

STANDARD DEFINITION OF DEFAULT AND LOSS

BSP MEMORANDUM, April 15, 2005

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In connection with the data collection exercise prescribed under Circular No. 439 dated 5 July 2004, banks shall be guided by the following standard definitions of default and loss:

A. Definition of default

A default is considered to have occurred in the following cases:

1. If a credit obligation is considered non-performing under existing rules and regulations;
2. If a borrower/obligor has sought or has been placed in bankruptcy, has been found insolvent, or has ceased operations in the case of businesses;
3. If the bank sells a credit obligation at a material credit-related loss, i.e., excluding gains and losses due to interest rate movements. Banks' board-approved internal policies that govern the use of their internal rating systems must specifically define when a material credit-related loss occurs; and
4. If a credit obligation of a borrower/obligor is considered to be in default, all credit obligations of the borrower/obligor with the same bank shall also be considered to be in default.

B. Definition of Loss

Loss, for purposes of accumulating data on loss in the event of default, refers to economic loss. It must therefore include discount effects, as well as direct and indirect costs associated with collecting on the credit obligation. Banks' board-approved internal policies that govern the use of their internal rating systems must include specific policies and procedures that should be followed in the determination of economic loss.

For guidance.

Adopted: 15 April 2005

(SGD.) ALBERTO V. REYES

Officer-in-Charge

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