minimum, the ESRMS shall:

- a. Define the level of risk appetite of the bank on E&S risk. The scope and complexity of the ESRMS shall be commensurate with the level of E&S risks associated with the bank's portfolio.
- b. Provide clear guidance in assessing E&S risks in the bank's operations, products and services, transactions, activities, and operating environment. The ESRMS shall also identify which sectors or activities have elevated or

emerging E&S risks or are considered to have harmful effects to the environment or society.

- c. Provide the tools for monitoring E&S risks as well as the compliance of the bank and its counterparties with sustainability-related standards, laws and regulations. The ESRMS shall likewise provide the measures that should be taken in case of breaches in limits or thresholds or non-compliance with sustainability-related standards, laws and regulations.
- d. Provide tools for assessing identified E&S risks and for considering the same in the aggregate risk exposures of the bank.
- e. Integrate E&S risks in stress testing exercises covering both short-term and long-term time horizons following the principles and requirements provided under Sec. 151. The results of stress testing shall feed into banks' capital and liquidity planning and management exercises as well as in the business continuity and disaster recovery plans.
- f. Identify the unit or personnel responsible for overseeing the management of E&S risks. The bank may establish a new unit to perform such function or integrate the same in the functions of existing risk management units. The ESRMS shall set out the duties and responsibilities of all personnel in the organization in managing E&S risks.

Internal Audit and Compliance Function. The audit and compliance functions shall incorporate in their respective programs the assessment of adherence to policies related to the management of E&S risks and evaluation of the robustness and continuing relevance of said policies. The internal audit function shall also review the bank's adherence to international sustainability standards and principles as well as relevant laws and regulations.

Disclosure Requirements. Banks shall disclose the following information in their Annual Reports:

- a) Sustainability strategic objectives and risk appetite;
- b) Overview of E&S risk management system;
- c) Products/services aligned with internationally recognized sustainability standards and practices. This shall include the issuance of green, social or sustainability bonds;
- d) Breakdown of E&S risk exposures of the bank per industry or sector;
- e) Information on existing and emerging E&S risks and their impact on the bank; and
- f) Other initiatives to promote adherence to internationally recognized sustainability standards and practices.

In addition to the above-mentioned items, banks shall also disclose in their Annual Report the progress of implementation of initiatives undertaken to integrate sustainability principles in their governance framework, risk management system, business strategy and operations.

If the foregoing disclosure requirements are captured in the Sustainability Report that is being submitted by publicly listed banks to the Securities and Exchange Commission, the Sustainability Report may be submitted together with the Annual Report to the Bangko Sentral in compliance with this requirement.

Section 2. Section 175 of the MORB on Disclosure requirements in the annual report is hereby amended to read, as follows:

Section 175 Public Disclosures

x x x

Disclosure requirements in the annual report. x x x

x x x

All banks shall prepare an annual report which shall include a discussion and/or analysis of the following minimum information in no particular order:

x x x

- f. Corporate information;
- g. x x x Sec. 174; and
- h. Information on sustainable finance as required under Sec. 153.

x x x

Section 3. Transitory Provision. Banks shall be given a period of three (3) years from the effectivity of this Circular within which to fully comply with the provisions in this Section. In this regard, banks shall adopt a transition plan with specific timelines to implement the board-approved strategies and policies integrating sustainability principles into their corporate governance and risk management frameworks as well as in their strategic objectives and operations. Banks shall provide its board-approved transition plan upon request of the BSP starting six (6) months from the effectivity of this issuance.

The foregoing provision shall be incorporated as footnote to Section 153 of the MORB.

Section 4. Effectivity. This Circular shall take effect fifteen (15) calendar days following its publication either in the Official Gazette or in a newspaper of general circulation.

FOR THE MONETARY BOARD:



BENJAMIN E. DIOKNO
Governor

29 April 2020