



Circular Letter No.:	2022-17
Date:	18 March 2022
Supplements:	CL No. 2019-39

CIRCULAR LETTER

TO : ALL EXTERNAL AUDITORS, AUDITING FIRMS AND INSURANCE COMMISSION (IC) REGULATED ENTITIES

SUBJECT : GUIDELINES ON MATERIALITY THRESHOLD

WHEREAS, the Insurance Commissioner under Section 437 of Republic Act (R.A.) No. 10607 (Amended Insurance Code) may issue such rulings, instructions, circulars, orders and decisions as may be deemed necessary to secure enforcement of R.A. No. 10607, to ensure efficient regulation of the insurance industry in accordance with global practices and to protect the insuring public;

WHEREAS, Section 6 (k), (l) and (n) of the R.A. No. 9829 (Pre-need Code) provides that the Insurance Commission (IC) have the power to:

- (k) Prepare, approve, amend or repeal rules, regulations, orders, and circulars and issue opinions and provide guidance on, and supervise compliance with, such rules, regulations, orders and circulars;
- (l) Formulate policies and recommendations on issues concerning the pre-need industry, including proposed legislations; and
- (n) Exercise such other powers as may be provided by law as well as those which may be implied from, or which are necessary or incidental to carry out the express powers granted the Commission to achieve the objectives and purposes of the law.

WHEREAS, Section 4 of Executive Order (E.O.) No. 192 series of 2015, provides authority to the IC to formulate rules, regulations to regulate the Health Maintenance Organizations (HMOs) and its related services;

WHEREAS, IC Circular Letter (CL) No. 2019-39 dated 08 August 2019 superseded IC CL No. 2009-29, stated that (Sec. 4.3.2) the accredited external auditors shall directly report to IC within fifteen (15) calendar days upon discovery of any matter adversely affecting the financial condition of the regulated entity, such as, but not limited to any findings involving fraud or error that may result to losses or potential losses the aggregate of which amounts to at least ten percent (10%) of the consolidated assets of the regulated entity is considered as material;

WHEREAS, the Bangko Sentral ng Pilipinas (BSP), under Circular No. 1040 Series of 2019, stated that actual or potential losses, the aggregate of which amounts to at least 10% of the consolidated total assets of the Bangko Sentral Supervised Financial Institutions are considered as material;

WHEREAS, the Securities and Exchange Commission (SEC), under Revised Securities Regulation Code Rule 68, had issued guidelines in relation to materiality threshold resulting from deficiency or inconsistency of information which involves transactions, amount or account that represents ten percent (10%) or more of the total of the related accounts or transactions and five percent (5%) for issuers of securities to the public;

WHEREAS, this Commission finds the need to release guidelines in determining materiality threshold consistent with the SEC;

NOW, THEREFORE, pursuant to the powers granted to the Insurance Commissioner under Section 437 of the Amended Insurance Code, Section 6 of the Pre-need Code of the Philippines, and Section 4 of E.O. No. 192, the undersigned enacts the following:

SECTION 1. APPLICABILITY

This CL shall be applied to Audited Financial Statements for the year 2022 onwards.

SECTION 2. DEFINITION OF MATERIALITY

Under Philippine Accounting Standards 1, it stated that “Information is material if omitting, misstating or obscuring it, could reasonably be expected to influence decisions that the primary users of general-purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.”

Materiality depends on the nature or magnitude of information, or both. An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole.

SECTION 3. MATERIALITY TEST

For the purpose of evaluating whether the information is material, quantitative and qualitative tests shall be applied by the external auditors and/or auditing firms:

1. Quantitative Test

- a) Deficiency or inconsistency in the disclosures of the financial statements and misstatements that may result from a deviation from prescribed policy, misrepresentation, fraud or error shall be considered material if the information involves a transaction, amount or account that represents:

- **Ten percent (10%)** or more of the total of related accounts or transactions for Insurance Commission Regulated Entities (ICRE), **non-publicly listed** and not part of a multinational company; and
 - **Five percent (5%)** or more of the total of related accounts or transactions for ICRE, **publicly listed** and/or part of a multinational company.
- b) Based on the circumstances identified by the Commission, materiality of the deficiency and misstatement in relation to the total assets or total liabilities may be considered.
- c) In resolving the issue of violation, due regard shall be given to the written explanation of the external auditor as to his basis in determining materiality and the exercise of professional judgement in issuing his audit opinion on the questioned financial statements.

2. Qualitative Test

In order to identify material misstatement or error, qualitative factors shall be considered which involve determination whether the misstatement, fraud or error:

- a) Affects the economic decisions of primary users of the financial statements;
- b) Affects the overall accuracy of the financial statements;
- c) Affects the entity's compliance with covenants under debt or similar agreements, regulatory requirements or contractual requirements of operation and other agreements;
- d) Relates to the incorrect selection or application of an accounting policy that has immaterial effect on the current period's financial statements but is likely to have a material effect on future periods' financial statements;
- e) Disguises a change in earnings or other trends, especially in the context of general economic and industry conditions;
- f) Represents a recurring misstatement that is likely to continue in future periods;
- g) Increases management compensation or creates an award that otherwise would not have been achieved;
- h) Is significant to users of the financial statements (e.g., in relation to forecast earnings);
- i) Affects key ratios monitored by analysts or other key users of the financial statements; and

SECTION 4. REPORTORIAL REQUIREMENT

The external auditor and/or audit firm shall include, applying the materiality test mentioned in this Circular Letter, any discovered material deficiencies or inconsistencies in the disclosures and material misstatements resulting from deviation from prescribed policy, misrepresentation, fraud or error in the report as required in Section 4.3 of CL No. 2019-39, to be submitted directly to the Financial Examination Group (FEG) of the IC within 15 calendar days upon discovery.

SECTION 5. REGULATORY AND SUPERVISORY ENFORCEMENT

Non-compliance of any section of this CL shall be considered as ground for suspension and/or delisting of external auditors and/or audit firms from the List of Accredited External Auditors¹.

SECTION 6. REVIEW PROVISION

This CL shall be subject to a review by the Commission at least once every five (5) years or upon any pronouncements from the International Accounting Standards Board related to concept of materiality.

SECTION 7. SEPARABILITY CLAUSE

If any provisions of this Circular shall be held unconstitutional or invalid, the other provisions not otherwise affected shall remain in full force and effect.

SECTION 8. EFFECTIVITY

This Circular shall take effect immediately.



DENNIS B. FUNA
Insurance Commissioner



¹ Suspension/Delisting of external auditors and/or audit firms shall be subject to the procedures prescribed under Section 6 of CL No. 2019-39.